Slovakia Small Business Assessment

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GEMINI

GROWTH and EQUITY through MICROENTERPRISE INVESTMENTS and INSTITUTIONS
7250 Woodmont Avenue, Suite 200, Bethesda, Maryland 20814

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Slovakia Small Business Assessment

by

Tony Barclay
Bruce Heatly

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EXECUTIVE SUMMARY

Slovakia's transition to a market economy got an initial boost from energetic privatization policies in the now-dissolved Czech and Slovak Federal Republic, but has slowed considerably in the past two years. The country is experiencing a significant economic decline. In the first half of 1993, GDP fell by 6.2 percent from the comparable 1992 figure, and industrial output declined by 15.5 percent. By August 1993 the budget deficit had risen above the target for the full year. Unemployment is expected to reach 15-16 percent in 1994.

Given the serious competitive disadvantages facing larger enterprises still owned by the state, most growth in GDP and employment must come from smaller firms under private ownership. Such firms, however, must contend with a difficult business environment. General macroeconomic conditions coupled with specific constraints in the small and medium-sized enterprise (SME) sector are inhibiting both expansion by existing firms and emergence of new ventures.

STRUCTURE AND CHARACTERISTICS OF THE SME SECTOR

Meaningful data are hard to come by in drawing generalizations about Slovakia's SME sector. A survey firm that tracks business registrations showed the following population in three broad categories, as of September 1993:

- 2,484 registered companies employing 25 to 499 people, of which 44 percent were privately owned;
- 16,743 registered companies employing fewer than 25 people, of which 77 percent were privately owned; and
- 266,292 "physical persons" licensed to do business in the general category of "craftsmen," which includes a wide range of economic pursuits.

The general picture of SMEs thus resembles an iceberg, with only the upper part visible above the water line by virtue of having obtained commercial registration. The precise size and shape of the iceberg are impossible to calculate, particularly in the informal sector, which falls below the water line. Data on economic activity by women, or among Slovakia's Romany population, which numbers 350,000, are not available, but would be essential to understanding the dynamics of the informal sector. Development strategies aimed at encouraging the private sector must address the needs of firms at both ends of the size continuum.

SUMMARY OF OPPORTUNITIES AND CONSTRAINTS

Interviews with entrepreneurs, government officials, and other informants identified two general types of constraints — indirect and direct — limiting the expansion of SMEs.

Indirect Constraints

- **Budget deficit.** Faced with declining GDP and shrinking tax revenues, the government must increasingly look to the financial sector for funds. Government debt to the banking sector, which stood at KCs 24.5 billion ($750 million) at the end of 1992, probably doubled in 1993.[1]

- **Inflation.** Inflation in 1993 was 20-25 percent, with no improvement expected in 1994. The government's efforts to control inflation through a tight money policy maintain interest rates at levels that are expensive for entrepreneurs seeking credit.

- **Liquidity.** Banks are short of loanable funds, and the commitments they do make show a consistent pattern favoring state-owned enterprises (SOEs).

- **Privatization.** The long-delayed second phase of voucher privatization has been announced for 1994, but the government is considering alternative methods, such as direct sales and auctions. Continued budgetary and bank-financed support of SOEs is a significant drain on the national budget, as production in heavy industry declines, unemployment increases, and revenue collections are reduced.

Direct Constraints

- **Credit and finance.** As a result of a tight money policy and the banking system's priorities for the allocation of available resources, private sector access to credit and investment capital is extremely limited. For the most part, firms in the SME sector, particularly start-up enterprises, are left to their own financial resources.

- **Business taxes.** The existing system encourages businesses to remain small to minimize corporate taxes, to avoid creating permanent jobs to escape payment of social taxes, and to seek loopholes in the law and engage in other tax-avoidance strategies.

- **Legislation and regulations.** Lack of comprehensive legislation restricts the establishment of new enterprises. For the SME sector, Slovakia's commercial law framework may be characterized as inconsistent and incomplete. What corrective action is being taken tends to be incremental.

PRINCIPAL INSTITUTIONS AND ACTORS IN THE SME SECTOR

Government

Early in 1993, the government created a free-standing, specialized agency with national coverage, the National Agency for Small and Medium Enterprise Development. An important feature of the new agency's structure is the inclusion of private sector representatives on its board of directors, along with

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[1] KCs refer to the currency of the Czech and Slovak Federal Republic. On February 8, 1993, the Slovak crown (Sk) became the currency of Slovakia.

ministerial appointees. The agency is well positioned to be a catalyst for change, and the inclusion of private sector interests in its governance structure is an encouraging sign.

Banking Sector

The newly commercialized state-controlled banks continue to hold the debt of large enterprises, many of them technically bankrupt, and these banks have a dominant share of the market. The Slovak-American Enterprise Fund (SAEF), created with support from the U.S. Agency for International Development (USAID), has a portfolio consisting exclusively of investments within the Slovak Republic. The State Agricultural Bank acts as an intermediary bank for a facility sponsored by SAEF, popularly known as the "American Loans Program." To date, eight loans have been approved for a total of Sk 20 million. The Slovak Guarantee Bank provides guarantees for SME lending up to Sk 500,000 ($15,000), but this facility has had only 15 percent usage. Its sponsor, the European Community's PHARE program, intends to redesign the program.

Donor-Assisted Programs

Business Service Centers offer business planning assistance, which is generally linked to the client's application for loan finance from a bank. MBA Enterprise Corps volunteers have staffed an Entrepreneurship Center in Bratislava and are opening new centers in other cities. The National Agency for Small and Medium Enterprise Development is establishing a two-tiered network comprising eight Regional Consulting and Information Centers and four Business Innovation Centers. On-Site Volunteer Programs rely on the presence of a volunteer who is formally sponsored by the firm's management. Both the International Executive Service Corps and MBA Enterprise Corps participate actively in these programs.

In assessing the impact on the SME sector, these firm-level interventions can be characterized as follows:

- The volunteer-staffed programs are responding to demand from firms with widely recognized and well-documented needs in Slovakia's newly emerging private sector.
- Client entrepreneurs typically have a wide assortment of problems, but limit their dealings with the consultants to a single "product," the business plan.
- At their present scale, these programs reach a small number of clients, who tend to be concentrated toward the upper end of the SME size range.
- The impact of these programs on client firms is hard to measure, beyond the rate of subsequent success or failure in obtaining finance.
- In their present form and size, it is not feasible for these programs to cover their costs.

Membership-Based Organizations

The largest voluntary association in the private sector is the Entrepreneur Association of Slovakia, which claims 19,000 members. The association is at a relatively early stage of organizational development. Its annual national membership dues are nominal (Sk 50, or $1.50), although several local (county) chapters levy additional charges to support branch offices. The density of coverage and strength of local chapters vary considerably. Several other voluntary business groups have been formed in the past two years, of which some are formally affiliated with the Entrepreneur Association.

The National Chamber of Commerce and Industry is a statutory body that all registered companies are legally required to join. Annual dues are high (Sk 8,000) and services are geared mainly to the interests of state-owned companies. There are no tailored services for SME firms that belong to the Chamber.

IMPLICATIONS FOR USAID ASSISTANCE STRATEGY

In the current context, USAID might usefully support three interdependent activities. These activities could be managed through a single small business policy project, to be based at the National Agency for Small and Medium Enterprise Development. USAID could:

- *Collaborate with the National Agency in the elaboration of government's umbrella policy* for the sector, and the preparation of new legislation, starting with the proposed Small Business Act. USAID assistance should aim at building the agency's capacity to analyze the full spectrum of policy issues (such as regulatory, financial, and fiscal issues) affecting SMEs.

- *Provide organizational development assistance to business associations and other voluntary bodies* with significant membership from the private sector. This assistance could be organized by the National Agency, which should have a clear mandate to reach out to all bona fide organizations with significant membership potential, whether regional-, national-, or industry-based.

- *Assist the agency or another organization with surveys and analytical support to develop better information* on the structure, composition, and dynamics of Slovakia's SME sector. This activity would help to identify economic subsectors with significant growth potential, and it would also examine the needs of household microenterprises and informal sector firms, whose role in the economy is not well understood.

Principal guidelines for the proposed project would include:

- *Duration.* The initial period of the project would be 15-18 months.

- *Long-term technical assistance.* An advisor, based at the National Agency and operating in a general advisory capacity, would serve as the anchor for project activity.

- *Flexible use of short-term technical assistance.* A component for U.S. short-term technical assistance should be included, to provide the ability to respond to demand under all three activity areas.

- *Involvement of Slovak professionals.* An effective project will depend on close teamwork between U.S. and Slovak professionals.

- *Training and internships.* U.S.-based short-term training and internships with a practical orientation should be built into the project, with eligibility for both National Agency staff and leaders of business associations.

- *Collaboration with Peace Corps.* The Peace Corps has a small business program with new volunteers strategically placed in locations all over Slovakia.

- *Networking and information exchange.* Such exchange should be used to promote dialogue with institutions in other countries concerned with SME development.

BACKGROUND

In its previous status as part of the Czech and Slovak Federal Republic, Slovakia shared in the fast-paced changes that followed the 1989 Velvet Revolution. Building on political reforms that were quickly introduced during the following year, Czechoslovakia took measures to start the transition toward a market economy. By 1992, the country had the lowest rate of inflation in Central and Eastern Europe, and maintained a large surplus in its balance of payments. The privatization program, which got off the ground in 1991, played a significant role in accelerating the economic transition. Within Slovakia, during this initial phase, 90 percent of small businesses changed ownership through restitution or sale by auction.[1] An additional 500 companies were sold through the voucher system. As of mid-1993, the private sector's share of industrial production in Slovakia had reached 20.3 percent, and 86 percent of retail trade had been privatized.

Sharp contrasts were evident in the industrial and economic structure of the two republics during the early phase of the transition. In the communist era, Slovakia's industrial base was centered on heavy weaponry and military equipment destined for markets in the Soviet Union and its client states. These markets have virtually disappeared, and the low-end technologies and equipment in those industries are not easily adapted to other uses. By comparison, industries in what is now the Czech Republic were geared to producing a more diversified range of finished products with more advanced technologies, which has made conversion to civilian uses considerably easier. Thus the policy decisions and implementation methods selected by leaders in the two republics reflected different economic and political scenarios.

When the federation dissolved, leading to Slovak independence on January 1, 1993, the transition from a state-directed to a market-based economy had begun to slow down. The new republic's economic performance has continued to lag behind that of its immediate neighbors. Entering its second year of independence, the country is experiencing a significant economic decline. In the first half of 1993, GDP fell by 6.2 percent over the comparable 1992 figure, and industrial output declined by 15.5 percent. By August 1993 the budget deficit had exceeded the total planned for the entire year under guidelines adopted by government and the International Monetary Fund. Unemployment is expected to reach 15-16 percent in 1994.

Given the serious competitive disadvantages facing larger enterprises still owned by the state (many of these commercialized as joint-stock companies, but with government the dominant shareholder), it is widely recognized that most growth in GDP and employment must come from smaller firms under private ownership. Such firms, however, must contend with a difficult business environment. General macroeconomic conditions, coupled with the specific constraints of scarce credit, frequently changing laws and regulations, and excessive social taxation, are inhibiting both expansion by existing firms and the emergence of new ventures.

In official policy statements, the Government of Slovakia has affirmed the need for ongoing reforms and has committed itself to resume the privatization program in 1994. It has also taken some steps to recognize the importance of small and medium-sized enterprises (SMEs), most notably the establishment in 1993 of an independent foundation, the National Agency for SME Development. As yet, however, there is no comprehensive policy statement that demonstrates high-level support for SMEs. Without such a policy framework, many specific measures that would help create a positive atmosphere

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[1] See the discussion below for the most common definition of "small business" in the Slovak context.

for private sector development cannot be undertaken. The fact that the National Agency holds responsibility for formulating this policy is a key factor in the analysis and recommendations that appear in this report.

STRUCTURE AND CHARACTERISTICS OF THE SME SECTOR

Prior to 1990, private entrepreneurship in Slovakia, while not unknown, existed on a small scale in informal (sometimes illegal) trading activities, or in selected occupations sanctioned by Communist Party authorities. The latter situation is exemplified by a leather craftsman whose products won prizes at several international trade shows in the 1980s, and benefited thereafter from benign neglect by party leaders in his home town; the party leaders enjoyed the favorable publicity he had gained.

Such situations were uncommon, however. For the most part, trading activity was restricted either to the strictly illegal black market, or to gray market transactions where party officials often took a cut from the proceeds. Manufacturing was effectively monopolized by the state, and the services industry was poorly developed. The absence of markets and the very real threat of punitive action by the state acted to restrict both the formation of capital and the creation of jobs in privately held businesses.

With the collapse of the communist system, many of the most obvious barriers to entrepreneurship were dismantled. A small number of dynamic individuals were able to move quickly when this happened. Some resigned from positions in state-run companies or scientific institutes, and established new firms that could use their technical skills. Others, who were already engaged in commerce on the margins of the command economy, were able to expand their operations in retail trade, opening new stores and emulating the behavior of consumer-oriented businesses in the west.

These first-wave entrepreneurs were well positioned, and were prepared to take risks when the barriers came down. They are not typical, however, of the small business population at large. Meaningful data are hard to come by when one seeks to draw generalizations about Slovakia's private sector. In an early interview, one informant told the assessment team that there were more than 300,000 private entrepreneurs in the country, almost all of them operating small or medium-sized firms. On the surface, at least, this figure has some basis in commercial statistics, which indicate the following numbers in three broad categories, as of September 1993:[2]

- 2,484 registered companies employing 25 to 499 people, of which 44 percent were privately owned;
- 16,743 registered companies employing fewer than 25 people, of which 77 percent were privately owned; and
- 266,292 "physical persons" licensed to do business in the general category of "craftsmen," including a wide range of economic pursuits.

These statistics were collected and analyzed by a Slovak consulting firm, TERNO, which tracks the numbers and classifications of firms holding business licenses, and prepares quarterly reports on a contract basis for the Ministry of Economy. TERNO itself is a spinoff from a government research institute, having been purchased and taken private by its two principals in 1991. They provide a broad, three-tiered framework that is useful for descriptive purposes.

Although TERNO's tracking reports partially illuminate the formation of private enterprise, they do not reflect the actual condition of the businesses that are listed. The reports are based on the list of

[2] These figures, and those that follow, are taken from a TERNO report produced in November 1993, and cited in Annex B.

firms that have completed requisite government paperwork, whether or not they are actually operating. Thus, in characterizing the SME sector, these statistics are likely to err on the high side by (1) not excluding businesses that fail, particularly sole proprietorships ("physical persons"); and (2) lumping full-time economic activity together with seasonal activity, when the latter is not the principal source of income for the person(s) involved. On the other hand, there is no assurance that the physical person category captures all types of activity in the informal sector, particularly trading activities in which women tend to play a major role. Data on economic activity by the Romany population, numbering perhaps 350,000, are likely to be even less reliable, given their marginal and mobile status in Slovak society.

With these caveats, it is nonetheless possible to spot some interesting trends in the data. Most striking is the rapid growth in the first and second categories (registered firms) during the 21 months between December 1991 and September 1993, the last period for which figures were available. As shown in Figure 1, small firms (those with fewer than 25 employees) nearly quadrupled in this interval, with almost all of the growth occurring in privately owned firms or the "other ownership" category, which includes joint ventures with foreign investors. An almost identical growth pattern occurred among midsized firms, and here the number of state-owned enterprises (SOEs) fell by more than half while the total number of midsized companies almost doubled. By comparison, the physical person/craftsman category grew by 30 percent from a base of about 200,000 in December 1991 (Figure 2).

The TERNO surveys also provide a breakdown into several general industry categories, including processing; building and construction; trade; hotels and restaurants; transportation, communications, and wholesaling; and a general category for services including data processing, research and development, and other commercial activity. Despite some inconsistencies in the data set, the rate of 1991-1993 growth (measured in number of enterprises) was fairly even across all categories for the small-firm group; for midsized firms, the same was true except that the number of service firms declined slightly. The biggest growth among physical persons/sole proprietors occurred in processing, which quadrupled from 12,589 to 52,863; and trade, which doubled from 35,158 to 75,170.

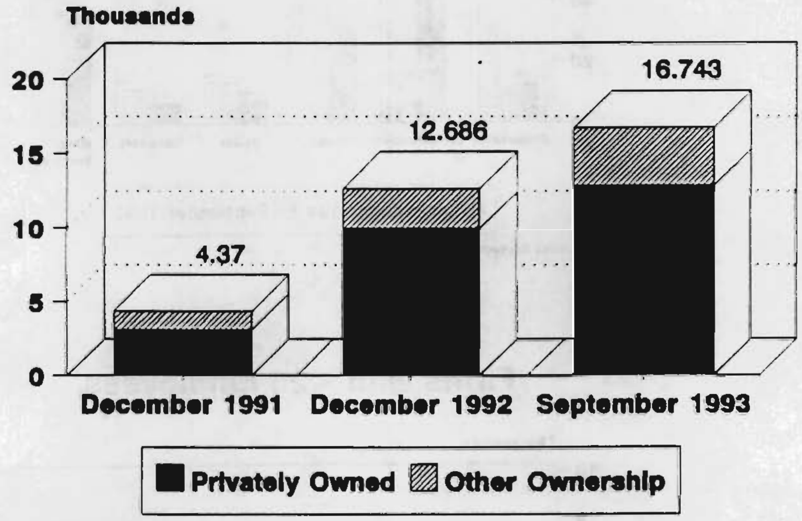
The general picture of SMEs resembles an iceberg, with only the upper part visible above the water line by virtue of having obtained commercial registration. As noted above, the three main categories mask some important variables, and while they appear to capture new entrants, they make no explicit provision for delisting companies that have ceased operations. In this respect, the precise size and shape of the iceberg are impossible to calculate, particularly in the informal sector, which falls below the water line, where accurate data collection tends to be very difficult.

These information gaps have important implications for this assessment of the SME sector, and for potential followup actions. First, they serve as a reminder that business leaders who successfully rode the first wave of opportunities after 1989 represent just a small fraction of the business population. Second, because of these gaps, questions about the viability and growth potential of small firms that have made their way onto the commercial register, but are struggling to survive in the present economic circumstances remain to be answered. Third, the gaps in understanding underscore the fact that tens of thousands of microenterprises have emerged in Slovakia based on the initiative of individuals, but with little or no formal business experience. What factors contributed to this emergence, and what factors constrain further development?

Development strategies aimed at encouraging the private sector must address the needs of firms at both ends of the size continuum. The nature of this assessment ruled out in-depth investigation of the issues affecting microenterprises, specifically factors relating to gender or ethnic status. Because the data on these issues are limited, the policy implications for smaller-scale enterprises are not yet apparent. Improving the information base through carefully designed and managed surveys is one of the principal recommendations put forward in Section Five of this report.

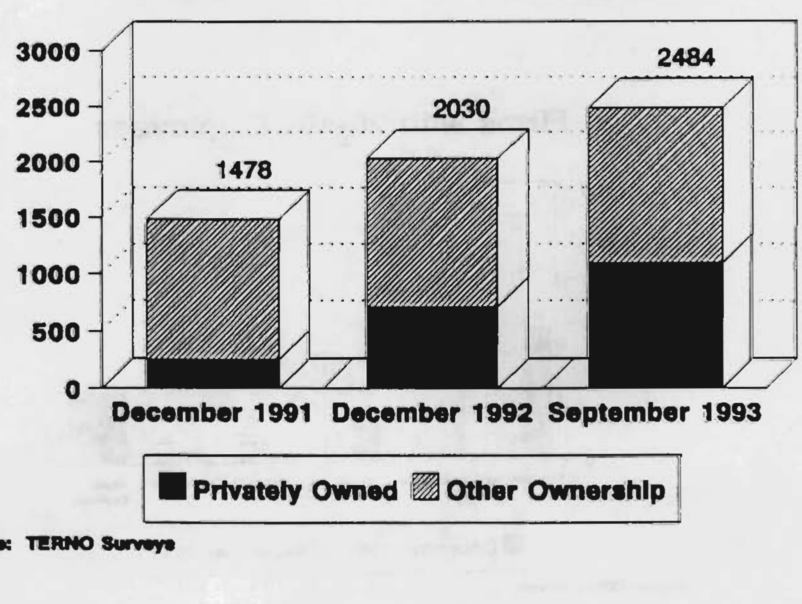
FIGURE 1
GROWTH OF FIRMS

GROWTH OF SMALL FIRMS
Registered Cos. with <25 Employees



Source: TERNO Surveys

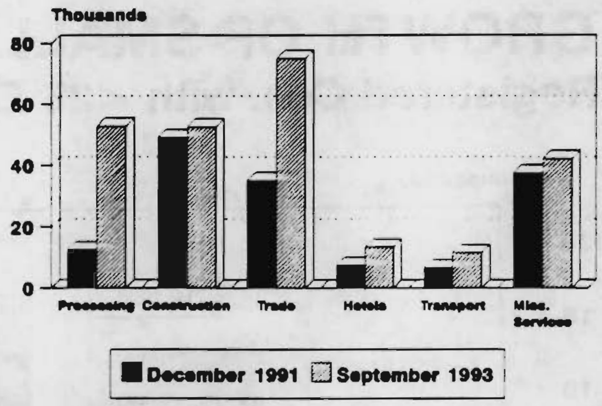
GROWTH OF MIDSIZED FIRMS
Registered Cos. with 25-499 Employees



Source: TERNO Surveys

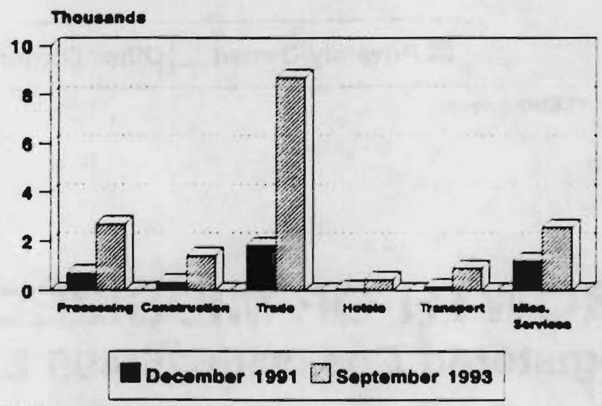
FIGURE 2
INDUSTRY BREAKDOWN

"Physical Persons" Category



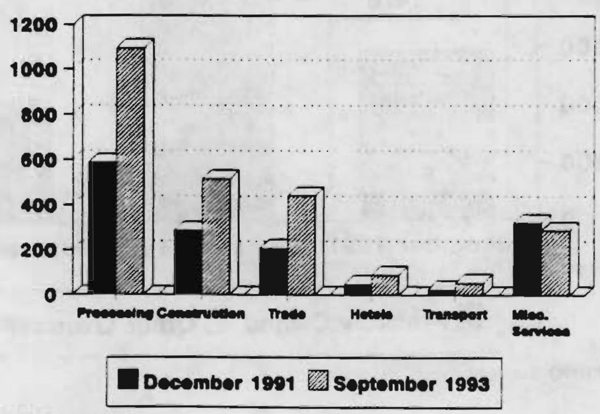
Source: TERNO Surveys

Firms with <25 Employees



Source: TERNO Surveys

Firms with 25-499 Employees



Source: TERNO Surveys

SUMMARY OF OPPORTUNITIES AND CONSTRAINTS

OVERVIEW

In spite of the opportunities provided by the law on entrepreneurship, which was enacted by the Federal Parliament in 1990, private enterprise has not developed as rapidly as it has in neighboring Central European countries. Based on 1993 estimates, the private sector's contribution to GDP in Slovakia was less than 25 percent, compared with Poland, where it accounted for more than 50 percent of both GDP and employment.

Numerous factors inhibit the growth of private enterprise in Slovakia. Many of them, such as the absence of an entrepreneurial tradition, scarcity of management skills and experience, insufficient capital and credit resources, and a prolonged recession in Western Europe, have direct impact at both the sectoral and firm levels. Other indirect but powerful constraints result from the government's policy initiatives to stabilize an economy that is undergoing severe stress. The difficulty of transforming the industrial base from production of heavy armaments to other uses is reflected in rising unemployment and falling export revenues. The task of economic management has been further complicated by the breakup of the former Federal Republic, which required the creation of new institutions on a national scale, including a Central Bank.

Although recognizing this broad spectrum of constraints, this analysis will focus on issues that affect the SME sector specifically. The analysis will examine opportunities to inject new forms of assistance, with support from USAID, that would complement, but not duplicate, programs and projects already in place. The assessment team found that there are numerous firm-level programs under way that are designed to assist entrepreneurs in improving management, financial, and technical skills. However, no donor-assisted programs are addressing the systemic, sector-wide, questions that determine whether Slovakia offers an enabling environment for new and expanding SMEs.

A critical missing element in the business environment is a comprehensive government policy statement that explicitly recognizes the role of private enterprise in a free market economy. Equally important is the limited capability of the private sector business community to attack the systemic constraints that inhibit SME growth. Business associations have begun to emerge at the national, regional, and municipal levels, but they are not yet equipped to formulate and successfully advocate policy changes that would improve the environment in which their members operate.

The analysis begins with a brief summary of the major points raised by Slovak entrepreneurs in meetings with the assessment team. Although the sample was small, given the limited time frame, the pattern of comments and concerns was consistent across interviews with business people in different industries and with different scales of operation.

THE ENTREPRENEUR'S VIEWPOINT: A SNAPSHOT

The team interviewed individual entrepreneurs who were operating in the capital city of Bratislava and in two regional centers, Galanta and Banska Bystrica. The same concerns were expressed by both demonstrably successful businessmen and by others who were apparently less well equipped to solve problems restricting their business activities.

In the first instance, a joint meeting was held with four entrepreneurs, the most successful of whom owned a department store, a supermarket, a restaurant, and an inn. Three of the four had been in business prior to the 1989 revolution; one had begun operations in 1980. Two had managed to obtain bank financing in the early 1990s, but no longer borrowed because of high interest rates (quoted at 25 percent) and limited availability of credit, even at banks where they were well known. Without access to reasonably priced credit, the supermarket owner had decided to discontinue a planned warehouse club operation. To factor in the cost of capital at 25 percent would have prevented him from offering heavily discounted merchandise, which is the primary feature of a warehouse club.

Another of the four businessmen also owned a department store, and had previously carried its inventory with bank credit. Although he claimed to have a good credit history, his bank no longer had funds available to loan to him. With all his capital thus tied up in inventory, he was prevented from expanding his business.

The introduction of a value-added tax (VAT) in 1993 had a dampening effect on sales, particularly for the retailers. When this replaced a highly unpopular turnover tax, it squeezed their pricing, because they could not pass on the entire tax burden to their customers.[3] Another tax issue concerned the burden of social taxes, for which the combined employer and employee contribution rates represent 50 percent of gross wages. The retailers were of the opinion that, in the current economy, the best way to maximize profitability is to decrease overhead by cutting staff — a process that they acknowledge merely exacerbates unemployment. The four were equally critical of the government's delay in completing the privatization program. They complained about the effects of subsidized competition from state-owned firms, noting that many such enterprises did not meet their tax obligations, were undependable as suppliers, and tended to be extremely slow in paying for the goods and services they purchase from the private sector.

This group provided an excellent example of how entrepreneurial talent can be diverted from its potentially valuable role in helping to steer the economy through the transition. Instead of leading by the example of innovation and dynamism, they must devote most of their time and energy to maneuvering around constraints in a generally unfavorable environment.

The assessment team also interviewed a company below the midpoint in size on the SME spectrum. This company was struggling with similar constraints on a smaller scale, with fewer resources in hand. Its primary business is the installation of electrical equipment and of residential and industrial cable television, and the production of small electrical components used in the installation process. The company, which has been operating for three years, is staffed by six partners, who previously worked together in an SOE, and four employees.

This company's primary concern is the lack of funds to expand the production of electrical parts. The personal savings of the partners provided start-up capital. With a reasonable customer base (numbering several thousand cable TV subscribers) but low monthly fees, they have been unable to accumulate sufficient capital internally, and have been unsuccessful in obtaining bank credit for lack of sufficient collateral. They are thus stymied in their efforts to expand.

The partners blamed the tax structure for their inability to accumulate capital for expansion. As owner-employees, they feel they are being treated unfairly in the sense that gross profits they generate

[3] The initial tax rate was 23 percent on finished goods and 5 percent on foodstuffs, but these rates were raised to 25 and 6 percent in the middle of the year, a step which caused further aggravation to the group in this interview session.

are taxed as company income, and subsequently as personal income tax. They shared the view that the social security tax burden for a private firm like their was particularly onerous, because state-owned firms were not assessed at a lower rate, but were usually delinquent in paying social taxes.

There was a noticeable difference in the level of sophistication and business know-how between the entrepreneurs whose experience began before the 1989 revolution, as described above, and the owners of the cable installation company. The former understand the system, and appear to know how to work their way through it, while the latter gave the impression that the problems were known, but solutions were beyond their grasp. Nevertheless, in spite of the differences among the entrepreneurs interviewed, they confirm that all face common constraints. Those constraints can be classified as indirect (deriving primarily from macroeconomic factors) and direct (having an immediate impact on the performance of individual firms).

Indirect Constraints

Budget Deficit

A key factor determining government economic policy is the need to finance a budget deficit resulting from declining revenues and rising government expenditures. The deficit reached Sk 17.5 billion by August 1993, versus a planned deficit of Sk 16 billion for the entire year.[4] In the face of declining GDP and shrinking tax revenues, the government must increasingly look to the financial sector for funds, thus draining the banks of resources that might otherwise be allocated to private borrowers. Government debt to the banking sector, which stood at KCs 24.5 billion at the end of 1992, is estimated to have doubled by the end of 1993.

Inflation

The government has been moderately successful in controlling inflation. Although the official figure for 1993 was approximately 15 percent, a more realistic figure is probably in the range of 20-25 percent, with no improvement expected in 1994. Efforts to control inflation through a tight money policy, however, have the effect of maintaining interest rates at levels expensive for entrepreneurs when seeking credit for working capital or expansion purposes.

Liquidity

A tight money policy and extensive use of financial sector resources to cover the deficit have produced a credit crunch in the banking sector. Although there is general agreement that the banks really are short of loanable funds, the commitments they do make show a consistent pattern favoring SOEs. It is difficult to assess the degree to which any bank is free to set its own lending policies; the financial system is dominated by banks that, though converted to joint stock companies, are still owned by the government through the National Property Fund.

A representative of one of Slovakia's largest banks, itself a spin-off of a state-owned bank, cited two troubled loans that account for approximately 30 percent of the bank's assets. These were inherited

[4] U.S. $1.00 = 33 Slovak crowns (Sk) as of January 1994.

from the bank's predecessor. One is a housing loan that carries an interest rate of 1 percent. Although the bank's spokesman expressed confidence that both loans would eventually be liquidated, there is no doubt that they should now be considered as nonperforming, because they generate no income and are in danger of ultimate failure. Such situations are far from unique in the SOE banking sector, and until they are resolved, there is little likelihood that the liquidity situation will improve.

Privatization

Although not strictly a macroeconomic issue, the pace of privatization of SOEs influences the speed of the transition to a market economy. There has been virtually no movement on the privatization front since the completion of the first wave of transactions in 1991-1992. A second phase of voucher privatization has been announced for 1994, but the government is considering alternative methods, including such traditional procedures as direct sales and auctions. This posture appears to be motivated by the expectation that foreign investors will bid up the prices of companies that are offered for sale, increasing revenues to the government. This is not altogether realistic, however, given the general state of the economy and the relative absence of potential investors showing interest in most of the SOEs slated for divestiture.

Disposition of the SOEs has become both an economic and a political issue. There is no question that continued budgetary and bank-financed support of SOEs is a significant drain on the national budget as production in heavy industry declines, unemployment increases, and revenue collections are reduced. As a political issue the slow pace of privatization has been criticized by all sides. The lack of a coherent program is evidenced by the fact that there has been no Minister of Privatization since the previous incumbent was dismissed in mid-1993. Of particular concern to the private sector is the Ministry of Privatization's position as supervisor of the National Property Fund, which holds a controlling interest in SOEs that have been converted to joint stock companies.

To further complicate the issue there is a common perception, particularly among private sector entrepreneurs, that the financial condition of SOEs is being allowed to deteriorate to the point where they will be sold off to insiders at a nominal cost. New and inexperienced owner/managers will have neither the resources nor the capacity to revive these companies, and the expectation is that many will ultimately fail.

Interviews by the team confirmed a widely held view among private entrepreneurs that a resumption of privatization, indeed a rapid acceleration of that process, is critical to the country's economic recovery. So long as three quarters of the economy remains under state control, with declining productivity and a high level of subsidization from the national budget and the banking sector, opportunities for expansion in the private sector will be severely constrained. The existing market structure forces many private firms to rely on state-owned or -controlled companies as their principal suppliers or customers. The weak financial condition of these suppliers and customers exposes the smaller enterprises to an increasing level of risk, and their preemptive claim on credit resources from the banking sector shrinks the amount of capital that could be made available for commercial lending. Midsized private firms are also disadvantaged in competing for customers with SOEs whose aggressive pricing policies are not restricted by the need to earn a profit.

The course of action the government must take to relieve macroeconomic constraints will entail significant legislative activity. However, government policy choices are restricted by the guidelines established under the country's stabilization agreement with the International Monetary Fund. The key component of these guidelines is the commitment to cut the budget deficit to 5 percent of GDP (Sk 16 billion), combined with a sharp reduction in the balance-of-payments deficit. The ability of the current government to meet these guidelines is problematic. The governing party does not hold a majority of the seats in Parliament, nor does it have a workable coalition. Any issues with political significance can only be acted on by securing the support of one or more of the opposition parties. This can be difficult if the actions to be taken are likely to intensify competition for voter support.

Direct Constraints

Although the entrepreneurs we interviewed appreciated the impact of macroeconomic factors, they were particularly interested in specific constraints to their day-to-day operations. They were almost unanimous in focusing on credit, taxes, and legislation.

Credit and Finance

As a result of a tight money policy and the banking system's priorities for the allocation of available resources, private sector access to credit and investment capital is extremely limited. Bankers interviewed report that assistance to SMEs plays an important part in their strategic planning for the future, but insufficient liquidity prohibits implementation of these programs. Further discussion, however, indicates that available resources are directed toward SOEs, many of which cannot repay existing debt and would undoubtedly fail if called upon to do so. At the end of 1992 Slovak banks reported questionable loans of only 3.2 per cent and loans temporarily in arrears at 11.3 per cent of loans outstanding. It is highly unlikely that this is an accurate assessment of portfolio status but, rather, demonstrates bankers' reluctance to admit to the gravity of their problems. Restructuring debt as it comes due avoids the issue of nonpayment, and postpones the time when the banks must reckon with the true financial position of both their borrowing clients and their own institutions.

An additional factor limiting SME access to credit is the banks' lack of experience in private sector lending. For 40 years, the primary function of these institutions was to respond to central government instructions to fund SOEs. SMEs operated on a highly restricted basis — usually in situations where local party leaders chose to look the other way — and had no commercial banking relationships. Today, with a growing source of demand for credit from emerging firms, there is no institutional expertise within the banks to work in this specialized field of lending. In an effort to compensate for this weakness, those banks that have money available seek to minimize risk by requiring collateral equal to 130-150 percent of the amount of the credit.

Postrevolution entrepreneurs state categorically that the banking sector is incapable of or unwilling to meet the credit needs of the SME sector. They maintain that only those with the proper connections are in a position to secure credit, and, in most such situations, the viability of the borrower's business activities may not be an issue.

Interviews with entrepreneurs, bankers, and government officials invariably cited the USAID-funded Slovak-American Enterprise Fund (SAEF) as the only source of credit and equity investment for entrepreneurs. This program is discussed below, but it is notable that less than 20 percent of SAEF's portfolio is committed to SME lending, and only a handful of loans have been made through its specialized credit window, at an average value exceeding $40,000. SAEF concentrates its resources on larger deals, including equity investments, and this is where it has achieved its largest impact in Slovakia's embryonic capital market.

To encourage higher-risk lending, the government established the Slovak Guarantee Bank (Slovenska Zarucna Banka or SZB) in September 1991. SZB's major efforts are directed to projects associated with the large privatization program, as well as support for the government's economic revival programs. The bank does not provide funding for credits, but under certain conditions it does make a contribution to project interest payments. In effect, this subsidizes the cost of borrowing. It is difficult to assess the effectiveness of SZB's activity without in-depth analysis, but it is safe to assume that the primary focus is on government projects that require government-guaranteed and -subsidized financing. Budgetary limitations prevent direct government support, but using the banking system to achieve the desired goal creates a contingent rather than a direct government liability.

For the most part the SME sector, particularly start-up entrepreneurs, is left to its own financial resources. New businesses must depend on personal savings or borrowing from friends and family members. Existing businesses, for the most part, must look to the same sources or use accumulated profits for further expansion. Several currently successful entrepreneurs interviewed by the team appear to have operated during the prerevolution market and managed to develop rapidly as the transition to a market economy got under way. The source of their capital is not easily identified.

Business Taxes

Though most entrepreneurs, particularly those short of working and investment capital, were concerned by the lack of access to credit, there was unanimous agreement that taxes are a major constraint to development and expansion. Entrepreneurs are subject to many different taxes and the rates tend to be high.

- Social taxes, whose cost equals 50 percent of gross wages, are primarily a social security contribution, with a small part representing a wage tax. Entrepreneurs complain that in spite of the size of the tax, workers receive very little in return. To obviate this tax burden, businesses routinely hire contract workers who pay their own (lower) social taxes, on the basis of being self-employed.

- Value-added taxes, which replaced a system of turnover taxes on registered companies, whose rate was sector-dependent but had reached as high as 29 percent. VAT was introduced at the beginning of 1993, with a dual rate structure for goods/services and basic foodstuffs, and the rates were adjusted upwards in July. This move was cited by entrepreneurs as an example of the unexpected changes in regulations that significantly affect business operations.

- Corporate income taxes are levied at a maximum rate of 45 percent on profits after allowable expenses, including depreciation, wages, inputs, interest, and owner's salary.

Entrepreneurs maintain that rationalization of the tax system would, in the long term, increase revenues to the state treasury. The existing system encourages businesses to remain small to minimize corporate taxes, to avoid creating permanent jobs to escape payment of social taxes, and to seek loopholes in the law and engage in other tax-avoidance strategies.

Current regulations also discourage unregistered gray market entrepreneurs from entering the official business community, which would generate increased tax revenues. Registered entrepreneurs are particularly resentful of the competition not only from firms that operate outside the tax system, but also from SOEs that reportedly owe billions of crowns in unpaid social taxes.

Legislation and Regulations

The sheer volume of legislation and regulations affecting private sector business operations is also a major concern for entrepreneurs. One entrepreneur cited a newspaper report stating that approximately 1,200 legislative changes had been effected since the transition to a market economy began.

Lack of comprehensive legislation restricts the establishment of new enterprises. Government officials appear to act on the theory that if there is no legal authorization to operate a specific type of business, particularly in the financial sector, then such activity must be deemed illegal. The lack of legislation allowing the creation of a private sector insurance company is a prime example of such barriers to entry.

The problem of meeting the high collateral demands of the banks is compounded by the provision that prohibits the use of personal property as collateral. Clearly this obstacle requires correction. Implementation of a new bankruptcy law has been delayed several times for fear of a possible domino effect. Although this concern is understandable, it serves to delay the inevitable, and endangers the stability of creditors who cannot anticipate settlement of debts.

For the SME sector, Slovakia's commercial law framework may be characterized as inconsistent and incomplete. What corrective action is being taken tends to be incremental. The confusion created by this situation prompted entrepreneurs to say that clear and timely information on laws and regulations is critical to their operations. They would like to see plain legal language with maximum notice prior to changes, as well as some analysis of how new laws and regulations, especially relating to taxes, would affect their businesses.

According to entrepreneurs, finance, taxes, and legislative issues represent the major direct constraints to further private sector development. Lack of accessible credit inhibits growth and job creation, as do costly social taxes. Frequent and confusing legislative and regulatory changes make long-range business planning ineffective. These issues, together with the implications of an economy where GDP continues to decline, and of a minority government that will find it politically difficult to effect major changes, present a difficult challenge for even the most aggressive entrepreneur.

PRINCIPAL INSTITUTIONS AND ACTORS IN THE SME SECTOR

GOVERNMENT AGENCIES

Since the revolution of 1989, the Ministry of Economy has had lead responsibility within the government for development of the entrepreneurial sector in Slovakia. Originally, the ministry directly managed a diverse group of activities specifically targeted at industry groups. Its departmental staff for these functions numbered only four, and coordination of these programs proved difficult. Since 1991, the ministry has been receiving technical assistance and financial contributions from the European Community's EC-PHARE facility, starting with a commitment of ECU 7.2 million in 1991.

Initial governmental efforts to frame policies supportive of private sector development placed a heavy emphasis on subsidized loan programs directed toward specific industries. In 1992-1993, more than KCs 200 million ($6 million) was disbursed in two such programs managed by the Slovak Guarantee Bank, in which the government absorbed between 50 and 75 percent of interest charges on eligible loans.[5] One program targeted manufacturing firms with high domestic raw material content, while the other was aimed at companies demonstrating high efficiency in energy use. Many firms benefiting from these loans appear to have been joint-stock manufacturing companies controlled by the National Property Fund. With limited staff and resources, the Guarantee Bank did not actively seek out startups or very small firms, and the targeting excluded service firms and trading enterprises.

Early in 1993, the government moved to create a free-standing, specialized agency that would have a larger staff and national coverage. The new organization was legally established as a foundation, which would receive partial support under the national budget and continued funding from EC-PHARE. The National Agency for Small and Medium Enterprise Development (Narodna Agentura pre Rozvoj Maleho a Stredneho Podnikania) began operations in September 1993. It has assumed most of the operational functions previously situated in the ministry, although it does not have independent authority to set policy or formulate legislation.

An important feature of the new agency's structure is the inclusion of private sector representatives on its board of directors, along with ministerial appointees. Of 13 members, two come from the Entrepreneur Association of Slovakia, one from the Council of Small and Medium Entrepreneurs, and one from the Slovak Chamber of Commerce and Industry. The Slovak Guarantee Bank and Slovak Savings Bank are also represented, along with other government entities.

Consultation at the board level has helped to initiate a process of policy dialogue between the government and the private sector. The National Agency convened several roundtable sessions in September 1993, at the time it began operations, and invited spokespersons from a wide range of organizations to discuss its objectives and to comment on issues affecting the SME sector. In this process, two expert groups were formed, one to provide input to a proposed new Small Business Act, and the other to examine problems concerning taxation and access to financial services.

Before the National Agency became operational, work had begun on a statement of principles for the proposed Small Business Act, which will eventually be submitted to the Slovak Parliament. The department head in the Ministry of Economy has been steering this process, and since September has interacted with the expert group on legislation. After receiving critical comments on a first draft from

[5] The guarantee program is described below.

the Legislative Council, which is the body charged with introducing new legislation to Parliament, the team revised the document and is now awaiting the go-ahead to proceed with drafting of formal legislation.

As new legislation is prepared, a potentially useful resource within the Slovak Government is the Anti-Monopoly Office, which is charged with facilitating the entry of new firms into markets previously controlled or dominated by SOEs. Its functions resemble those of the U.S. Federal Trade Commission, and its staff have received training from commercial law experts financed by USAID.[6] To date, the office has not played a formal role in policy making for the SME sector, but its potential contribution should not be overlooked.

Admittedly, dialogue between the public and private sectors is in its very early stages. Communication channels are dependent on personal relationships and initiative, because policy analysis and action planning capabilities for the relevant issues are not well developed on either side. Formal mechanisms for negotiation and compromise have also not yet been tested. But the agency's organizational design legitimizes private entrepreneurs as stakeholders in the policies and legislation adopted by government, and provides a platform on which dialogue and collaboration can be conducted in the future.

Operationally, the National Agency contains four technical departments:[7]

- Regional development and advisory services, including operation of centers at sites around the country that serve individual firms, a network of business incubators, and liaison with private sector associations;
- Policy, program development, and strategy, including relations with other government entities, regulatory issues, and development of legislation affecting the SME sector;
- Information systems and public relations, including development of databases and information exchange with firms outside Slovakia that are linked to the Euro-Info Center network centered in Brussels; and
- Financial instruments, including the guarantee funds and small loan programs managed by the Slovak Guarantee Bank and Slovak Savings Bank.

The agency enjoys a broad mandate to address many of the issues constraining the growth of individual firms and the sector as a whole. It is well positioned to be a catalyst for change, and the inclusion of private sector interests in its governance structure is an encouraging sign, as is the fact that the government does not have a voting majority on the board. Its creation suggests that the government considers SMEs to be an important element in future economic growth, and intends to coordinate financial and nonfinancial assistance programs more closely.

Even so, the total staff of 20 remains small relative to the span of activities, and it appears that the work of crafting a comprehensive, integrated policy framework has only begun. The assessment team

[6] This assistance was delivered through the American Bar Association's Central and East European Law Initiative program.

[7] The descriptions given here do not use the precise Slovak titles for the respective departments.

did not have the opportunity to study the latest draft statement of principles, and thus is not in a position to comment on the likely content of the new Small Business Act, but notes several concerns:

- Government's basic approach to financial services for SMEs has not been finalized, in part because poor results from the guarantee mechanism funded by PHARE indicate that this instrument needs to be redesigned;

- The Ministry of Economy continues to favor subsidy schemes for target industries, having requested Sk 900 million for this purpose in the 1994 budget:[8]

- Dialogue with private sector groups is sporadic and sometimes confrontational, which frustrates efforts to reach consensus on important issues of substance; and

- Our interviews with entrepreneurs carried a consistent refrain that the government doesn't listen, and that regulatory and taxation policies are in constant flux, making it impossible for owners and managers of private firms to plan their affairs and measure their risks.

FINANCIAL INSTITUTIONS

Situation of the Banking Sector

The banking sector in Slovakia is dominated by banks that were previously owned by the state and have been converted to joint-stock companies as part of the program of privatization. Until the process of privatization is completed, majority positions in these banks are held by the National Property Fund, and they remain under the control of the government. In addition to the former state-owned banks, a number of small privately owned banks have been established. Because they have limited capital and liquidity, these newer banks play a relatively minor role in the financial sector.

The newly commercialized state-controlled banks continue to hold the debt of large enterprises, similarly controlled by the National Property Fund, that have received preferential consideration since the beginning of the transition to a market economy. Continued financing of these weak companies, many of them technically bankrupt, tends to absorb bank liquidity, as does the need to fund the government deficit. These twin commitments effectively block the private sector's access to the resources of the banking system.

Specialized Financial Institutions

Slovak-American Enterprise Fund

SAEF represents the single largest infusion of investment capital into the Slovak economy. The fund is widely known, and is regarded by many Slovak entrepreneurs as more receptive to private sector innovation than the major commercial banks. However, both by design and in actual practice, SAEF's clientele overlaps only marginally with the small business sector.

[8] The amount finally approved for these schemes was Sk 200 million.

Originally formed as a subsidiary of a fund operating in both the Czech and Slovak Republics, SAEF has evolved into a stand-alone entity whose portfolio consists exclusively of investments within the Slovak Republic. In two-and-a-half years of operation, the fund has committed approximately $16.4 million to 30 individual projects, of which 38 percent represent equity investments and the balance consists of loans. SAEF's portfolio includes investments as small as $10,000, dating back to its early operations in 1991-1992; however, the composition of its deal flow has changed, with larger projects (upwards of $1 million) now predominating. This pattern reflects management's perception of relative risk between small and midsized or large firms, and the opportunity costs of staff time devoted to analysis and monitoring of the fund's investments. However, SAEF has joined with the State Agricultural Bank (see below) in setting up a specialized loan window for smaller firms.

For project analysis and appraisal, the fund relies on several MBA Enterprise Corps volunteers who are assigned to its staff. Almost all applicants who approach the fund are referred to outside consultants who will assist them in preparing detailed business plans. Consulting services on an hourly fee basis are available from the Entrepreneurship Center and from at least one private Slovak firm, TERNO, which has assisted nine potential SAEF clients with business planning.

State Agricultural Bank

Slovenska Polnohospodarska Banka or SPB was founded in June 1990 as the first Slovak bank without direct ownership by state and foreign institutions. Its original capital was KCs 296 million. Shares are widely held, with the European Bank for Reconstruction and Development (EBRD) owning a 20 percent equity position. Minority shareholders include the Ministry of Agriculture and the Slovak Insurance Company. SPB's primary market is new and developing enterprises, with 75 percent of borrowers comprising firms with fewer than 100 employees.

SPB acts as an intermediary bank for a facility sponsored by SAEF, popularly known as the American Loans Program, which began operations in the fall of 1993. This facility was capitalized by a $3 million contribution from SAEF and an equal investment by SPB. The program considers loan proposals in production and manufacturing sectors from Sk 600,000 to Sk 3 million, with preference given to projects that promote job creation, exports, and environmental initiatives. Loans have a maximum maturity of four years, and a grace period of one year. To date, eight loans have been approved for a total of Sk 20 million. Interest rates carry a 2 percent subsidy with the average rate at approximately 18 percent.

Slovak Guarantee Bank

SZB was established in September 1991 as a government-owned guarantee institution to support large privatization projects and government economic revival programs. SZB's primary function is to provide security in the form of a guarantee to banks where the borrower cannot meet collateral requirements. For SMEs (up to 200 employees), SZB will provide a 75 percent guarantee for loans up to Sk 20 million. Other programs will provide an 85 percent guarantee for loans up to Sk 100 million. For small loans to firms in the agricultural sector, grants are also provided in an amount equal to 10 percent of the loan.

With regard to SME lending, SZB provides guarantees for credits up to Sk 500,000 ($15,000) under a program funded by EC-PHARE in the amount of ECU 3 million. As with other SZB guarantees, this program is designed to assist small businesses that cannot meet a commercial bank's collateral requirements. According to EC-PHARE representatives, this guarantee program has had only 15 percent usage, and in conjunction with the National Agency, they are considering reallocating the funds. Bankers maintain that although SZB programs serve the purpose of reducing risk, they do not solve the problem of liquidity.

DONOR-ASSISTED PROGRAMS SERVING ENTREPRENEURS

Over the past two-and-a-half years, two models have been employed for delivering direct assistance to individual entrepreneurs and firms. Each relies substantially on the participation of volunteers with business management or technical qualifications. U.S. citizens have played prominent roles in such programs, which represent a visible and important part of USAID/Slovakia's portfolio.

Business Service Centers

Establishments offering assistance to multiple entrepreneurs represent one model for delivering technical assistance and training at the firm level. Supported by funds raised privately in the United States, Entrepreneurship Centers in Bratislava (open since 1992) and Banska Bystrica (opening in February 1994) are staffed by American volunteers and Slovak counterparts.[9] Each center offers business planning assistance, which is generally linked to the client's application for loan finance from a bank or SAEF, as its principal service. The standard charge for consulting assistance paid by Entrepreneurship Center clients is Sk 300 per hour. MBA Enterprise Corps volunteers have been involved since the center concept was launched two years ago; additional personnel will come from the group of 15 Peace Corps small business volunteers whose two-year assignments begin in February 1994. Bratislava's Entrepreneurship Center served about 30 clients during 1993, the majority of them referrals from SAEF.

The National Agency for Small and Medium Enterprise Development is establishing a two-tiered network comprising eight Regional Consulting and Information Centers (RCICs), and four Business Innovation Centers (BICs). Three of the RCICs are now fully operational. EC-PHARE funding has supported the provision of physical infrastructure and equipment, and professional staffing comes from individuals recruited by the agency, or seconded from government, with additional participation of Peace Corps volunteers planned in selected regions. RCICs aim at providing general consulting services to new and established SMEs: these include preparation of business plans, advice on legislation and tax matters, and information linkages with agency headquarters to identify potential suppliers and customers. Under current policy, RCICs will not charge clients for these services, and their recurrent funding thus depends on the agency's budget, which in turn derives mainly from the EC-PHARE grants.

The Business Innovation Centers are specially designed to cater to startup entrepreneurs, and operate on the incubator concept. They lease facilities, computers, and office equipment at subsidized rates to entrepreneurs who have minimal investment capital and are trying to get new ventures off the ground. BICs also help their clients search for grant assistance and subsidies to develop new products, and are supposed to tap the information system at agency headquarters to find suppliers, potential foreign investors, and customers. The Bratislava BIC is operational, and is located in the same building as the National Agency's headquarters.

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[9] A similar Entrepreneurship Center operates in Prague.

On-Site Volunteer Programs

The second form of assistance is more intensive, relying on the presence of a volunteer who is formally sponsored by the firm's management. Both the International Executive Service Corps (IESC) and MBA Enterprise Corps participate actively in these programs. Each host firm provides housing and logistical support, having defined specific needs where expert assistance is needed.

IESC has matched more than 60 volunteers with Slovak firms for assignments ranging from two weeks to a maximum of three months. The organization's talent pool consists of retired U.S. executives, many with long experience in specific industries or product lines, who offer their services on an expenses-only basis. Typically, an IESC volunteer is recruited to help a company tackle a specific technical or managerial problem, working closely with its owners and top managers. IESC's country representative actively markets the concept, and seeks out potential clients that range from startup firms to larger, established firms that are being restructured or privatized.

The MBA Enterprise Corps supplies volunteers for 12-month assignments with client firms, drawing on a pool of new MBA graduates from U.S. business schools who have had several years' prior experience working in private industry. The Enterprise Corps currently supports seven enterprises in manufacturing industries that range from gaskets to surfboards. Their roles are defined by the sponsoring firms, and include hands-on assistance with financial management and reporting, marketing and strategic planning, product quality improvement, and related business applications.

Similar programs oriented to firm-level assistance were previously operated by the Citizens Democracy Corps and the Financial Sector Volunteer Corps, but these organizations are no longer active in Slovakia. In the agricultural sector, where relatively few privately held firms operate, a successful ongoing program managed by Volunteers in Overseas Cooperative Assistance (VOCA) advises Slovak cooperatives and small-scale private farmers on various production, processing, and marketing problems.

In terms of their impact on the SME sector, these firm-level interventions can be characterized as follows:

- These programs are responding to widely recognized and well-documented needs in Slovakia's newly emerging private sector. The quality of personnel, especially volunteers, has generated substantial good will, and most clients of these programs have been receptive to outside assistance;

- Although client entrepreneurs typically have a wide assortment of problems (such as marketing, distribution, and process control) in their businesses, many limit their dealings with the consultants to a single product, the business plan, anticipating that going through this ordeal will qualify them for loans;

- At their present scale, these programs reach a small number of clients, who tend to be concentrated toward the upper end of the SME size range. This means that microentrepreneurs, many of them self-employed, and many of them women, are rarely being reached;

- The impact of these programs on client firms is extremely difficult to measure, beyond the rate of subsequent success or failure in obtaining finance. However, even this limited indicator is not used in a systematic manner by some of the volunteer programs. The objectives of the sponsoring organizations vary, and are not always clearly specified; and

- In their present form and scale, it is not feasible for these programs to cover their costs. Both IESC's system, in which the client firm pays subsistence and housing costs for volunteers, and the Entrepreneurship Centers' hourly fee for consultations, incorporate the principle of cost-sharing. However, RCICs do not levy any charge for their services.

MEMBERSHIP-BASED ORGANIZATIONS

The largest voluntary association in the private sector is the Entrepreneur Association of Slovakia (Zdruzenie Podnikatel'ov Slovenska or ZPS), which claims 19,000 members. Established in January 1990, it has a small headquarters staff (2 professionals), an elected board of directors with 18 members, and a cadre of 12 technical advisors who donate their time to the organization. Along with individual members, ZPS also has 15 "collective members" representing industry groups (for example, transportation, bakers, and confectioners) and localities (for example, Michalovce and Banska Bystrica).

Supported by a $78,500 grant from the Center for International Private Enterprise, ZPS increased its membership by more than 4,000 from 1992-1993, began publishing a weekly column in the business newspaper *Trend*, and created a legislative advocacy group. Two representatives from ZPS were appointed to the 13-member Administrative Board of the National Agency, and its president serves on the interministerial National Economic Council. These official designations indicate that government views the organization as a principal spokesman for private sector interests in the SME policy arena, though not the only one.

ZPS is at a relatively early stage of organizational development. Its annual national membership dues are nominal (Sk 50), although several local (county) chapters levy additional charges to support branch offices. The density of coverage and strength of local chapters varies considerably. The most dynamic local leadership is in Galanta, Jilina, and Spisska Nova Ves, and entrepreneurs from these counties serve prominently on the General Board of the association. At Banska Bystrica, efforts to form an Entrepreneurs Club with annual dues of Sk 10,000, affiliated with ZPS, have limited recruitment to about 40 members. On a national scale, the association has tapped only about 5 percent of the potential business population, which is estimated to be more than 350,000.

In November 1993, ZPS received a grant of ECU 40,000 ($50,000) from the National Agency to equip the three strongest local branch offices with computers and fax machines, and to undertake a long-range strategic plan to clarify its goals, formulate an approach to advocacy, and strengthen its financial viability. These activities are ongoing. On the legislative front, a four-person working group from the association is drafting a bill that strongly emphasizes the role of private enterprise in SME development. The group plans to introduce this bill in Parliament through sponsorship by one or more individual MPs. It is conceived as an alternative to the proposed Small Business Act being drafted by the National Agency. A spokesman for the working group argued that the National Agency was drafting a "government bill" which failed to distinguish the needs of privately owned firms from the needs of state-owned and joint-stock companies.

The long-run vision of ZPS' leadership is to create an umbrella organization that can speak and act on behalf of a wide range of voluntary groups encompassing the entire private sector. Many of the groups would be industry-specific or geographically based, and a modest beginning has been made here by enlisting the 15 collective members, which are listed in Annex D. This ambitious goal will not be easy to achieve, both because the association's resources are very limited, and because the formation of an all-inclusive structure may not fit with social and political realities in Slovakia. For example:

- The concept of voluntary affiliation is new, and memories of forced membership in organizations with "official" status remain fresh. Thus many individual entrepreneurs interviewed for this assessment expressed distaste or skepticism about the value of joining any type of business association;

- The current leaders of ZPS are representative of the first wave of postrevolution entrepreneurs. Many have been quite successful, and they value the association as a network for maintaining contacts among one another. This does not necessarily translate into a commitment to attack the problems faced by newer and smaller-scale business operators; and

- Complications are likely in recruitment and retention of members, insofar as ZPS is perceived as taking on an explicit political identity. Advocacy functions, including proposals for new legislation, tend to be most effective when they can be separated from the political party affiliations of members. At the present time, ZPS is closely identified, by some observers, with the Party of Slovak Entrepreneurs, a splinter party with no seats in Parliament, which has openly opposed the current government.[10]

Several smaller associations have sprung up during the past two years, including one entitled the Association of Middle-Sized Slovak Entrepreneurs, which is still in the formative stage, but claims to represent a more specialized constituency than ZPS. Industry-based groups are also beginning to emerge in fields such as real estate, construction, and professional services. Over time, some of the latter may attach themselves to the national structure envisaged by ZPS, but this will depend on the perceived advantages of affiliation, and the demonstrated effectiveness of an umbrella organization in influencing government policies.

The National Chamber of Commerce and Industry (Slovenska Obchodna a Priemyselna Komora, SOPK) was formally established by a legislative act in 1992, but its predecessor organization in the communist era was composed exclusively of SOEs. Although membership has diversified with the entry of privately owned firms, companies controlled by the state — either directly or via the National Property Fund — continue to exert strong influence over the Chamber's affairs and policies. As of January 1994, the Chamber claims 17,500 members, which shows an increase of 1,000 over the past year. Approximately 80 percent of the member firms are privately owned.

By law, all enterprises in Slovakia that are listed on the Commercial Register are required to join the Chamber and to pay annual membership dues of Sk 8,000. Additional fees are charged based on a company's taxable profit, as reported on its tax return. There is also a provision for voluntary membership (dues are Sk 3,000) by sole proprietors and agricultural processors. Currently there are 200 such members. In practice, some individual entrepreneurs either decline to join in the first place, or allow their dues payments to lapse. To date, the Chamber has not taken any direct action against those who do not pay; however, they are not eligible to receive services (such as SOPK's biweekly newsletter, or free consulting advice from its professional staff), or to participate in trade fairs or exhibitions where SOPK plays a leading role.

[10] The leader of this party gained wide publicity by convening a rally at Poprad in October 1993, where he threatened that private firms would boycott payment of social taxes unless state-owned companies were forced to make up the large amounts of such taxes in arrears. Although there is no official link between ZPS and the Party of Slovak Entrepreneurs, many individuals belong to both, and the party chairman serves on the association's board of directors.

A representative of the Chamber sits on the board of directors of the National Agency. However, the Chamber does not have any specific programs or services targeting the SME sector, and it has not taken an aggressive public position in favor of privatization. Its most visible public role involves sponsoring and organizing participation by member firms in trade fairs and exhibitions, inside and outside the country. There is a General Assembly of 100 members that is elected in a decentralized voting process and represents the membership at large; this body elects the Chamber's officers and board of directors. Among the private entrepreneurs interviewed by the team, the organization is viewed as a defender of the status quo that does not provide value to its members proportionate to the high level of dues.

IMPLICATIONS FOR USAID'S ASSISTANCE STRATEGY

USAID/Slovakia has made the creation of a viable private sector the major thrust of its country assistance program. During the past two years, it has invested heavily in preparing large SOEs for privatization, by committing substantial consulting resources to strategic enterprises in industries such as textiles, building materials, and chemicals, as well as defense plants seeking to convert to commercial production. For reasons outside the scope of these interventions, however, the actual pace of privatization has remained much slower than in the other three Visegrad Pact countries of Hungary, Poland, and the Czech Republic.

The government's pledge to resume privatization, perhaps accelerating it to make up for lost time, presents difficult political choices, and its implementation timetable is highly uncertain. The costs of continued delay to the economy as a whole, and to the banking system in particular, were cited in interview after interview. The asset base and financial condition of many of the larger enterprises continue to deteriorate, a trend which lowers the probability that foreign investors will come forward to offer attractive prices. As the pool of potential purchasers shrinks, the likely financial returns to the state also diminish, raising the perceived political risk of actually completing divestiture of companies. This near-term dilemma is offset, however, by the reality that neither the government budget nor the banking system can sustain the subsidies that presently flow to keep the nonviable state enterprises afloat.

Experience in Slovakia, and elsewhere in Central and Eastern Europe, underscores the point that privatization is not a panacea. In terms of actions that may stimulate entrepreneurial expansion and job creation, it is necessary, but not sufficient. In the case of the emergent SME sector, this is especially true: many of the constraints noted in this report would be only partially mitigated, and only indirectly addressed, if Slovakia's privatization program were placed on a fast track and completed in the shortest possible time.

The main focus of this assessment, therefore, has been on the *sufficient conditions* that would complement the eventual accomplishment of privatization, and create an environment in which Slovakia's small business sector would not only increase its share of GDP but also contribute to sustained GDP growth in the long term. It should be clear from the preceding sections of this report that the sufficient conditions themselves will take time to be established. Certain elements involving regulatory reform or legislative action may appear to be concrete and straightforward; but the necessary consensus for making such changes may not yet exist. Many of the institutional actors with a stake in creating and maintaining an enabling environment for private enterprise are inexperienced and do not yet have all the tools needed to fulfill their potential roles.

The principal ongoing activities in USAID/Slovakia's small business portfolio were not intended to address issues of this kind, which are sectoral and systemic in nature rather than company-specific. By their very nature, volunteer services to individual firms, and to small clusters of clients at the Entrepreneurship Centers, are not designed to modify the policy and regulatory framework in which the firms operate. Similarly, the infusion of SAEF capital into the Agricultural Bank's small business window has a potentially high demonstration effect, but by itself cannot influence the government's policy decisions regarding entrepreneurial access to capital.

The establishment of the National Agency for Small and Medium Enterprise Development marks a very important step in the Slovak Government's approach to the private sector. It provides an institutional framework on which an umbrella policy and accompanying legislation can be based, and it has been designed with explicit communication channels to stakeholders in the private sector, as well as within government.

In the current context, there appear to be three interdependent activities that USAID might usefully support, and thereby help to put in place the sufficient conditions mentioned above:

- **Collaboration with the National Agency in the elaboration of government's umbrella policy** (statement of principles) for the sector, and in the preparation of new legislation, starting with the Small Business Act. USAID assistance should aim at building the agency's capacity to analyze the full spectrum of policy issues (regulatory, financial, fiscal, for example) affecting SMEs. In this respect, assistance should treat policy analysis and formulation as ongoing responsibilities, rather than a one-shot deal that concludes when the Small Business Act is enacted into law.

- **Organizational development assistance to business associations and other voluntary bodies** with significant membership from the private sector. Such assistance would have the objective of strengthening these organizations, most of which are very young, in membership services and advocacy. Rather than selecting a single organization as the client for such assistance, it is recommended that this function be based in the agency, with a clear mandate to reach out to all bona fide organizations with significant membership potential, whether regional-, national-, or industry-based.

- **Assistance with surveys and analytical support to develop better information** on the structure, composition, and dynamics of Slovakia's SME sector. This activity would help to identify economic subsectors with significant growth potential, and it would also examine the needs of household-level microenterprises and informal sector firms, whose role or extent in the economy is not well understood. This would take data collection beyond the list of commercially registered companies, which number less than 20,000, into the category of physical persons and craftsmen, numbering several hundred thousand, whose economic activities cover a wide spectrum.[11]

These activities would involve a combination of technical assistance and training, and could be blended in a single project housed at the National Agency. The assessment team's findings indicate that the assistance would be very timely, given the current stage of development in the SME sector, and that the National Agency is receptive to the general concepts outlined here. Although we have not been able to conduct an extensive dialogue with all of the possible stakeholders in the private sector, demand for organizational development support is likely to be high, given the agency's limited resources and short experience. Better, more complete information on the SME sector will benefit business associations as they seek to build their membership base, and should also inform and improve the process of policy making within government.

An issue requiring further dialogue between USAID and the National Agency concerns the degree of fit between this proposed project concept and the ongoing assistance from EC-PHARE.[12] In the current year, PHARE is providing 60 percent of the agency's operating budget, with the balance coming

[11] An example from Kenya illustrates the utility of carefully planned and managed information activities. A survey of the informal sector helped the Kenya Rural Enterprise Program (K-REP) to understand its client base and adapt its financial services accordingly. GEMINI project staff from DAI and Michigan State University assisted K-REP in this exercise.

[12] In addition to PHARE assistance, a German technical advisor is now based at the National Agency, with a mandate to coordinate SME assistance from German nongovernmental organizations as well as official bilateral programs. The assessment team did not meet with him, however.

from the Slovak Government. The agency's headquarters and branches (RCICs and BICs) are being equipped, the financial instruments component is due to receive additional capital, and PHARE is providing technical assistance personnel to support information systems development and the credit programs. Although there is no obvious conflict or redundancy between these activities and the policy-oriented assistance that USAID might provide, this point will need to be verified.

If there is general agreement that the National Agency would be an appropriate base for a small business policy project, the following guidelines should help to finalize the basic design. They combine insights from the GEMINI experience in Poland, observations made by the assessment team, and insights from people who were interviewed:

1. **Duration.** The project should reflect the long-term nature of capacity-building objectives in the private and governmental institutions where it will work. An initial period of 15-18 months might be appropriate, with the possibility of continued USAID involvement, depending on the results achieved, after September 1995, the end of the next U.S. fiscal year. Continuity in assistance will be desirable if the project shows satisfactory progress in the first phase.

2. **Long-term technical assistance as an anchor.** The project should be managed by a resident long-term U.S. advisor who would serve for its full duration. This person would be based at the National Agency; a preliminary draft scope of work appears in Annex E. It is recommended that he or she operate there in a general advisory capacity, rather than being attached to one of the four departments, because the three proposed project activities tend to cut across internal departmental lines.

3. **Flexible use of short-term technical assistance.** A component for U.S. short-term technical assistance should be included, to provide the ability to respond to demand under all three activity areas. For example, National Agency staff are likely to request expert assistance on legal and tax policy matters; the Entrepreneur Association may seek help in promoting its services to prospective new members, or training in policy advocacy; and short-term assistance will probably be needed to design and oversee surveys of small-scale and microenterprises. For illustrative purposes, a brief scope of work for a short-term legal advisor is included in Annex E.

4. **Involvement of Slovak professionals.** An effective project will depend on close teamwork between U.S. and Slovak professionals. Although National Agency staff will be both counterparts and clients for this project, the small size of the organization means that personnel will be stretched thin, at least in the immediate future. It is recommended that the project be enabled to access long- and short-term services from well-qualified Slovak professionals. They would be especially valuable in outreach activities with business associations and other private sector clients outside Bratislava. This binational approach to staffing follows the successful method used in GEMINI's Poland Small Business Project. A draft scope of work for a long-term Slovak advisor appears in Annex E.

5. **Training and internships.** Practical, short-term training and internships with U.S. institutions should be built in, with eligibility for both National Agency staff and leaders of business associations. To ensure timeliness and relevance in these activities, they should be managed in close coordination with the project's technical assistance to the National Agency and the business associations.

6. **Collaboration with Peace Corps.** Close collaboration with Peace Corps/Slovakia's small business program should be explicitly built into the project. The cadre of midcareer volunteers entering service in February 1994, all with significant prior business experience in the United States, will be strategically placed in locations all over Slovakia, including RCICs and Entrepreneurship Centers. The placement of a volunteer from this group in the National Agency's headquarters represents an important asset to the proposed project.

7. Networking and information exchange. The project should actively promote information exchanges with other institutions concerned with SME development. USAID's worldwide experience base in this field would augment the information accessible through the EC's communications network, to which the National Agency is now linked. The GEMINI project's dissemination network provides one proven model for accessing and distributing such information.

Although these guidelines have been derived in part from experience with the GEMINI Small Business Project in Poland, they have been deliberately framed in general terms. It will be critically important to tailor activities to the institutional, economic, and cultural context of Slovakia. The main measures of success of the project should be framed in terms of improved institutional capability, both within the National Agency and in private sector associations.

ANNEX A

LIST OF PERSONS INTERVIEWED

USAID/Bratislava

Patricia J. Lerner, USAID Representative
Loren L. Schulze, Project Development Officer
Marian Krško, Project Advisor
Roman Snajdr, Project Advisor

Slovak-American Enterprise Fund

Leighton Q. J. Klevana, President
Douglas Swaim, Senior Investment Officer

Antimonopoly Office of the Slovak Republic

Eugen Jurzyca, Director of the Fourth Executive Department
Andrej Juris

United States Embassy

Christopher Sandrolini, Economic and Commercial Attaché

Entrepreneur Association of Slovakia

L'udomir Dolgos, Member of General Board
Milan Hatnančik, Member of General Board
JUDr. L'udovit Paus, General Secretary
Miroslav Knitl, Advisor

National Agency for Development of Small and Medium Enterprise

Jozef Brhel, General Director
Ján Foltin, Director, Dept. of Information and Foreign Activities
Ivan Katriak, Director, Dept. of Coordination
Brendan Martin, EC-PHARE Advisor

The Entrepreneurship Center - Bratislava

Ann Steele and Thomas Reich, Senior Consultants (MBA Enterprise Corps)
Ing. Iveta Zraková, Consultant

International Executive Service Corps

Ing. Voytech Molnar, Country Director, Slovakia

Peace Corps

William C. Piatt, Director, Slovakia
Michael Honegger, Acting Director, Slovakia

KNO Worldwide

Margaret Mari Novak, Partner
RNDr. Tibor Filipovič, Trainer

Business Leaders in Galanta Region, Southwestern Slovakia

Milan Hatnancik, Retailer in Galanta and Board Member of Entrepreneur Association of Slovakia
Jãn Kanyik, Retailer in Dunajska Streda and Board Member of Entrepreneur Association of Slovakia
Robert Keller, Owner/Manager of Security Agency, Galanta
S. Szabó, Owner/Manager of Szabo Souvenir, Galanta

The Entrepreneurship Center - Banska Bystrica, Central Slovakia

Lloyd Jarkow, Senior Consultant (MBA Enterprise Corps)

Office of the Mayor, Banska Bystrica

Karel Sedlar, Director of Entrepreneurship

Entrepreneurs in Banska Bystrica

Ing. Anton Gálik, Director of Fittich Alarm, Electronic Security Firm (partly owned by a Swiss firm)
Ing. Jozef Maslik, Partner of Electris, Cable TV Service Firm
RNDr. L'ubomir Kontšek, Director, and Ing. Vendelin Maretta, Technical Director, KELCOM Security Co. (franchise of Canadian firm)

Investment and Development Bank

Ing. Dipl. Ignác Prno, Chief Manager, Strategy and Planning Department

Slovak Guarantee Bank

Ing. Gabriela Sedlăkovă, Director of Banking Operations
Ing. Daniel Jõna, Department for Small and Medium Enterprises

American Bar Association-Central and East European Law Initiative

Paul F. Zendzian, Liaison for Slovakia

Ministry of Economy

Dipl. Ing. Štefan Turan, Director, Enterprise Development and
Regional Policy Department

Ministry of Finance

John R. Fadoir, U.S. Treasury Budget Advisor

European Bank for Reconstruction and Development

Igor Tham, Resident Representative

Construction Firm Owner/Manager, Bratislava

Ing. Robert Helm, Director, BAUPROFING

Slovak Agricultural Bank

Ing. Kovácová, Director of Small Business Lending
Ing. Viera Gajdošová, Banking and Trade Specialist, Credit Dept.

Slovak Chamber of Commerce and Industry

Ing. Anton Lisý, Director of Entrepreneurial Relations and Regional Policy
Ján Vlčko, Director of Legal and Financial Consulting Dept.
JUDr. Ing. Pavel Kopál, Consultant-Specialist

Presidential Office of the Slovak Republic

Brigita Schmognerova, Head of the Economic Policy Development

ANNEX B

LIST OF DOCUMENTS REVIEWED

Bijan B. Aghevli et al. *Stabilization and Structural reform in the Czech and Slovak federal Republic: First Stage*. International Monetary Fund, Occasional Paper No. 92, March 1992.

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M. Mari Novak, KNO Worldwide. *Small Business Development Sector Assessment in the Czech and Slovak Federative Republic*. Prepared for Peace Corps, Prague, September 1992.

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TERNO [Institute for Trade, Tourism, and Small and Medium Enterprises, Ltd.]. *Analysis of Small and Medium Enterprises in the Slovak Republic*. Prepared for the Ministry of Economy, Bratislava, November 1993.

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________. "On the Road to Middle and Eastern Slovakia." Trip Report by P. Lerner, M. Krsko, R. Snajdr, June 1993.

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ANNEX C

PARTIAL TRANSLATION OF BROCHURE FROM NATIONAL AGENCY FOR SMALL AND MEDIUM ENTERPRISE DEVELOPMENT

[SLOVAK: NARODNA AGENTURA PRE ROZVOJ MALEHO A STREDNEHO PODNIKANIA]

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SECTION I: UNTITLED MAIN BROCHURE

The Agency is an independent institution governed by an Administration Board.

The objective of the Agency is to initiate the development and growth of existing and newly established small and medium enterprises in the Slovak Republic. The Agency secures coordination of all activities for supporting small and medium enterprises in the Slovak Republic, including financial services, at the international, national, and local levels.

First of all the Agency:

a/ prepares the state policy and strategy that is necessary for the field of small and medium enterprises, and submits the policy and strategy to the central bodies of the Government of the Slovak Republic;

b/ identifies and analyses barriers to entrepreneurship development;

c/ supports and participates in cooperation with financial institutions with regard to creation of credit and guarantee schemes;

d/ supports and develops regional consulting and informational centers;

e/ co-operates with already existing European informational networks and databases in the entrepreneurial field;

f/ will initiate a widening scope of activities in the field of small and medium enterprises by means of an advertising campaign for the public, issuing information literature, organizing conferences, seminars, and exhibitions;

g/ is authorized to carry out the functions of the Program Management Unit of the Small and Medium Enterprises Project, which facilitates and coordinates PHARE program assistance to the Slovak Republic; and

h/ co-operates with domestic and foreign sponsors for the benefit of small and medium enterprises in the Slovak Republic.

In order to achieve its objective, the Agency uses the following instruments and methods:

- Support in building the network of Regional Consulting And Information Centers and Business Innovation Centers;
- Support by obtaining financial means;
- Information;
- Legislative activities;
- Active participation in the restructuring of enterprises in privatization process;
- Determining the direction of investments; and
- Education

The Agency, by means of special financial means used as credit collateral in the Slovak Savings Bank, allocates the financial means determined for support of small and medium enterprises into the financial institution, and in this way supports prospective entrepreneurial projects. In the future, the

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Agency will establish a seed capital fund that will enable the people without sufficient capital of their own to start up businesses in the manufacturing and production fields.

The objective of the Agency in the information sphere is to build (1) a European Information Center, and (2) a Slovak Small And Medium Enterprises Database.

Legislative activity by the Agency for improvement of conditions for small and medium enterprises is as follows:

a/ The Agency, in cooperation with associations of entrepreneurs in Slovakia, will investigate the valid legal regulations relating to business activity, and will initiate necessary changes that stimulate the development of small and medium enterprises.

b/ The Agency proposes amendments to the tax system that lead to the decrease in tax burden of small and medium entrepreneurs.

c/ The Agency, in cooperation with the Slovak Republic Ministry of Labor, Social Issues, and Family, proposes and realizes the arrangements that stimulate new jobs creation.

At the head of the Agency there is an Administration Board that consists of 13 members with the right to vote. The members are appointed by the Ministry of Economy, from representatives of the following organizations:

- Slovak Republic Ministry of Economy
- Slovak Republic Ministry of Finance
- Slovak Republic Ministry of Labor, Social Issues, and Family
- Slovak Republic Ministry of Environment
- Association of Villages And Towns of Slovakia
- Slovak National Agency For Foreign Investments And Development
- Slovak Chamber of Commerce And Industry
- Entrepreneur Association of Slovakia
- Slovak Guarantee Bank
- Slovak Savings Bank
- Council of Small And Medium Entrepreneurs

In addition, a representative of European Community (whose PHARE program paid most of the costs connected with establishing the Agency) and representatives of other sponsoring organizations may participate in the Administration Board, without the right to vote.

The resources of the Agency come from the state budget, supported in particular by the European Community by means of the PHARE-SME Program.

SECTION II:
TITLED "REGIONALNE PORADENSKE A INFORMACNE CENTRA"

[REGIONAL CONSULTING AND INFORMATION CENTERS]

The network of Regional Consulting And Information Centers, in whose establishment and development the Agency significantly participates, is spread all over Slovakia. The task of the Agency is to provide comprehensive consulting services to operating and newly established small and medium enterprises in the fields of:

- consulting services with regard to entrepreneurial plans;
- working out the business plan;
- conditions for doing business in a region;
- legislation consulting;
- financial consulting;
- tax consulting; and
- the labor market.

Regional Consulting and Information Centers (RCICs) have information on which basis the experts in the centers will assess the potential success of a business plan, determine its possible constraints, and identify suppliers, customers, and competitors. The advantage of consulting services in these Regional Consulting and Information Centers is their professional and information basis, which is provided by linking the centers to the Agency's headquarters.

Business Innovation Centers (BICs) have an important role in the system of support for small and medium enterprises. BICs primarily focus on creation of a positive business environment for firms that bring an innovative business intention. Besides comprehensive business consulting, BICs provide the entrepreneurs, who are starting their business for the first time, with material assistance. BICs serve as incubators for small firms, and in this way help them to decrease the costs that are needed for starting the business. BICs lease the office and computer equipment, software, and offices as well for a small fee. Moreover, BICs create conditions for securing financial assistance, and assist in securing sales possibilities and obtaining grants. Using the European Network of Innovation Centers (EBN), the BICs intermediate the contacts with the firms operating in this network. They can also help with promotional activities, and organize common participation of incubator firms in exhibitions. BICs can arrange contacts for incubator firms with highly qualified experts from the required field.

RCIC Locations:

RCIC POPRAD: Ing. Peter Litavec, CSc.
Popradske nabrezie 16, 059 06 Poprad
tel.:092/455232, 455225, fax:092/63127

RCIC MARTIN: Ing. Jarmila Canadyova
Divadelna 31, 036 01 Martin
tel.:0842/36327, fax:0842/36329

RCIC NITRA: Ing Dusan Slizik, CSc.
Farska 7, 949 01 Nitra
tel.:087/410107, fax:087/410106

RCIC PRESOV: Ing. Jan Hudacky
Namestie mieru 3, 080 01 Presov
tel.:091/32663, fax:091/32663

RCIC ZVOLEN: Ing. Miroslav Grekco
Studentska 986/10, 960 01 Zvolen
tel.:0855/29912, fax:0855/29905

RCIC TRENCIN: Ing. Jan Jezik
Hviezdoslavova 3, 911 01 Trencin
tel.:0831/36720, fax:0831/36720

RCIC POVAZSKA BYSTRICA: Ing. Jozef Hosmaj
Okresny urad prace, stred Centrum 13P/17
017 01 Povazska Bystrica
tel.:0822/62793, 62797, fax:0822/22001

RCIC LUCENEC: Ing. Miroslav Hasko
Namestie republiky 8, 984 01 Lucenec
tel.:0863/22039, fax:0863/27210

RCIC TREBISOV: Ing. Jan Petr
M.R.Stefanika 1161/184, 075 01 Trebisov
tel.:0948/5711, fax:0948/5711

BIC Locations:

BIC BRATISLAVA: Ing. Jan Strelecky, CSc.
Nevadzova 5, 821 01 Bratislava
tel.:07/237666, fax:231736

BIC PRIEVIDZA: Ing. Frantisek Vrtak
Sveniho 9, 971 01 Prievidza
tel.:0862/26733, fax:0862/22169

BIC SP.NOVA VES: Ing. Michal Buza
Zimna 72, 052 01 Spisska Nova Ves
tel.:0965/26254, fax:0965/26980

BIC KOSICE: Augustin Sokol
Loslerova 2, 040 01 Kosice
tel.:095/6222174, fax:095/6228661

SECTION III:

"POZICKY A ZARUKY PRE MALYCH A STREDNYCH PODNIKATEL'OV" [LOANS AND GUARANTEES FOR SMALL AND MEDIUM ENTREPRENEURS]

There are three support programs:

1/ PHARE Program for credit collateral in the Slovak Guarantee Bank

2/ PHARE Program for collateral for small credits in the Slovak Guarantee Bank

3/ Small Loans Program in the Slovak State Savings Bank

A. Loan Guarantee Scheme

Support is represented by providing a guarantee up to a maximum of 75 percent of the loan value borrowed from the banking institution.

Conditions for providing a guarantee:

a/ Small and medium private enterprises can apply for a guarantee.
b/ The enterprise must be newly established or must be in operation less than two years.
c/ The enterprise may employ no more than 100 persons.
d/ Headquarters of the enterprise and realization of business plan must be in Slovak Republic territory.
e/ The enterprise does not have a necessary property security for a guarantee of the credit.
f/ The business entity must be focused on production field or tourism.
g/ The state ownership must not be higher than 50 percent of the enterprise equity.
h/ Within the framework of this program the enterprise can obtain guarantees for credits within the framework of one business objective.
i/ It is impossible to take a guarantee for previously granted credit.
j/ The guarantee cannot be transferred.
k/ The maturity of the credit may be 1-5 years and the credit must be paid on August 21, 1999 at the latest.

The credit may be used for:

- purchase of machines and equipment
- purchase, building, and reconstruction of houses and land property
- purchase of basic inventories and raw material or material for further processing, however maximally up to the amount of 30 percent from the amount of required credit.

In return for the guarantee, the borrower of credit from the Slovak Guarantee Bank pays a fee from the volume of the guarantee in amount of 1 percent for short-term credit; 1.5 percent for medium-term credit; and 2 percent for long-term credit.

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B. Small Business Guarantee Scheme

Support is represented by providing the guarantee up to a maximum of 80 percent of the credit that is provided by the lending institution.

Conditions for providing the guarantee:

1/ Small and medium private enterprises may apply for the guarantee.
2/ The enterprise must be new or recently established.
3/ The enterprise may employ a maximum of 25 persons.
4/ Headquarters of the enterprise and realization of the business plan must be in Slovak Republic territory.
5/ The business project must be focused on production, tourism, craftsmanship, repair and maintenance, or similar activities.
6/ Within the framework of this program the enterprise can obtain the guarantees for credits within the framework of one business plan.
7/ The guarantee cannot be provided with a retrospective date of maturity.
8/ The guarantee is not transferrable.
9/ Maturity of the credit must be 1-3 years and the credit must be paid on September 9, 1996 at the latest.

The credit may be used for:

- purchase of machines and equipment
- purchase, building, and reconstruction of houses or land property
- purchase of basic inventories and raw material or material for further processing.

For taking over the guarantee, the receiver of the credit of Slovak Guarantee Bank will pay the fee from the volume of the guarantee in the amount of: 1 percent for short-term credit and 1.5 percent for medium-term credit.

C. Small Loan Program

The maximum loan permitted is Sk 800,000. It is possible to obtain a loan under the following conditions:

1/ The applicant's enterprise must have been founded after 1990.
2/ There may be no more than 25 employees in the enterprise.
3/ The business project must be focused on production, tourism, craftsmanship, repair and maintenance.
4/ The loan can be provided for:
   - purchase of machines and equipment
   - purchase, building, and reconstruction of houses and land property
   - purchase of basic inventories and raw materials or material for further processing.

The loan has a maximum maturity of five years, and the interest rate is 2.5 percent above the discount rate of National Bank of Slovakia.

ANNEX D

BACKGROUND INFORMATION ON ENTREPRENEUR ASSOCIATION OF SLOVAKIA

ENTREPRENEUR ASSOCIATION OF SLOVAKIA

An interest group of enterepreneur subjects - citizens of Slovak Republic. Association is a decesive representative of privat entrepreneur activities in Slovak Republic. It was established 28.1.1990 as the first association of privat entrepreneurs after the revolution in 1989. Since 1.3.1993 it is the member of European Confederation of Associations of Small and Middle-sized Enterprises in Brusseles.

Activity principles :

* voluntarity
* respecting the right for freedom for speech and opinion of each member
* apolitical character

Main aims :

* support the common legitimate interests of privat sector
* representation of the privat sector in the Council of Economical and Social Agreement
* representation of the privat sector in the Economical Council of the Government of the Slovak Republic
* representation of the privat sector in further governmental and ungovernmental institutions (Fund of National Property of the Slovak Republic, Employment Fund, National Insurance, National Agency for Small and Middle Business and others)

Organizational structure :

* EAS General Meeting
* EAS General Board
* EAS President
* EAS Vicepresidents
* EAS Advisory Board
* EAS District Boards
* EAS Clubs and EAS Collective Members

EAS Clubs and EAS Collective Members :

* Association of Agro-turistic Entrepreneurs of Slovakia
* Association of Privat Driving Schools
* Association of Road-building Organizations of Slovakia
* Association of Land-owners and Agro-entrepreneurs of Slovakia
* Association of Women-entrepreneurs and Women-managers of Slovakia
* Slovak Association of Entrepreneurs in Transport
* Slovak Association for Foreign Entreprising (SLOVEX)
* Slovak Association for Consulting
* Entrepreneur Association of Bakers and Confectioners in Slovak Republic
* Association of Real-Estate Offices of Slovak Republic
* Club of Entrepreneurs in Banská Bystrica
* Club of Entrepreneurs in Zvolen
* Club of Entrepreneurs in Michalovce
* Club of Entrepreneurs in Senica
* Slovak Association of Dancing Teachers

Contact Address :

Entrepreneur Association of Slovakia
Secretariat
Cukrová 14
813 39 Bratislava
Slovak Republic
Phone, Fax : (+07) 368 872

ANNEX E

ILLUSTRATIVE SCOPES OF WORK FOR PROPOSED TECHNICAL ASSISTANCE

SCOPE OF WORK

SHORT-TERM LEGAL ADVISOR

To assist the Project Manager in the implementation of the Slovakia Small Business Policy Project, the Advisor will undertake the following tasks:

1. Review National Agency for Small and Medium Enterprise Development (NASMED) proposals for new laws and/or amendments to existing laws and regulations affecting SME development.

2. Consult with Slovak and resident western attorneys to ensure proposals are in conformity with Slovak legal practices and procedures and to identify those areas of Slovak legal practices requiring amendment in order to address SME needs.

3. Develop an action plan that will identify the process for ensuring passage of proposed legislation.

4. Prepare written report of activities for Project Manager before departure.

5. Undertake those tasks appropriate to consultant's technical expertise as requested by the Project Manager.

ILLUSTRATIVE SCOPE OF WORK

SLOVAK ADVISOR

To ensure effective implementation of the USAID/Slovakia Small Business Policy Project, the Project Manager will be assisted by a long-term Slovak professional who will act in the following advisory capacity:

1. Establish and maintain day-to-day liaison with staff of National Agency for Small and Medium Enterprise Development (NASMED).

2. In consultation with NASMED staff, assist the Project Manager in identification of those project components to receive priority implementation. (policy, legal, financial, SME advocacy)

3. Establish collaborative linkages with Government and private sector and Slovak counterpart individuals and organizations capable of providing input on specific project components. (policy, legal, financial, SME advocacy)

4. Assist Project Manager in developing national, regional, and local SME advocacy/outreach sub-project and to implement same.

5. Identify appropriate Slovak candidates for short-term consulting assignments as may be required.

6. Undertake such other tasks as may be requested by the Project Manager.

7. Oversee all project activities in the absence of the Project Manager.

8. Supervise Slovak staff and otherwise undertake tasks of Office Manager.

ILLUSTRATIVE SCOPE OF WORK

PROJECT MANAGER, SMALL BUSINESS POLICY PROJECT

As part of USAID/Slovakia's efforts to help create a positive policy and regulatory environment which will enable the formation of new, and the expansion of existing, small and medium enterprises; and to encourage private sector business organizations in Slovakia to establish and implement activities designed to promote private sector interests, the Senior Advisor will undertake the following tasks:

1. Assist National Agency for Small and Medium Enterprise Development (NASMED) to develop strategies which address SME policy, legal, regulatory, and financing constraints and opportunities.

2. Assist NASMED in the development and implementation of SME advocacy programs relevant to legislative, regulatory, and financial reform initiatives to create and sustain competitive market development and the formation and expansion of SME's.

3. Assist NASMED in strengthening the SME advocacy capability of national, regional, and local business associations to serve as the voice of the private sector in promoting the implementation of the above strategies and programs.

3. Create positive linkages and collaboration between donor-funded technical assistance projects concerned with SME development in Slovakia. Such collaborative efforts will specifically include Peace Corps Volunteers in the field.

4. Identify the need for and recruit U.S.-based and Slovak professionals with appropriate skills for short-or long-term assignments to respond to demands for specific technical expertise.

5. Supervise day-to-day project management including:

    - Supervision of project staff and short-and long-term consultants;

    - Personnel administration;

    - Monitoring of progress against work plan goals and objectives and producing quarterly reports for USAID;

    - Maintenance of project records and accounts; and

    - Maintaining regular communications with USAID Representative in Bratislava, the Bureau for Europe and the Newly Independent States, and the Government of Slovakia on all matters of relevance to project management and implementation.

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