An Evaluation of Phare SME Programmes

Slovak Republic

Final Report

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The report is based on fieldwork and the position as at October 1998.

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Introduction

This is one of a series of ten Phare SME Country Evaluation Reports which examines the contribution of Phare's SME programmes in the context of macro economic and SME developments in the country since the transition process began. This is part of the horizontal evaluation of the Phare's SME programmes being undertaken for the Evaluation Unit by an RDH/LDK consortium of three EU specialists supported by local consultants in each country. This country evaluation report, has been prepared by Charles Monck with Dr Daniela Zamanovicova, the Deputy Director of the Centre for Economic Development, a Research Centre in Bratislava, based on preparatory work undertaken between June-August 1998 and a three week evaluation mission in October 1998.

The Country Evaluation Report follows a common format. The first chapter sets out the main features of SME development in the context of key changes in the economy and the political make up of Slovakia since 1989. The chapter includes sections on the financial environment and institutional developments effecting SMEs. The second chapter summarises Phare's SME programmes and the work of other donors, and then reviews the appropriateness of the overall design of Phare's SME programme in the context of the country's priorities.

The formal evaluation of the financial and the institutional programmes are set out in chapters three and four respectively, based on a standard evaluation methodology and logical frameworks that are included in appendices A to E. Particular projects have been selected, and detailed interviews were carried out with a small sample of intermediate and final beneficiaries in selected areas. The results of each evaluation are set out in a common format covering relevance, efficiency, effectiveness, impact and sustainability, together with a discussion of key issues and future priorities. The conclusions and recommendations arising from the evaluation are set out in chapter five.

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Chapter 1 Main features of SME developments in Country

1.1 Macro economic and political context:

The Slovak Republic was born out of the Czech and Slovak Federation in 1993, and inherited a strong rural tradition and an industrial base. To a large extent, the industrial base dates from 1945 and was consisted of very large enterprises (particularly in heavy engineering and armaments) servicing the needs of the former Soviet Union. Since independence, after a continued fall in output in 1993, the country has experienced four years of growth with inflation falling from 23% in 1993 to 6% in 1998. Bratislava and the neighbouring regions have grown considerably faster than the regions in the north and east, stimulated by inward investment and small firms particularly in services and trade. Some of the major political and economic developments are summarised in table 1.1 below:

Despite this growth, the country is now faced with a rising foreign trade deficit (-6.9% GDP) and a high government debt (-5.7%), due to increased imports, inefficient tax collection, an expansive fiscal policy, pegged exchange rate and a tight monetary policy. Commentators have argued that the country has been slow to carry through the industrial restructuring, which has been characterised by powerful vested interests and widespread political patronage. This has retarded the process of privatisation and restructuring, and the carrying though of necessary political reforms. The private sector has been constrained by a weak banking system, interest rate volatility, and a high public sector borrowing requirement. Following the 1998 general election, the new government was faced with high expectations and little room to manoeuvre.

Table 1.1: Macro Economic Indicators

	1990	1991	1992	1993	1994	1995	1996	1997
Real GDP Growth Rate (%)	-2.8	-14.8	-6.5	-3.7	4.9	6.9	6.6	6.5
Current Account Balance (% GDP)	n/a	n/a	0.4	-5.0	‘4.8	2.3	-11.2	-6.9
Government Budget deficit (% GDP)	n/a	n/a	-11.89	-6.2	-5.2	-1.6	-4.4	-5.7
Gross Foreign Debt (% GDP)	n/a	n/a	n/a	30.9	31.2	33.3	41.5	55.0
Real-effective Exchange rate (1994=100)	84.2	78.3	81.8	95.8	100.0	105.9	108.2	n/a
Inflation Rate (CPI, avg.)	10.4	61.2	10.0	23.2	13.4	9.9	5.8	6.1
Unemployment rate (%)	1.6	11.8	10.4	12.2	13.7	13.1	11.1	11.6
Exchange rate SK per Euro	-	-	-	36.1	38.1	38.9	38.9	38.1

Statistical Office of the Slovak Republic, EBRD, National Bank of Slovakia and IMF

The period since independence has been dominated by Meciar’s nationalist coalition, which, except for a brief six month period in 1994, has held power until it was defeated by a four party right of centre coalition following a general election in October 1998.

Against this background, economic policy has been more oriented towards dealing with the legacy of large state owned enterprises, reacting to the growing social problems arising from rising unemployment and attracting inward investment, rather than improving the environment for small firm development.

Due to concerns about the policy of the Meciar government towards democracy, Slovakia was not included in the first group of countries applying to join the European Union. However, within days of coming to power, the new coalition, which is markedly more pro-

European, has requested the EU to reconsider its decision, with the result that accession related issues have now become significantly more important.

1.2 Growth and development of SMEs

Prior to 1989, vertical integration was especially favoured with a single enterprise being responsible from energy production to manufacturing, retail and housing. In 1986, the average size of an enterprise was 2,100 employees with less than 2% of the population in industrial enterprises with less than 500 employees[1]. Unlike in some other East European Countries, there has been very little tradition of SMEs, which were actively discouraged in Slovakia. Given this legacy, a high priority was initially given to improving the environment for SME development, which led to a surge of activity in 1991 and 1992, particularly amongst self employed people; however, many of these early businesses were either transformed or collapsed.

Table 1.2: Births and Deaths of self employed and legal entities

Rate of formation	1991	1992	1993	1994	1995	1996	1997
Self employed registrations	244,963	139,711	7,609	21,584	43,893	49,116	24,609
de-registrations	55,099	45,059	29,803	21,914	59,422	54,197	14,070
Net increase	**189,864**	**94,652**	**(22,194)**	**(330)**	**(15,529)**	**(5,081)**	**10,539**
Legal Entities: Registrations	10,018	10,636	7,979	8,819	5,549	9,660	6,108
de-registrations	180	1,157	621	160	865	794	487
Net increase	**9,838**	**9,479**	**7,358**	**8,659**	**4,684**	**8,866**	**5,621**

After an initial surge, since 1992, the number of self employed (registered tradesmen) has stabilised at around 250,000 people, with ‘start ups’ (around 30,000) being offset by a similar number of self employed ceasing trading (by returning to full time employment, registering as unemployed or registering their business as a legal entity); on average, around 20% per year are de-registering. Of the 256,000 registered self employed in 1997, 33% were in trade, 26% were in services, 17% in industry, 12% in construction and 9% in agriculture..

During the same period there has been a steady increase in the number of legal entities (companies and partnerships), with an average formation rate of around 8,000 per year,. The overall numbers of both small firms (with less that 25 people) and medium sized firms (up to 499 employees) doubled between 1993 and 1997. Of the 5,905 new businesses which registered in 1997, 46% were in trade, 32% in services, 14% in manufacturing and 8% were in construction.

Table 1.3: Number of enterprises by size over time: 1990 to 1997 (old classification)

Size distribution	1991	1992	1993	1994	1995	1996	1997
Self employed	200,817	286,284	265,262	266,213	255,685	251,685	256,631
1-24 employees	8,095	16,973	23,838	30,997	37,868	46,953	47,784
25-499 employees	1,743	2,344	2,847	4,337	4,977	5,997	5,732
>500 employees	652	588	508	375	330	310	305

At the end of 1997, there were around a quarter of a million self-employed businesses, and a further 53,000 legally registered small and medium enterprises. Their share of total employment is summarised in the table below, and provides the best basis for comparing with EU States:

Planned Economy Monthly. 5/1989

Table 1.4: Percentage employment distribution 1997 (EU definition of SME)

Number of Employees	% of total employment **in Slovakia**	% of total employment **in EU states**	Employment distribution **Industry**	Employment distribution **Construction**	Employm't distribution **Trade**	Employm't distribution **Transport**
Self employed	21.6		12.6	31.2	67.4	25.0
Micro: 0 - 9	10.6	33.2				
Small: 10-49	7.7	18.9	16.9	18.9	14.4	12.1
Medium: 50-249	19.5	13.5	8.7	23.6	6.7	25.9
SMEs	59.4	65.6	38.2	73.7	88.5	63.0
Large: > 250	40.6	34.4	61.8	26.3	11.5	37.0
Number of employees	2,029,147	111.4m				

Sources: Slovak National Statistics. Fifth Annual Report, European Observatory for SMEs 1997

The steady reduction of employment in large (mainly state owned) enterprises has been offset by the substantial growth in self-employment and micro firms, which together account for 32.2% of employment, similar to EU countries. But the proportion employed in small firms (10-49 people) is significantly lower (7.7%) than for EU States (18.9%).

The self employed and micro enterprises account for the rapid growth in trade and service sectors, whereas the proportion of people employed in small enterprises in the manufacturing sectors remains relatively low.

1.3 Key issues effecting the development of SMEs

The rate of formation and subsequent growth of small firms has been stimulated by market opportunities, declining employment prospects in state owned enterprises, changes in government legislation making it easier to set up a private business, and access to bank credit for growth firms in the period up to 1996.

However, small firm surveys and feedback from various unions and associations of small firms suggest that whilst there have been some improvement in the operating environment since 1989, new barriers have arisen which have made SME development more difficult, despite the growth of the domestic economy:

Table 1.5: Some key barriers facing SME development

Main barriers	**Commentary: how its importance has changed over time**
1. Frequent changes in legislation, particularly relating to tax and social insurance payments	*Changes have become more frequent; Tax Officials and SMEs find it increasingly difficult to keep up to date; interpretation now more difficult*
2. Lack of access to credit for SME development	*Access to bank credit, particularly by start ups and young growing enterprises with a limited track record and collateral, has become more difficult*
3. Administrative burdens due to ineffective internal co-ordination of SME regulations	*SMEs, for example, must make tax, insurance and licence declarations to an increasing number of bodies*
4. Limited awareness of the SME environment in government	*Politicians and senior servants have a low level of awareness of the real operating environment of SMEs and this is not taken into account when framing new policies and legislation.*
5. Tax burden	*SMEs believe that they carry a disproportionate share of the country's tax burden (compared to large firms, many of whom lack the funds to pay taxes)*
6. Lack of transparency	*Corruption is inhibiting SMEs to gain access in a transparent way to markets in Slovakia*

Main barriers	Commentary: how its importance has changed over time
7. Insufficient support from Government for small firms	*SMEs are critical about the very limited tangible support to improve their operating environment*
8. Weak management capacity of many SMEs	*Lack of small business management experience and limited budget available for management training*
9. Lack of experience of most SMEs in export markets	*Need to improve access for SMEs to export services*

Sources: Entrepreneurs Association, Chamber of Commerce, and the National Agency reports

The political support for the SME sector has changed over time. Initially, under the influence of Federation policies, government recognised that support to SMEs was a vital part of developing a market economy. At first, this position was supported by the Meciar government and the short-lived coalition government in 1994. After Meciar's return to power in 1994, it provided increasing levels of support to large firms (flagship enterprise policy), to maintain employment and solvency. Ministers of Economy and Finance, most of whom had previously been in senior management positions in large enterprises, have been more aware of the needs of large enterprises and have had a limited understanding of the potential of SMEs, which some believe could erode the position of large enterprises. This has also reflected their political interest to be seen to be supporting regional and local employment in existing enterprises, rather than providing support to entrepreneurs, most of whom would be more likely to vote for opposition parties; however, shortly before the election all parties expressed support for small firms. Despite this relatively negative environment, the role and importance of SMEs in the Slovak economy has steadily increased.

1.4 Financial market

There has been very limited growth in credit, after taking inflation into account, and this growth has mainly been in foreign currency loans. Whilst credit in real terms increased by 15% in 1996, the overall level fell by 2.2% in 1997. The 'shortage' of new credit has been due to several factors. Deposits have not grown in line with demand for credit. An increasing proportion of credit is tied up in 'temporary illiquid assets and classified/loss making' loans, with over half of the banks' credit portfolio effectively frozen. And in 1997 and 1998 banks have increased their holdings in more profitable government securities, to finance the increasingly large government debt.

Table 1.6: Flows of deposits and credits

SK billions	1993	1994	1995	1996	1997
Total credits (local and foreign) SK B	268.9	272.9	310.8	374.4	388.9
% increase in credit minus inflation	-	-12.0%	-1.6%	+14.8%	-2.2%
% of SK loans as temporary illiquid assets and loss making loans	22%	36%	55%	48%	55%
Total credit allocated to small businesses SK B	11.6	10.8	12.3	12.9	15.1
% of credit to small businesses	4.3%	3.9%	3.9%	3.4%	4.4%
New loans to Slovak private companies SK B	-	6.9	12.4	17.5	12.7

Source: National Bank of Slovakia

Published information from the National Bank of Slovakia on the availability and uptake of credit by SMEs is limited and difficult to interpret. The loan portfolio is dominated by a limited number of large loans to medium and large enterprises; most loans (90%) are in Slovak crowns, of which 40% is short term (under one year), 23% is medium term and 37% is long term.

In December 1997, there were 29 commercial banking institutions in Slovakia (23 in 1993). Three are state banks, 7 are private banks without foreign capital, 14 include foreign participation, and 4 are branch offices of foreign banks. In addition there are nine foreign banks with representative offices. Three large state controlled banks dominate the sector: VUB, IRB and the Slovak Savings Bank, which are strongly under the influence of the government through the National Property Fund. These banks account for 60% of all loans, 70% of deposits and 80% of all branches, and the majority of the bad loans. A recent Trend report (17.6.98) indicated that profits in these state banks, where provisions against bad debts has been substantial, have been very low, despite the substantial increase in interest rate spread: profits in VUB were 1.7% and 1.2% in the Savings Bank. In contrast, profits in smaller banks which have low levels of non performing loans, have been very high: return on capital was 54% in Tatrabanka, 51% in Creditanstalt, and 39% in VUB Wustenrot.

Table 1.7: Summary of the banking structure:

	Bank	Total assets ($m)	Capital ($m)	BIS ratio	Credit rating	No of branches	Shareholders
1*	Savings Bank	5,420	378	Na	BBB	703	Government
2	Vseobecna Uerova Banks	5,371	347	11.1	BB+	39	Government
3	Ivesticna a Rozvojova Banka	1,425	60	<8	BB	49	Private (VSZ)
4*	Tatra Banka	1,017	40	12.4	BBB	27	Private (Raiffeisen)
5*	Pol'nobanka	920	68	9.2	B	16	Private (EBRD)
6*	Istrobanka	653	40	13.7	BB	25	Private
16*	Slovak Guarantee Bank	111	64	Na		5	Government

Source: Phare SME Horizontal Financing Final Report, 1997
* Banks with Phare SME Financial Programmes

Interest Rates

Broadly, average loan interest rates to enterprises fell in line with the discount rate, as inflation fell from 23.2% in 1993 to 5.8% in 1996. However, in 1997, with a sharp increase in government borrowing through Treasury Bills and with limited funds available, interest rates and spreads increased significantly (up from 5.6% to 9.6%) although inflation held steady. In 1997, a total of SK 88 billion (Euro 2.2 billion) of Treasury bills were sold with 1-11 month redemption's yielding 12.6% to 30.6% (average 23.5%). Whilst in 1995 the Phare loans appeared to be appropriately priced, by 1997, they were well below market rates.

Table 1.8 Changes in interest rates over time.

	1993	1994	1995	1996	1997
Treasury bill average interest rate					23.5
Av lending rate (new loans to enterprises)	18.0	19.2	14.9	14.2	21.2
Phare SME Support Loan interest rate	na	na	14.5 - 12.3	11.8	11.8
Central Bank discount rate	9.5	12.0	12.0-9.75	8.8	8.8
Av time deposit rate	12.72	14.2	12.2	8.6	11.6
Av Spread	5.3	5.0	2.7	5.6	9.6
Inflation (CPI %)	23.2	13.4	9.9	5.8	6.1
True interest rate	-5.2	5.8	5.0	8.4	15.1

Source: National Bank of Slovakia

Loan finance for SMEs (around SK 15.1 billion: Euro 400 million)

The proportion of loans, classified as "small businesses" in the statistics collated by the National Bank, has been very low, averaging only 3.4 - 4.4% of loans, with no increase except in 1997 despite inflation and the growth of the small firm sector. At the end of 1997, total bank credit to small businesses amounted to around SK 15.1 billion (around Euro 400 million), of which the Phare loan programmes amounted to around Euro 32 m and contributions from multilateral and bi-lateral donors amounted to a further Euro 180 m (mainly for medium sized enterprises). On the assumption that the size of an average credit to a small enterprise is between Euro 50,000 and 125,000 (SK 2-5 m), banks would have perhaps around 4,000 to 7,500 loans outstanding to SMEs in any one year.

These statistics confirm reports from the Regional Agencies about the severe lack of credit in for SMEs in the last two years. It is in this context that the Phare and other special credit lines should be viewed.

As in most other countries, the primary source of funding for SMEs has been the owners' funds, family and friends and trade credit. Before 1993, several Banks did develop lending programmes for small firms; but because credit appraisal procedures for small firm lending were not well developed, they incurred losses. New appraisal techniques have been progressively introduced, but loans to small firms have become progressively more difficult to obtain, particularly by 1997, with the increase in Treasury Bill auctions. This is illustrated by the case study of the Savings Bank, the largest partner in the Phare SME Loan Programmes.

Savings Bank (the largest partner in the Phare SME Loan Programmes)
The Savings Bank's lending policies to small firms changed significantly towards the end of 1996. Up till then, the Savings Bank would consider applications for short and long term loans to clients who have banked with them for at least 2 years. Increases in credits to customers fell from SK 11.5 billion (Euro 290 million) to SK 3.9 billion (Euro 100 million) in 1997, due to the switch in funds towards Treasury bills which increased by SK 5 billion (Euro 130 million) in 1996 and SK 13.4 billion (Euro 350 million) in 1997. Because new deposit income fell from SK 9.5 billion (Euro 250 million) to SK 3 billion (Euro 78 million) in the same period, the Savings Bank, which is a prime source of funds on the interbank market reduced its level of interbank funds by SK 13.5 (Euro 350 million) in 1996 and a further SK 8.9 billion (Euro 230 million) in 1997.

Between 1996 and 1997, interest on customer loans reduced from 17% to 12%, whereas the return on money market activities increased from 14% to 19%, and the average returns on Treasury Bills increased from around 10% to 13%. As a result the proportion of earnings from loans to customers has reduced from 44% to 28%, and income from Treasury bills and securities has increased from 21% in 1996 to 35% in 1997.

There are clear signs of crowding out, due to the combined effect of a large number of non performing loans with state enterprises, and increased more profitable lending to the government. In this situation, banks have tended to allocate the reduced level of credit to large enterprises and the utilities (encouraged by the Government as well as pressure from large enterprises faced with serious cash flow problems) rather than to the small firm sector, where they perceive the risks to be higher.

This position is unlikely to change until the Government deficit is reduced to acceptable levels and international confidence has been regained enabling Slovakia's largest enterprises to raise money more economically on the international money market. This will result in an increase in the availability of local credit and lower interest rates, 'affordable' by small and medium enterprises. The table below summarises our assessment on the current availability of fund to SMEs (excluding foreign loans):

Table 1.9: Availability of market based sources of finance by SMEs (excluding donor-supported sources)

	Start ups and micro firms (1-9 people)	Small enterprise (10-24 people) less than 3 years old	Small enterprise over three years old	Medium sized enterprise
Short term funds	Never	Occasionally	Possible	Possible
Long term funds	Never	Never	Occasionally	Possible
Guarantee	Never	Never	Occasionally	Possible
Leasing	Exceptional	Occasionally	Possible	Possible
Equity capital	Exceptional project	Occasionally	Occasionally	Occasionally

Source: Consultant's assessment

Whilst availability is the major problem, there are other reasons why accessing bank credit has become progressively more difficult for SMEs, which are summarised in Table 2.5 below:

Table 1.10: Primary reasons for financial problems

Reason	Commentary
Lack of track record	Enterprises without an established relationship with their bank are less likely to be able to secure a credit. Start ups and enterprises under two years old are especially vulnerable
Level of collateral	Normally collateral of at least 130-150% of the loan is regarded as essential. Much depends on the property circumstances of the owners of the enterprise. There is evidence that some banks are reluctant to accept family apartments.
Interest rate	'Market' interest rates can generally only be afforded by trading companies requiring short-term loans. When a long term credit is used for an investment project, small enterprises (particularly start ups) have great difficulty in meeting these high interest payments until sales have been fully established
More profitable deals elsewhere: lack of competition	With more profitable deals elsewhere, banks, particularly those that have incurred large bad debt portfolios, and are only just profitable, are reluctant to lend to small enterprises. The reasons given include higher management costs, greater risks and lack of track record.
Previous poor experience of banks	Banks now generally recognise that lending to small enterprises is more difficult.
Lack of credit management skills	Banks loan appraisal and credit management skills and procedures have improved in the last three years. This is generally not a major limitation.

Source: consultant's assessment based on feedback from banks, the National Agency and unions of entrepreneurs

Leasing (SK 16.7B -Euro 445 million - in 1996 to all sectors)

In 1996 leasing contributed an extra SK 16.7 billion (4.4%) to the supply of credit to the private sector. There are about 50 companies offering lease finance, with 60% of the market dominated by five companies. Leasing has grown rapidly from SK 3.5 billion (Euro 90 million) in 1994, to SK 6.0 billion (Euro 156 million) in 1995 and SK 16.7 billion (Euro 434 million) in 1996. Cars account for 58%, equipment and machinery 25%, lorries 8% and computers and office equipment 6%. Though the civil and trade codes do not explicitly cover leases, they do include provision for a hire contract with a purchase option. Provision is however made for leases both within the laws covering Income Tax and Value Added Tax.

Guarantee Funds (SK 1.4 billion for SME credits: Euro 37 million)

The Slovak Sate Guarantee Fund was established by the Ministry of Finance in 1991 to manage a number of financial programmes including the provision of guarantees for SMEs and agricultural enterprises. Significant funds have been channelled by the Ministry of Economy to the Guarantee Bank in the last four years. Five SME related funds provided guarantees to 439 enterprises totalling SK 1.4 billion (Euro 36 million) at the end of 1996: average value was SK 3.2 million (Euro 85,000). The Phare funded Guarantee Scheme is reviewed in Section 2.2 and summarised in table 2.4 below. In addition there are two agricultural guarantee schemes (SK 1.9 billion: Euro 500 million) and four special purpose guarantee schemes (SK 1.5 billion: Euro 40 million). A separate USAID guarantee programme (around $3 million) covering loans up to $150,000 is managed by Tatrabanka

Equity, Venture Funds and Capital Market (around Euro 110m available: all sectors)
Several funds with access to foreign capital are operating in Slovakia. The majority (see table 2.9 for full list) are orientated towards medium sized established enterprises where the deal size is typically in excess of Euro 0.75 to 1m. Only two funds have been designed to invest in start ups and smaller enterprises, the Seed Capital Co, a subsidiary of the National Agency with funds from Phare (reviewed in Section 2), and a regional investment fund, PKPF, operating in the Zilina area. The culture of venture funding is still rather new. Its success depends on building up a number of case examples and developing alternative exit routes for the funds. The capacity of Bratislava Stock Exchange is still very limited and does not yet perform a role for raising funds. Unrelenting high interest rates resulting in a lack of liquidity in the capital market have undermined the price setting functions of the Stock Exchange.

Credit Unions/ Mutual Support Credit Institution (at planning stage)
Slovakia was the earliest country to start credit unions, the first financial co-operative being formed in 1845. These survived until 1952 when they were absorbed into the Savings Bank. Because of the centralised structure of credit institutions in Slovakia, there is now a renewed interest in setting up credit unions to fill a financial gap amongst the smallest SMEs and the personal sector. A pilot project in Detva, initiated by the National Agency, is being considered, but progress is dependent on new legislation and support from SME bodies. Whilst the Slovak Union of Craftsmen has backed the proposals, initial support from individual RAICs appears to have been more limited, despite the importance that both bodies place on improving access to credit.

1.5 Legal and Regulatory Issues effecting Finance for SMEs

Table 1.11 reviews the most important regulatory and legal issues affecting the provision of finance to small firms.

Table 1.11: Regulatory and legal issues effecting finance for SMEs

Area	Commentary
Transparency	Connections still play a significant part in deciding whether an enterprise should receive a credit. In general, most large firms are better connected than small enterprises, unless the owner manager had previously occupied an influential position in a large enterprise. Banks are protected as the banking act provides for confidentiality to be maintained between the bank and its clients.
Accounting systems and requirements	Most accounts prepared by SMEs are structured to minimise taxation and may not include a full disclosure of income and an overstatement of costs. Consequently, it can be very difficult for financial institutions to assess the financial performance of SMEs. Only joint stock companies and enterprises whose sales exceed SK 40 million (Euro 1 m) must be audited. Local audits are significantly below international standards. Double or single entry book-keeping systems are required depending on the status of the enterprises,
Corporate income tax	40% rate. Assessment has proved to be difficult due to frequent changes in legislation.
Banking services	With the exception of deposit taking (covered under the civil code) all other services are covered under the Commercial Code. But there is a lack of legal regulation relating to provision of mortgages. Consequently there is an absence of commercial mortgage finance for property investments.

Area	Commentary
Bankruptcy arrangements	The bankruptcy arrangements are not functioning. Following recent changes in legislation, the number of bankruptcy claims have increased but the courts are overloaded, and proceedings are taking several years. Up to Oct 1997, 4,000 bankruptcy claims had been registered, out of which 143 had been before the court and one case finished. There have been 10 amendments to the basic law on bankruptcy and settlement, the main effect of which has been to postpone bankruptcy claims. The 1997 Revitalisation Act protects firms, determined by a government appointed Revitalisation Committee from bankruptcy. But no revitalisation project has been approved. In a 1997 amendment, proceedings against those not protected by the Revitalisation Act (mainly small enterprises) will be speeded up. Small firm associations are arguing that the present arrangements discriminate against small firms.
Collateral	The recovery of physical assets pledged as collateral for bank loans is proving to be very slow: typically up to two years. Banks are reluctant to accept the family house as collateral due to problems of recovery and resale. This is a serious problem for entrepreneurs with few other assets.

1.6 Institutional Developments

Ministry of Economy: since the formation of Slovakia, the Ministry of Economy has taken the lead for SME Policy. The department for SME and Regional Development consists of the Head of Department and 6 staff (nominally 3 on SMEs and 3 on regional development), which reports through the General Director to a State Secretary whose responsibilities span industrial policy, science development and commercial policy. The Secretary of State was the Head of the National Agency and is now Chairman of its Board of Trustees, the General Director is a Board member, and the Head of Department was involved in the establishment of the Agency in 1993.

Although several senior staff in the Ministry are now well informed on SME issues, key politicians (Ministers of Finance and Economy), in almost all cases, have been drawn from senior managerial positions in large state enterprises. It is important, therefore to recognise that the main focus of the Ministries of Finance, Economy and Labour have been orientated towards solving problems relating to the macro economy and the complicated economic and social issues surrounding Slovakia's largest enterprises rather than focusing on the economic development opportunities offered by SMEs. Whilst there is general acknowledgement of SMEs, there has been little confidence that SME development can play a major role in the restructuring process.

Whilst the Ministry of Economy has the prime responsibility for SME development a number of other Ministries also play a significant role, but there is little or no co-ordination between these bodies:

Ministry of Finance: its impact on SME development has been very considerable through taxation, pricing and monetary policies and the detailed regulations relating to their implementation; but there is little evidence any special consideration is given to SMEs when these policies and regulations were drawn up. The Ministry of Finance is also responsible for the overall supervision of Slovak Guarantee Bank, which includes several credit guarantee and financial support programmes for SMEs

Ministry of Labour, Social Affairs and Family: the Ministry has a substantial Fund for Employment (financed by a 1% salary tax paid by employees and 3% by employers 3%). 70% of this fund is for new job creation (interest free refundable and non-refundable grants) managed through the 79 District Labour Offices. This includes a provision for unemployed people to obtain limited financial support to help set up a business. The Fund also supports

CEPAC, a training foundation which has contracts with several of the RAICs to run full time 10-week courses for unemployed people wishing to start up in business.

Ministry of Agriculture: has a number of programmes to support agriculture and food processing enterprises.

Ministry of Interior: the Ministry is responsible for all licence and trade registration of legal and physical persons wishing to conduct a business. It is also responsible for the work of the District and Regional Administrations, which include sections engaged in planning and infrastructure development.

Ministry of Foreign Affairs has responsibility for co-ordinating foreign multilateral and bilateral assistance.

Office for the Regions, Science and Technology is responsible for regional development policies and is engaged in drafting new proposals for setting up a National Agency for Regional Development, as well as being the main interface with the European regional programmes.

Co-ordination of SME policies and programmes between the Ministries is recognised as being weak. As part of the Government's 1997-2000 State Medium Term SME Support Policy, which was agreed in 1997, the Ministry of Economy is committed to establishing a Slovak Government Council for SMEs to improve co-ordination, but it has not yet been established.

Some of the key institutional developments are summarised in Table 1.12 below:

Table 1.12: Institutions, policies, laws and regulations impacting on SMEs

Area	Summary	Impact on SME Sector
Institutional development	Slovakia Guarantee Bank set up in 1991 Department for SMEs set up in Ministry of Economy in 1993 NADSME set up in Feb 1993 Export Information Centre set up in 1998	Important channel for managing government financial programmes to SMEs Primary point of reference in government Executive Agency to implement SME programmes Executive Agency for export programme
Government funding for SME sector	Annual Budget for SMEs, channelled through NADSME and the Slovak Guarantee Bank (SGB), which also manages a range of other guarantees and interest rate subsidies to entrepreneurs, on behalf of several government departments	**Funds NADSME SGB** 1993 SK 30.7m SK 843m Euro 0.8m Euro 22m 1994 SK 316.8m SK 580m Euro 8.2m Euro 15m 1995 SK 665.8m SK 1267m Euro 17m Euro 33m 1996 SK 68.6m SK 1115m Euro 1.8m Euro 29m
Other SME related legislation	1995. Act defining SMEs and providing powers to Ministry of Economy to provide financial support to SMEs 1997 State Medium Term Support policy of Ministry of Economy 1998 SME section in Acquis Communitaire	Confirms government powers and recognises that SMEs are a distinct group First formal commitment by government in relation to SMEs Defines Government action programme for the development of SMEs

Area	Summary	Impact on SME Sector
Regional policy developments	1996 Law leading to the setting up of 8 regional administrations. Regional development co-ordinated through the Office for Regions, Science and technology Pilot RDA set up in Zilina and extended to small RDAs in 6 other areas. A National Regional Development Agency and new arrangements in each region are expected to be set up with the capacity to manage the EU Structural Funds.	It will be important that close working relations are developed with NADSME and the RAICs to ensure that SME programmes are fully integrated into the new regional development strategies
Commercial legislation:	General framework for enterprise given in Commercial Code (1991), Civil Code (1991) and Trade Licence Business Activities (1991)	These define procedures for forming a business as a private person or as a legal entity and provide a framework for contracts. SME bodies have identified a number of changes to improve and clarify these key acts.
Tax laws and regulations	Little progress has been made to influence the Ministry of Finance and the various taxation bodies to improve the tax environment for SMEs	A more structured approach, focusing on a limited number of important issues supported by research to justify the proposed changes will need to be taken.

1.7 Representation and lobby network

SME interests are represented through a number of associations, including:

- Entrepreneurs Association with around 18,000 members (of which around 9,000 are members of 26 other bodies which are collective members of the Association)
- Slovak Union of Tradesmen, which include a number of specialist guilds and tradesmen's societies
- Slovak Union of Small Business Owners
- Slovak Chamber of Commerce and Industry. Current membership of 3,800 (2040 paying members) drawn from enterprises on the Commercial Register
- Slovak Chamber of Agriculture and Food (complementary body for agriculture and food production
- Employers Association: an umbrella body representing public bodies and private sector employers

A review undertaken in 1997 by Enterprise plc (formerly Lancashire Enterprises) with support from the British Know How Fund concluded that 'lobbying and representation on behalf of the SME sector is inconsistent, uncoordinated and unfocused. While successful in some limited instances, it is far less effective than it could or should be....' The study identified a number of reasons for the ineffectiveness of these bodies:

- issues reflecting the self-interest of the bodies without taking into account wider economic and social issues.
- lack of anybody within government with the authority to influence the operational behaviour of government's own organisational network - the ministries
- overlap, competition and poor co-ordination between representative bodies
- lobby bodies have a poor understanding of how to engage and use the press and media
- poor research to support and substantiate the case for change

- attempting to cover too many issues rather than concentrating on a limited number of high priority issues
- poor understanding of the machinery of government, and limited contact network
- a need to clarify and redefine the role of the National Agency so that it can play a more effective part

Some of the primary barriers identified by representative bodies include:
- rapid changes, particularly in relation to tax legislation and regulations. Some items have been changed 4-5 times in a year
- poor drafting of tax legislation resulting in serious differences in interpretation, particularly in the areas of income tax, import duties, deposits and surcharges, so that charges are hard to predict, even by experts.
- lack of transparency: public bodies have arbitrary powers to waive import surcharges and sanctions for non payment of taxes etc, which small firms believe favours large enterprises
- additional administrative burdens on small firms arising from declarations and payments to different bodies (e.g. the need to make payments of health insurance, social insurance, employment fund to separate bodies)
- new legislation which, it is claimed, will have a negative impact on SMEs (e.g. Acts on Public Procurement, and the Fund for the Support of Foreign Trade)
- entrepreneurs complain of excessive taxation, which reduces motivation and reduces their capacity to make new investments utilising retained profits.
- the relative tax treatment of natural persons and legal entities

Neither the Ministry of Economy nor the National Agency believes that they have the brief or the capacity to scrutinise proposed and new legislation to assess its impact on SMEs. This is largely undertaken by the representative bodies with the support of external advisers normally working on a voluntary basis. Due to the reactive nature of much of this work, if a problem is identified it is often too late for modifications to be included in the legislation.

1.8 The National Agency for the Development of SMEs (NADSME)

The National Agency for the Development of SMEs (NADSME) was set up by the Ministry of Economy in 1993 to act as a co-ordinating body for all activities aimed at supporting the development of SMEs. The National Agency was established as a non profit foundation by the Ministry of Economy and in 1997 transformed into an Interest Association of Legal Entities, with a membership which includes the Ministry of Economy and seven associations of entrepreneurs. At present it is controlled by a Board of Trustees with representatives from the Ministry of Economy (2), the Entrepreneur Association (1), the Union of Crafts (1), Slovak Chamber of Commerce and Industry (1), Slovak Association of Entrepreneurs and Managers (1), the Union of Towns and Villages of Slovakia (1), Slovak Union of Consumer Co-operatives (1), Association for the Protection of Rights and Interest of Entrepreneurs (1), Ministry of Finance (1), Slovak Union of Productive Co-operatives (1).

The National Agency has a staff of 30, organised in six departments each with a Director covering the following areas:

Co-ordination: (Staff 1+4) with people engaged in:

- the development of SME policies, legislative work, and support to unions and associations of entrepreneurs to strengthen their representation and lobby roles (one person see section 1.6 above);
- the preparation of information booklets for entrepreneurs; and
- the Spin Off Programme (two people - see below)

Regions and Education: (Staff 1+2) responsible for developing the Regional Advisory and Information Centres and Business Innovation Centres (see below) including:
- their establishment;
- professional development;
- financial support; and
- performance monitoring

Financial Support Programmes: (Staff 1+2) responsible for the analysis of financial problems facing SMEs and the monitoring of financial programmes to address these gaps including
- the support loan programme;
- the small loan programme;
- loan guarantees;
- seed capital; and
- micro credit. (see Chapters 2 and 3)

Economy and Administration: (Staff 1+5) responsibilities include:
- the work of the PMU for Phare funds for SME development;
- accounting;
- personnel; and
- administration.

Information and International Activities: (Staff 1+6) responsibilities include
- the Euro Info Correspondence Centre (3 staff)
  - participation in Europartinariat, Interprise and other foreign and domestic events,
  - the development of business information system covering the products and services offered by Slovak entrepreneurs, and three involved in
- the computer network, DTP and internet services. (3 staff)

Subcontracting Exchange of Slovakia (SES). (Staff 1+3+2 P/T)
This programme is designed to increase the flow of subcontract work from foreign customers, particularly in engineering and light industries.

1.9 Regional Advisory and Information Centres (RAICs) and Business Innovation Centres

With the active encouragement and support of Phare, a network of Regional Centres has been established. Three pilot Regional Agencies and one Business Innovation Centre were set up in 1992 as part of the Federal SME programme, co-ordinated from Prague. Between 1993 and 1996 the network was expanded to 12 RAICs and 5 BICs, (less the Bratislava BIC which ceased to get financial support from the National Agency/Phare after 1996).

Each Centre covers, on average, around 1,350 companies and around 9,100 self-employed businesses in an area of 7,300 sq km and a population of 200,000 people. The smallest Agency in Komarno covers 2,200 sq km with a population of 110,000; the Agency serving the largest population (outside of Bratislava) is in Povazska Bystrica in the north (population: 483,000), and the Centre in Koscise in the East, where there is also a BIC, covers the largest area - 239,000 sq kms. The larger and longer established centres have opened branch offices to improve local coverage: two agencies have two, and four have one branch.

RAICs have been established as separate legal entities as Associations, with partners drawn from locally based organisations with an interest in SME development. The box below summarises the membership of RAICs in 1996:

Members of the 12 RAICs	
Elected municipal authorities	15
State administrations (district authorities)	8
Banks	8
Enterprises	21
SME associations and unions	7
Others (mainly educational institutions)	8
Total	**73 bodies**

Source: National Agency survey of RAICs undertaken in 1996

The four National Agency/Phare funded BICs offer a similar range of advisory and information services as the RAICs, but also provide incubation facilities. In several instances, their programmes include the provision of support to innovative start-ups, particularly those housed in the incubator. The fifth BIC based in Bratislava, also received funding from Phare via the National Agency. But this was discontinued in 1997 after the 1996 Phare Evaluation of the SME Programme, though the exact reason does not appear to be very clear, and may have been based on a misunderstanding. The Bratislava BIC is recognised by EBN and is also the Correspondent for the Relay Centres under DGXIIIs programme. It appears to have played a valuable role in helping other BICs to develop programmes to encourage innovative start-ups. There is now a need for Phare and the National Agency to review the decision to exclude the Bratislava BIC from the network.

Chapter 2 Phare Programmes for SME Development

2.1 Introduction

From 1990 to 1993, Phare programmes were drawn up with the Federal government of Czechoslovakia in Prague, but in 1993, the Slovak programmes were divided and run from Bratislava. A total of Euro 173 million has been committed to Slovakia up to the end of 1997, which included Euro 32 million for SMEs and small additional allocations for regional development and export programmes which will also benefit SMEs but have not been included within this evaluation. The allocation for SME programmes is summarised in table 2.1 below:

Table 2.1: Allocations to SME Development in each Financial Memorandum

Programme '000 Euro	1991	1993	1994	1995	1997	Total
Financial	4,000	5,250	2,000	5,720	7,000	23,970
Institutional	3,327	1,750	250	1,280	1,500	8,107
Total	7,327	7,000	2,250	7,000	8,500	32,077

Note: there was no allocation to SME Development in FM 1992, and there was no Financial Memorandum for Slovakia in 1996.

2.2 Phare Financial Programmes for SMEs

The objective of the Phare financial programmes as set out in the 1993 Financial Memorandum (covering guarantee, seed capital and funds for small loans) has been to increase the availability of capital to SMEs, due to the lack of liquidity in the banks, particularly to support long term investments and the lack of personal savings by individuals. A second objective was be to increase the capability of banks to provide SME services. Technical assistance would be provided to assist banks and their branches to assess the viability of business plans from SMEs, appraise loan applications and monitor loan repayments. Initially the focus was towards the provision of finance to SMEs with investment projects. In 1995, the scope was extended to cover micro credit for start-up businesses. At the design stage particularly in the early period, importance was placed on achieving a high disbursement rate.

Table 2.2 summarises the allocation of funds for SME financial projects and the date when disbursement commenced.

Table 2.2: Financial programmes included in the Phare Financial Memoranda

Date allocated	Summary	Allocation	When disbursed
FM 1991	Guarantee Programme Small Loan Programme	3 m 1 m	1992 1994
FM 1993	Support Loan Programme Seed capital programme (Seed Capital Co) Know-how support for banks: Bank Windows Programme Know-how support for Mutual Support Credit Institution (Credit Union)	3.35 m 1.0 m 0.7 m 0.2 m	1994 1995 1996/7 1996/7
FM 1994	Support Loan Programme	2.0 m	1995
FM 1995	Support Loan Programme Seed capital programme Micro-credit programme	5.2 m 0.3 m 0.22 m	1996 1998 1997

Date allocated	Summary	Allocation	When disbursed
FM 1997	Support Loan Programme Seed capital programme Micro-credit programme + TA/3 and TA/4	5.2 m 1.0 m 0.8 m	Not released Not released Not released
Total		23.97 m	

The main feature, inputs and outputs of each of the financial projects are summarised below:

Small Loan and Support Loan Programmes (allocation: Euro 16.75 m)
The Euro 1 m Small Loan Programme was launched through the Savings Bank in April 1994 after the National Agency for Development of SMEs had been established. Following rapid take up, the first phase of the larger co-funded Support Loan Programme was launched with three banks at the end of 1994. The loan size was increased from SK 800,000 (Euro 20,000) to SK 5 million (Euro 130,000) and the criteria were extended from 25 to 500 employees. The object was to fund longer-term investment projects most likely to contribute towards the restructuring of the Slovak economy following the scaling down and closure of many large enterprises. It also included provision for co-funding by the government and the participating bank, achieving a 2 to 1 gearing on Phare funds. There was an expectation that a revolving fund of Euro 75 million (SK 30 b) would be created with each party contributing five tranches of Euro 5 million. Due to pressures on government funding and the lack of the 1996 FM, only two phases have been implemented, and the third phase funding of Euro 5.2m, part of the 1997 FM is expected to be released shortly.

Table 2.3: Summary of inputs and outputs of Phare Loan Projects

Type and size of fund, date set up, partners	Terms of finance available	Uptake: Criteria and number of clients etc
Small Loan Fund. • Euro 1m (SK 40m) allocated from FM 1991 as a revolving fund • Run by NADSME through Savings Bank. • First loan in April 1994 • Ownership: NADSME	• Loans of up to Euro 20,000 (SK 800,000) • Lending in SK, exchange risk covered by project • Losses covered by NADSME • SMEs up to 25 employees • Investment projects. • Repayment up to 5 years • Nat. Bank discount rate + 2.5% • 100% collateral required • All projects reviewed by the RAIC as part of bank appraisal.	• Loans fully dispersed by Aug. 1994 • 59 clients. • Now, total of Euro 1.8m lent (180%) to 133 clients. • Average loan 13,500 Euro (SK 540,000). • Bad debts: 19 cases, 14.3% of loans made
Support Loan Programme. • Euro 10.55m (SK 200m) allocated from FM 93-95 and a further Euro 5.2m from FM 97 (not released) • Revolving fund with matched funding from the Government and the partner bank (Savings Bank 1994, Tatra Bank in Dec 1994, Istrobanka in April 1996 and Pol'nobanka in Oct 1996). • Total funds: Euro 31.7m (SK 1200m), + a further Euro 15.6m to be released • Ownership of Phare funds: NADSME	• Loans of up to Euro 125,000 (SK 5m) • Lending in SK, exchange risk covered by project • 46.7% of losses taken by NADSME and 53.3% by bank • Investment projects • SMEs with up to 500 people • Repayment up to 5 years • Nat. Bank discount rate +2.5% • Minimum 83% collateral • All projects reviewed by the RAIC as part of bank appraisal	• Total of Euro 44m (SK 1,789m) lent over the period, • 146% of initial sum. • 591 clients. • Average loan: Euro 74,400 (SK 3m). • Bad debts: 75 cases, 12.7% of loans made.

Guarantee Programmes (allocation: Euro 3 m)

The overall framework for Phare's Financial programmes date from the 1991 Financial Memorandum, developed for Czechoslovakia as a whole which included Euro 4 million for financial programmes in Slovakia. When the split took place in 1993, the first of the two guarantee schemes with the Slovak Guarantee Bank was in operation. The second guarantee programme intended for micro loans was eventually merged with the first loan programme. Uptake since has been very slow with only 30% of the fund utilised to date.

The Phare guarantee programme was established under an agreement between Phare, the National Agency and the Slovak Guarantee Bank to overcome the lack of collateral faced by SMEs during the early stages of their development. Phare and the Government made contributions resulting in a fund of Euro 5 million enabling guarantees of Euro 15 million to be made, covering up to 75% of bank loans to enterprises under two years old employing less than 100 people.

Table 2.4: Summary of inputs and outputs of Loan Guarantee Project

Type and size of fund, date set up, partners	Terms of finance available	Uptake: Criteria and number of clients etc
Loan Guarantee Scheme. • Euro 2m in 1992 (FM 1991) and Euro 1m in 1993 (FM) • Matched government funds creating Euro 6m fund (SK 240m) at Slovak Guarantee Bank • Guarantee capacity of Euro 17.6 m (SK 704m). • First guarantee in Nov 1992. • Ownership of Phare funds: NADSME	• Guarantees to SMEs with less than 100 employees • Up to 75% of loan principal (Euro 300,00: SK 10m) • Guarantee fee is 1% for short-term loan, 1.5% for medium term and 2% for long-term loan. • Available through 15 banks	• Guarantees provided since Nov 1992. • 30% of fund utilised. • 110 guarantees made. • Average length: 3.31 years. • Average value: Euro 48,000 (SK 1.9).

Micro-credit Programme (allocation: Euro 220,000 + 800,000)

Because entrepreneurs frequently have little or no funds and a lack of any external sources for start ups, provision was made in the 1995 FM for a pilot Micro-credit programme in three regions, (SK 300,000 - Euro 7,800 loans repayable over three years) to be expanded in subsequent years if it proved successful. Due to delays in implementation, the first loans were not made until March 1997. A further Euro 800,000 has been allocated to the Micro-credit programme from the 1997 FM, subject to an evaluation of the pilot programme, which has recently been completed.

The Phare pilot micro credit scheme (worth Euro 220,000 from FM 95) was launched in March 1997 through three Regional Centres. The fund was fully dispersed in 12 months. From 109 applications, 47 loans averaging Euro 6,800 for up to three years at an interest rate of 8.8%, based on the National Bank's discount rate + 1.5%. No failures have been reported to date. Technical assistance for the design of the scheme was funded by the British Know How Fund. The scheme is managed by the RAICs each, of which have appointed a fund manager to appraise the application and a loan committee made of people from five separate organisations. The loan committees consider regional needs, additionality, the reports of the fund manager and, in two centres, a separate financial appraisal prepared by the local bank's credit officer. Decisions to lend require a two-thirds majority.

Table 2.5: Summary of inputs and outputs of Phare micro loan project

Type and size of fund, date set up, partners	Terms of finance available	Uptake: Criteria and number of clients etc
Micro loan Programme. • Euro 220,000 (SK 8.3m) allocated from FM 1995 • Run by NADSME through three RAICs. • Started in March 1997 • Ownership: NADSME	• Loans from Euro1,200 to 7,000 (SK 50-300,000) • Exchange risk and losses taken by NADSME • SMEs with less than 10 people • Repayment up to 3 years • Nat. Bank discount rate +1.5%. • 100% collateral required	• Loan fully dispersed between 3/97 and 6/98. • 109 applications and 47 loans to clients in Povaska Bystrica, Presov and Zvolen. • Average loan size Euro 5,800 (SK 226,500)

Venture Capital (allocation: Euro 2.3 m)

To facilitate the development of a venture capital fund for start ups and young SMEs with growth potential, the Seed Capital Co was set up as a subsidiary of the National Agency with an initial grant of Euro 1 million from Phare (FM1993) and Euro 300,000 (FM 1995). A further Euro 1m has been allocated but had not been released at the time that the fieldwork for this evaluation was being undertaken.

The company was launched in October 1995 to make small equity investments up to Euro 75,000 (SK 3m) in small enterprises. The company, which has offices in the National Agency, is run by a staff of two fund managers and an administrator. Total annual running costs of Euro 95,000 were covered in the first two years by the Phare grant, and, in 1998, from interests, fees and dividends. The main sources of enquiry were from the company's own marketing and media stories (65%). Enquiries from the National Agency loan programmes (16%) and the RAIC network (15%) were rather low. From 218 completed business plans, 11 investments totalling SK 27 m (Euro 720,000) have been made in 7 companies, including 4 second round investments.

Table 2.6: Summary of inputs and outputs of Phare support for venture funds

Type and size of fund, date set up, partners	Terms of finance available	Uptake: Criteria and number of clients etc
Seed Capital Co • Euro 1 m (FM 1993) + Euro 300,000 (FM 95) + Euro 1 m (FM97) not yet released • Subsidiary of NADSME. • Company set up in Dec 1994 Operational in October 1995 • Ownership: NADSME	• Equity and loans of up to Euro 1.2 m (SK 5m) in SMEs with less than 200 employees. Target IRR sought is 20%. • Exchange risk and losses taken by the Seed Capital Co	• 14 investment projects: • Euro 1.2 m (SK 48m) 92% dispersed • 8 companies. 4 start ups and 4 existing businesses. • Amount written off to date: Euro 85,100 (SK 3.4m)

Know-how Support (allocation: Euro 0.9 m)

There were two main know-how support programmes covering the financial programmes. The Bank Windows project was intended to provide know-how for a one-year period to the partner banks during the introduction of the Phare loan programmes. A second project involved a one-year pilot project to look at the feasibility of setting up credit unions in Slovakia. In addition there were small allocations to help prepare the Business Plan and subsequent training of staff of the Seed Capital Co, and commission evaluation studies of the Seed capital Project in 1997, the guarantee fund and the pilot micro credit projects in 1998.

2.3 Other donors

All loan schemes and most of the equity programmes from other donors have been geared to medium sized established enterprises, generally with export earnings, requiring funding in excess of SK 5m (Euro 120,000). Other than Phare, there are no other programmes geared to meeting the needs of start ups, micro firms and small enterprises requiring less than Euro 120,000. With the Phare programmes, there is no exchange risk (as the funds are transferred to the National Agency and are held in their balance sheet in local currency) and the credit risk is being shared between the commercial bank and the National Agency; in all the other programmes, the international funding institution has provided funds on the basis that the credit risk should be taken by the commercial bank and the exchange risk by the end client, rather than the National Bank or the external donor/bank.

Table 2.7: Summary of main programmes of other donors

Donor, date set up, size and type of fund, partners	Terms of finance available	Uptake: Criteria and number of clients etc
LOAN PROGRAMMES (allocation of Euro 180m)		
EIB Apex Global Loan I (Euro 28m) and II (Euro 50m in 1995). 15-year sovereign loan with the National Bank, which has on lent the fund to VUB and Tatrabanka.	• Loans in Euro from Euro 40-20 m at LIBOR + . Credits must not exceed 50% of the project cost. Usual collateral required	• At end of 1996, Euro 22m (80% of Apex 1) disbursed • 5 projects: cellulose/wood pulp, pharmaceuticals, sanitary, electronics and materials. • Av loan: SK 180m (Euro 4.3m).
EXIM Bank of Japan. Two Step Loan 1. $42m contracts with four banks: VUB, CSOB, Tatra, Pol'nobanka Two Step II. $42m contract with 7 banks Two Step III Credit line signed in 1997	• Loans of up to $5m (SK 165m) to SMEs up to 600 employees, which must contribute 30% of the funds. • Up to 8 years at National Bank discount rate + 4.75 %	• At the end of 1996, JEXIM I fully dispersed. 211 projects. Average loan size: SK 7.5m (Euro 180,000) • JEXIM II. 52% dispersed. 72 projects. Average SK 13.8m (Euro 330,000)
EBRD Credit Line (up to DEM 30m) with Istrobanka and Tatra Banka (DEM 15m)		
Slovak American Credit Program $3m provided with matching money from Pol'nobanka	• Loans from SK 600,000 to 7.5m (Euro 14,000 to 180,000) for SMEs. Up to 5 years at National Bank discount rate + 3.2%	• At the end of 1996, $2.7m dispersed. 27 projects. Average $100,000 per project (SK 3.3m)
EQUITY and LOAN PROGRAMMES (allocation of Euro 110 m)		
Slovak American Enterprise Fund	• Equity and loan capital of SK 10 to 50m (240,000 to Euro1.2m)	• At the end of 1996, $22m dispersed. 30 projects. Average $730,000 per project (SK 24m)
US Small Loan Scheme $3.5m	• No details	• Fully dispersed to 32 firms. Average SK 3.6m (Euro 85,000)
Post Privatisation Fund. Euro 30m EBRD, Euro 12m Phare (privatisation programme) and 1.3m Euro Slovak Government Managed by Framlington/CET under contract since late 1996	• Equity and loan capital in the range of Euro 1-5m (SK 40-200m)	• 3 investments in 1997, 10 active projects, 12 projects on hold.
Advent private Equity Fund, managed by Advent Management Slovakia Euro 2.0	• Equity and loan funds for quoted and unquote companies	

Donor, date set up, size and type of fund, partners	Terms of finance available	Uptake: Criteria and number of clients etc
Povazsky A Kysu Podnikatsky, based in Zilina. Fund. Euro 1.5 with Phare support, (regional programme). Firms in North Central Slovakia	• Equity and loans for start ups and expanding firms • Euro 132 -530,000 (SK 5 - 21m)	
Tyn Fund $38m	• Equity and loan capital: • Min $1- 10m (SK 33-330m)	
GUARANTEE FUNDS		
Slovak Guarantee Bank	• Range of guarantee funds for SMEs	
USAID Loan Portfolio Guarantee Programme, managed by Tatrabanka	• Up to $3m per bank. 50% guarantee, (70% with microloans) on loans up to $150,000 at a fee of 0.5 + 1.5-2.0% utilisation fee	

2.4 Phare support for institutional development

The objective of Phare's institutional programmes has been to improve the environment for SME development by focusing on the legal and regulatory environment and better access of SMEs to knowledge and information.

Phare has supported the development of new institutions to service the needs of the SME sector involving:
- the establishment and development of a National Agency to co-ordinate this work, undertake national SME support projects relating to regulatory issues, lobbying and representation work and the provision of specialist support services to SMEs,
- the setting up of a network of Regional Advice and Information Centres and BICs, providing services to start ups and small firms.

The decision by the new government to set up a National Agency for SME Development, shortly after the partition of Czechoslovakia in 1993 was a turning point for support for SMEs in Slovakia. It was supported from the outset by Phare, who have been the primary source of funding (and influence) both for a central agency and a network of business advisory centres. Steady support by Phare has provided the continuity and security that the National Agency required to get established, building up a high level of internal capability and experience. It has played three distinct and important roles as follows:

a) the network manager in the allocation and management of Phare funds for SME support services, run by the National Agency itself, contracted out to the network of RAICs and BICs;

b) the fund manager/monitor of Phare (and government) funds allocated to the provision of loans, micro loans and equity projects for SME development.

c) the project co-ordinator to strengthen the lobbying capacity of SME representative organisations, identifying areas for government to introduce improvement in the legal and regulatory framework

Initially, Phare funded a two-year technical assistance programme in 1991/92 to help in the design and establishment of the first RAICs and the National Agency (two long-term experts), together with an on-going programme of training of the advisory staff. This was followed by short inputs of technical support to review a particular area, help the agency to design and implement a new service or evaluate progress.

In addition, Phare has provided direct financial support to fund agreed programmes of the National Agency in the following areas:

- ECU 1.17 million (14%) as a contribution to direct operating costs of the National Agency (under a cost sharing formula with the Ministry of Economy)
- ECU 2.23 million (27%) for particular projects managed through the National Agency:
  - Euro 694,000 for policy and support to the unions and associations of entrepreneurs,
  - Euro 113,000 for the Euro Information Centre;
  - Euro 275,000 for the subcontracting project;
  - Euro 108,000 for support for fairs and the Europartinariat;
  - Euro 240,000 for the spin off project
  - Euro 800,000 for other projects and technical assistance
- ECU 3.7 million (46%) to provide business support services to SMEs through the network of the RAICs and BICs
- ECU 1.0 million (13%) for technical assistance on defined projects by western experts

The more detailed analysis of Phare contributions is set out in Table 2.4, which summarises the main allocations through the Financial Memorandum, and Table 2.5 which summarises actual disbursement of Phare and Government contributions across the primary areas of activity.

Table 2.8: Phare allocations to institutional work through Financial Memoranda

Euro '000	FM 1991	FM 1993	FM 1994	FM 1995	FM 1997	Total
Policy	140	18		50	50	**258**
SME Organisations	176	52		118	90	**436**
RAICs ad BICs	1,334	625	80	700	960	**3,699**
Euro Info C	18	20		35	40	**113**
Sub Contract	100	100		35	40	**275**
Fairs	81	27		-	-	**108**
Spin-offs	50	100		50	40	**240**
NADSME	250	250	170	220	280	**1,170**
Other	628	108		72	-	**808**
Long term TA	550	450				**1,000**
Total	**3,327**	**1,750**	**250**	**1280**	**1,500**	**8,107**

Table 2.9: Income and expenditure of the National Agency

Item ‘000 Euro	1994	1995	1996	1997
Income Funds from Phare	1235	1590	998	685
Funds from Ministry of Economy	183	202	146	135
Total	**1418**	**1792**	**1144**	**820**
Expenditure Institutional support	181	131	41	25
Domestic and foreign fairs		50	27	20
Regional Support		42	13	
Other		20	14	29
Support to RAICs	225	388	455	244
Support to BICs	231	258	151	50
Relations with representative organisations		60	8	
European Information Centre				
Subcontracting Exchange of Slovakia		281	35	112
Information System				
Regional projects		46	13	
Other	84	127	110	99
NADSME costs	212	187	131	106
Total	**1418**	**1792**	**1144**	**820**
% contribution by Phare (ex. RAICs and BICs)	**77%**	**82%**	**73%**	**74%**

Source: NADSME Annual Reports

Contribution to operating costs of the National Agency and PMU (Phare allocation: Euro 1.17 million)

The cost of running the National Agency is covered by contributions from Phare and the Ministry of Economy according to a memorandum of understanding drawn up in September 1996. It anticipated that Phare’s contribution to running costs would fall from 40% (Euro 210,000) in 1996 to 20% (Euro 130,000) in 1999 with corresponding increased funding from the Slovak Government. However, the overall contribution of Phare to National Agency programmes (excluding the financial programmes and support to the regional information and advisory centres) has been around 74%.

The main programmes of the National Agency funded by Phare are summarised below:

Support for policy development and SME Associations (Phare allocation: Euro 700,000)

In recent years, the majority of Phare support for policy development has been allocated by the National Agency to SME Associations to build up an analysis, lobbying and administrative capability and expand their membership amongst SMEs. Internally, the main thrust for policy development has lain with the Chief Executive, supported by senior managers and one specialist with periodic assignments undertaken by foreign consultants. The most significant output has been the Annual State of SMEs Report, which analyses key changes in the SME sector, and identifies priorities for future SME development.

Euro Info Correspondence Centre and fairs (Phare allocation: around Euro 383,000)

Since 1993, the National Agency has housed the Euro Info Correspondence Centre, providing entrepreneurs with access to services as part of DG23 European Information Service Network, including access to BRE and BCNET. The Agency organises and provides finance for around 120-150 selected SMEs to exhibit in four domestic trade fairs, Europartinariat and Interprise events, as well as a new Slovak National Interprise event.

In 1997, the Centre handled 1,036 enquires from enterprises (including 56% enquires from foreign enterprises mainly from other EICs) including 177 new clients and 300 enquires from consultants, trade associations and government bodies. The majority of enterprise enquiries were from firms employing less than 10 people (93%). 430 enquiries related to partner searches (38% from local enterprises). The reported number of enquires from the RAIC network in 1997 was around 45.
The department also organised participation in two Europartenariats and one Interprise event per year. The Centre appears to have only limited contact with other bodies engaged in export support, e.g. Export Information Centre, Chamber of Commerce.

Subcontracting Exchange of Slovakia (Phare allocation Euro 275,000)
The Subcontracting Exchange of Slovakia (SES) was set up at the end of 1994 with technical input from three experts from UNIDO. A team of 5/6 people have been engaged in bringing foreign firms and Slovakian subcontractors together, with a specialist unit for automotive subcontracting exchange, and a new Francophone business centre

Around 120 Slovak companies mainly in mechanical engineering and also garments and leather products are members of the Exchange. In 1997, the office dealt with enquiries from 120 foreign firms, which led to 26 firms visiting potential partners in Slovakia. It also organised and provided funds for 43 firms to attend four foreign events. In the mechanical engineering field, the specialist believed that regular subcontract work has been placed with around 10 Slovak firms. Whilst the programme has been successful in identifying interested foreign companies, it has not led to many meaningful relationships due to the poor performance (high costs and poor delivery times) of many of the Slovak sub-contractors. SES makes little use of the RAICs as they do not believe that they have specialists who could help these firms to change attitudes and improve their competitiveness.

Spin Off Programme (Phare allocation: Euro 240,000)
The Spin-off Programme, aimed at identifying and assisting the separation of SMEs from larger parent companies was initiated in 1994 with technical assistance from the French National Agency for the Development of SMEs (ANCE). The programme is run by two people from the National Agency with assistance of four RAICs and a Bratislava provider

The first programme with five large companies led to some 13 spin-offs being identified, and the setting up of eight companies, employing a total of 700 people. The second programme with one large enterprise was less successful; several spin-outs were identified but ownership and control were retained by the large enterprise. The third programme was with a major TV enterprise. Ten businesses were identified, the managers attended a two week training programme and all have now set up an SME, employing around 500 people. About half are independent, and the rest are 50;50 joint ventures with the large enterprise. The fourth programme began last November with four large enterprises; 10 projects have been identified and some have started. Four large enterprises have joined the fifth programme, and it is hoped that 10 spin outs will be developed. RAICs have only played a limited role, in part because of the low fee paid (Euro 1,000 per spin out) for their services, which includes providing help to the spin out to prepare their business plan and provide continuing support.

Support for Business Support Services through the RAICs and BICs (Phare allocation: Euro 3.7 million)
Subject to the availability of funds, each year, Phare funds for SME business support services are allocated by the National Agency to the network of 12 RAICs and 4 BICs established with Phare support between 1992 and 1996. Contracts are placed with each RAIC and BIC to provide a specific number of free and partly paid services to start ups and small enterprises unable or unwilling to pay market prices. This includes the provision of initial and follow up consultations, the preparation (and assessment) of business plans, and the provision of training within agreed budgets (based on an hourly rate of Euro10 - SK 400). Centres are expected to charge start ups an average of SK 50-100 per hour, and SK 100-150 per hour for existing companies. The value of the contract with each Centre is the same though the output mix will vary according to the local demand for services. Centres are encouraged to allocate the free and partly paid services to those clients least able to pay; but for those clients who

can afford to pay, Centres charge an average of around SK 500 per hour (Euro 12). The average contract value per RAIC has been around Euro 30,000 per year.

The number of staff in each RAIC varies from four to eight (average 5), with a total of 46 people engaged in the provision of consultancy services (average of 3.8). Several Centres also make use of external advisers on a regular basis.

Over the years, the size of client firms has remained unchanged, - the majority of clients (74%) were self-employed, and, of the registered companies, 90% employed less than 25 people. But the proportion of work for start-ups reduced from an average of 59% in the period between 1995 and 1997 to 31% in the first half of 1998, reflecting a deliberate policy to target services more towards existing businesses. On average each year, the network of 16 Centres (until 1997 -17) deal with around 10,200 clients, prepare or assess around 1,300 business plans and deliver 140 training courses, resulting in around 580 start ups.

Overall outputs 1993-98 (RAICs and BICs)		
Number enquiries for general information	21,009	
Specific advice to SMEs	25,807	
(sessions to support the development of business plans, financial analysis, market research, gaining contracts abroad)		
Number of business plans developed	7,461	
Number of new businesses set up	2,067	
Number of enterprises assisted to raise finance	1,470	
Number of design and development projects	231	
Number of training courses organised	642	
Number of participants on courses	10,368	
New job opportunities	10,000	
Total number of registered clients	10,331	
0-9 employees	71%	
10-24 employees	19%	
25-250 employees	8%	
> 250 employees	2%	
Additional features of BICs		
Incubation area	5,000 sq m	
Average number of firms in each incubator	19	
Age of firms	1-4 years	
Total employment in incubator firms	422	
Total number of start ups in BICs	235	+ 26 firms in Bratislava BIC
Number of new innovative products developed	21	+ 30 projects in Bratislava BIC

2.5 Activities of other donors

The activities of bilateral donors have been co-ordinated in almost all cases through the National Agency. In addition, donors have provided technical support and project funding to a limited number of RAICs and BICs.

Netherlands: Technical assistance in the period 1995-7:

- development of a Management Information System for the National Agency and the Centres for client handling and performance monitoring,
- software to support the development of business plans
- a matching programme to promote trade relationships between Slovak and Dutch companies

Germany: Technical assistance in the period 1995-7:

- support for the development of a number of unions and associations of entrepreneurs including the Slovak Union of Small Business Owners and the Slovak Association of Crafts
- collaboration with specific RAICs to assist their clients to improve their production capacity
- sector initiatives, involving seminars, study visits to Germany and provision of consultancy services

Great Britain: Technical assistance in the period 1995-98:

- the training of RAIC staff (1995)
- the drafting of the Medium Term SME Strategy
- the design of the pilot micro credit system
- studies to examine the barriers to SME development, focusing on lobbying and representation, and access to credit facilities
- support to two RAICs to help their enterprises develop links with British enterprises
- support for the formation of an Association of RAICs and assistance to a pilot RAIC to be accredited under ISO 9000.

France: Technical assistance in the period 1994-5:

- the setting up of a subcontracting programme, which led to a design project with UNIDO and Phare. Subsequent collaboration with the Subcontracting Exchange of Slovakia to analyse the needs of French partners and identify potential Slovak subcontract partners
- a training programme for unemployed people wishing to start a business, which led to the formation of the Association of CEPAC Slovakia, formed jointly by the National Agency and the National Labour Office to manage the programme
- development of the Spin Off programme and the training of National Agency staff

United States: Support from 1994:

- identification of potential Slovak enterprises seeking business partners in the United States
- the setting up of three Entrepreneurship Centres in Bratislava, Banska Bystrica and Koscise to provide information to entrepreneurs
- the deployment of 15 Peace Corps volunteers to work as consultants in the RAICs and BICs with access to the MBA Enterprise Corps of specialist experts
- the training of staff of the network and staff recruitment
- provision of funds for a UNIDO study for the Ministry of Economy to improve the collation and analysis of SME sector information to support the development of clearer policies and strategies for SME development (1997)

2.6 Relevance of the Programme

Phare has played a crucial and central role in helping the government to develop SME institutions to support the development of the SME sector. The development of the National Agency at arms length from government has proved to be a good solution. In Slovakia, the National Agency has come to fulfil more than an executive and co-ordinating role; it is also partially involved in policy preparation and development, activities that would normally be undertaken within government. With the assistance of the National Agency, the government has formulated some broad mission objectives for SMEs; but these have yet to be translated into clearly defined short-term policy objectives and priorities. Consequently it is not easy to assess to what extent Phare programmes are meeting government priorities, as these have not been properly defined. Part of the problem is that the development of SMEs has not been a particularly high priority for the last five years, and so the government has been very happy to accept Phare's support.

At the outset, Phare quickly became a principal source of funding for a wide range of SME programmes in the field of information, advice, training and provision of finance. Maintenance and development of these programmes depended to a large extent on continued Phare support, which tended to reinforce existing relationships and patterns of development. There were four consequences:

- there was an acceptance of existing Phare funded programmes, which de facto set the priorities for SME development.

- insufficient resources were allocated to help the Ministry of Economy to develop its national priorities for SME development, which would then be the basis of future national and donor backed programmes

- there has been an absence of independent research, analysis and performance monitoring to assess the relative options and provide an analytical basis for formulating future government policy priorities for SME development and the allocation of government, Phare and bilateral donor funds to meet defined targets

- despite a general commitment, little progress has been made to establish either an SME Council to improve dialogue between SME representative organisations and government, or an inter ministerial body to co-ordinate and develop SME policies across the main government departments with an interest in SMEs.

In practice, the main interlocutor for Phare's SME programmes has been the National Agency rather than the Ministry of Economy. But the National Agency neither has the remit or the capacity to undertake many of these tasks. Within Phare, whereas in the early days the Task Manager had more time to develop and review forward strategy, over time the number of sectors being covered by a Task Manager and number of on-going administrative functions has increased. Consequently, Phare programmes for SME development have increasingly been determined by expediency rather than based on needs analysis and a clearly thought through strategy. Most of these shortcomings were identified in the Evaluation of the Phare SME Programme in 1996. Whilst some steps have been taken, the problem has become more serious as the number of projects now being pursued has increased, funding from all sources is tighter, and the innovative capacity of the National Agency may not now be so strong, due in part to the departure of several of its senior executives: (only one of the six original directors who initiated the early programmes is still with the Agency).

In particular there is no basis for assessing or comparing the performance and added value of different financial schemes, or projects being taken forward by the National Agency. What, for example is the comparative performance and value of the various financial programmes, and how should resources be allocated to achieve optimal pay back in terms of government policies for SME development? Similarly, several of the National Agency programmes have been running for several years and now need to be reviewed to determine which projects should be expanded and which projects should be closed to release resources for projects with a higher priority. To address these questions, more resources will need to be allocated towards research, analysis and policy formulation, supported, perhaps with technical assistance.

Despite these shortcomings in the design and the comparatively low priority placed by government on SME development in practice in the last five years, much has been achieved. The National Agency and the network of RAICs and BICs has provided an effective institutional platform for the development of SME programmes in Slovakia, and the attraction and mobilisation of resources from other donors, which in most instances has been of value.

Chapter 3 Evaluation of Phare Financial Programmes

3.1 Logical Framework: main criteria for assessment:

The Logical Framework (LF) approach has become the de facto European Commission standard for project design, monitoring and evaluation. Five criteria are used for evaluating programmes, relevance, efficiency, effectiveness, impact and sustainability. These terms and the general approach are summarised in appendix A.

Using this approach, a log frame for financial programmes has been drawn up to identify the anticipated inputs, outputs and objectives of financial programmes. The table also includes a set of key questions, which have been built up against each of the evaluation criteria and the table considers what verifiable evidence might exist to enable these questions to be answered. The subsequent fieldwork focused on assembling evidence to help answer these questions.

3.2 Project Selection and methodology of evaluation

Sample

The Small Loan Programme (and the pilot Support Loan Programme) was selected for detailed evaluation, as it has been running for a significant period of time (since 1994) and represents the largest Phare SME programme in Slovakia.

Whilst the Support Loan Programme is being run through four banks, the Savings Bank was selected for the evaluation as it is the only bank to have been involved in both loan programmes and has also been a recipient of technical assistance under the Bank Window project.

The evaluation concentrated on the Bank’s loan portfolio at one of its branches at Nitra, whose performance, the bank believed, was reasonably representative of their branch network. Nitra was also chosen as it is the location of the RAIC, which had been selected for the evaluation of an institutional programme. This enables a comparative assessment to be carried out between the Bank’s and the RAICs customers. A more detailed summary of the Nitra Region is provided in the case study in section 5.4 below.

Key questions relating to the Support Loan programme, which are set out in the Log Frame (appendix B), are summarised below:

Relevance: to what extent has the programme clear objectives, to what extent does the design address them in an optimal way, and should changes be made to the design of the programme?

Efficiency: the level of public subsidy, rate of disbursement and the selection of applicants

Effectiveness: in what ways has the programme improved the performance of these firms, and were these firms the most appropriate for the programme?

Impact: to what extent has the programme altered lending policies in the bank?

Sustainability: what financial and management arrangements have been made for the programme to continue?

3.3 Achievements of Small Loan and Support Loan Programmes

The parameters of the small loan and support loan programmes are summarised in table 3.1:

Table 3.1: Input output details of the Loan Programmes

Parameter	Small Loan Programme	Support Loan Programme
Funds	Phare Euro1m (SK 38.5m) (No local contribution)	Phare Euro 2 x 5.2m (SK 400m Ministry of Economy SK 400m Four Banks SK 400m Resulting leverage: Euro 1 from Phare attracted Euro 2 locally
Clients	Up to 25 employees	Up to 500 employees Trade businesses excluded
Loan details	Loans in local currency Up to SK 800,000 (Euro 21,000) Up to 5 year pay back Interest: 2.5 % above discount which has been 8.8 = 11.3% Collateral: 100% of loan	Loans in local currency Up to SK 5m (Euro 133,000) Up to 5 years pay back Interest: 2.5% above base which has been 8.8% = 11.3% Collateral; as required by bank
Ownership	Fund owned by NADSME	Phare and government contribution owned by NADSME
Losses	NADSME accepts 90% of risk	NADSME accepts 2/3s of the risk of its contribution (2/3s of loan) ie 46.6%
First round lending	April – August 1994	November 1994 - Mid 1997
Number of applications Number of loans made	Not known 133	1,746 591
Funds allocated at start Total loans made to date % revolved	Euro 1m: SK 38.5m Euro 1.86m: SK 71.9m 186%	Euro 31.2m: SK 1,200m Euro 46.5m: SK 1,789m 148%

An analysis of the loans made by the Savings Bank indicates that 55% of loans were for premises, 37% for equipment and 8% for stocks. These were guaranteed by collateral with a value of 132% of the value of the loans made, 64% of being property assets and 29% with equipment. The number of support loans made by the Savings Bank were 85 in 1994, 51 in 1995, 70 in 1996, 38 in 1997 and 15 in 1998.

The two tables below, based on information provided by the four banks up to June 1998 provide an analysis of the types of customers being granted loans under the programme, in terms of the age of the business, employees, sectors and size of the loan obtained. Whilst there are small differences in terms of size and sectoral make up of the clients between the four banks, these differences are not significant.

Table 3.2: Profile of Enterprises Receiving Support Loan Programme

Age of business		Employment		Sector	
Date of formation	**83 cases * %**	**Employment**	**315 cases * %**	**Sector**	**591 cases %**
> 1992	34%	**0**	4	**Food industry**	16
1992 - 1994	55%	**1-4**	11	**Textiles**	9
1995 - present	11%	**5-9**	16	**Wood process**	12
		0-9 employees	31%	**Iron, plastics**	15
		10-24	33	**Glass, stone**	3
		25-49	14	**Construction**	9
		10-49 employees	47%	**Printing**	2
		50-99	14	**Energy**	2
		>100	8	**Chemicals**	3
		>50 employees	22%	**Tourism**	8
				Services	21

* It was not possible to obtain analysed data from all of the banks

Table 3.3: Percentage distribution by size of loan and number of employees (194 loans)

Size of loan/ employment	0-9 Employees	10-49 employees	>50 employees	Total
< SK 1m (<∈ 26,000)	7.5%	3.5%	-	11.0%
SK 1 - 1.9 m (∈ 26-50,000)	5.5%	10.5%	1.0%	17.0%
SK 2 - 2.9 m (∈ 50-78,000)	3.5%	8.5%	4.5%	16.5%
SK 3 - 3.9 m (∈ 78-103,000)	3.5%	6.5%	3.5%	13.5%
SK 4 - 4.9m (∈ 103-130,000)	1.0%	7.0%	4.0%	12.0%
> SK 5.0 (> ∈ 130,000)	4.0%	14.0%	12.0%	30.0%
Average loan: SK	SK 2.37m	SK 3.28	SK 4.12 m	SK 3.26m
Average loan: Euro	61,500	85,200	107,000	85,000

Source: Analysed data from Pol'nobanka

There is good correlation between the size of the enterprise and the size of the loan. 30% of enterprises obtained the maximum of SK 5.0 million (Euro 130,000), 40% of whom were those employing more than 50 people. This is reflected in the annual loan size for the three size groups of enterprises.

Figures from a pilot survey undertaken by the RAIC in Zvolen for the National Agency indicates that 56% heard about the loan programme from the RAIC, 50% from the bank and 19% from the media. In two thirds of the cases the companies themselves prepared the business plans. The remainder, mainly start ups and smaller companies, used the services of the RAIC.

The Sample

A sample of seven cases with the Savings Bank and 2 others was examined at Nitra. A profile of the Savings Bank Branch and the procedures adopted in processing a typical Support Loan Case are summarised in the box below. More background on the economy of the Nitra Region and the RAIC are provided in a box in Section 5 .

Nitra Branch of the Savings Bank: processing a Support Loan application

The Nitra Branch of the Savings Bank has a total of 170 employees. Its primary work involves the management of customer's current and deposit accounts in the Nitra District (population of 162,000), where there are around 1,500 registered enterprises and 8,600 self employed people. The branch has a small credit department of three credit officers and an accountant responsible to the Operations Manager. The operating limit for the Credit Committee of the branch is SK 4m (Euro 100,000), above which, projects have to be submitted to the Credit Committee at Head Office for approval. The Nitra Branch has made seven Phare loans, two under the small loan programme and five under the larger Support Loan Programme.

Clients with projects that require long-term finance are required to complete an application form and submit a business plan, which in some cases may have been put together with the assistance of the RAIC. Provided the client meets the general criteria of the programme the Business Plan is referred to the RAIC for evaluation and comments, and contact is made with Head Office to determine whether cash would be available, if the proposal is approved. A credit officer in the branch is required to carry through an appraisal and consider collateral arrangements, as laid down in the Bank's general credit manual and prepare the dossier for consideration by the Credit Committee. Though the RAIC nominally have a right to attend, in Nitra this is rarely exercised. If the application is approved, the branch sets up the loan and manages the repayment programme.

Meetings were held with 6 entrepreneurs (4 of whom received loans from the Savings Bank and 2 who obtained loans from two other banks in Nitra), the Adviser in the RAIC who undertook the review of the project, and one of the credit officers in the Savings Bank Branch where each of their seven cases were reviewed. Meetings were also held with the General Director, and staff in the Savings Bank with responsibility for the direction and management of the programme and with staff in the National Agency engaged in monitoring the programme. The nine case studies (2 small loans and 7 support loans) are summarised in Appendix F.

Relevance

Did the Loan Programme meet the needs and policies of the country

A policy objective of the Government has been to increase the number and competitiveness of small and medium sized firms in the size range of 10 to 100 employees, where Slovakia is under-represented compared to the EU. There are a significance number of established SMEs with viable financial plans for investment projects who cannot secure finance from the banking sector, and are too large to be financed using their own, family or friends resources. Since the end of 1996, banks have limited credit and are able to charge high interest rates to large customers who are known and have an established track record with the bank, including, in many cases, good export earnings. Whilst the Japan EXIM Bank resources provide funds above Euro 200,00 (SK 8m) and EIB projects average Euro 4.3 m (SK 180m) , the Phare Support Loan Programme has been the only source of funds for investment projects in the range of Euro 25,000 to 125,000 (SK 1-5m) for start ups and enterprises with a limited track record.

To what extent was the design appropriate

The credit programme is addressing a real need for funds. With interest being below the market rate, the demand for funds has exceeded supply. However, because no economic objectives were set at the design stage (e.g. jobs, growth potential, exports), if a project meets the selection criteria, it will be supported even if normal bank funds had been available.

A key feature of the design was the decision to channel funds through the National Agency rather than directly to the banks, or via the National Bank in order to encourage the development of closer relationships with participating banks, both nationally though the National Agency, and perhaps more importantly locally between the branches and the RAICs.

Though these opportunities have not been fully utilised and there is considerable scope to improve relationships, it has led to a better understanding of each other's orientation and interests. There is no evidence that the National Agency or the RAIC has interfered in the appraisal and selection of projects by the Bank. The Savings Bank in Nitra valued the input of the RAIC in the preparation of the Business Plan and the collation of all the paperwork required for processing a loan. But it appears that the RAIC does not have a particularly close relationship with the Savings Bank. Although permitted to attend, it does not attend credit meetings and there appears to be no dialogue on cases, even when a client was taken to court for failing to repay his loan. Part of the problem is that the banks are still very hesitant to share information with the National Agency or the RAICs, and have yet to see the full benefit of the partnership as they are not actively trying to enlarge their client base.

Under the terms of the agreement with the European Commission, the funds from Phare are now clearly in the ownership (and form part of the balance sheet) of the National Agency, for the Support Loan Programme. Whilst changes may be made to loan conditions, these must first be agreed with the Ministry of Economy and the European Commission, though it is unclear when prior approval from the Commission ceases.

It was clear from the review of cases with the Savings Bank in Nitra that before late 1996, most of the projects would have been able to get funds from the Bank, but at a higher interest rate. Whilst some of the larger clients would have accepted the higher interest rate, several of the start-ups would not have taken a loan at commercial rates. Neither the Bank nor the RAIC have considered whether projects could get funds from commercial sources, as this was not one of the selection criteria. However, loans made in 1997 and 1998 are 'additional' due to the overall shortage of credit.

A major limitation of the programme is its size due to the shortage of public funds. A key feature of the design was to build up the capital of the fund to around Euro 75m, with equal contributions of about Euro 5 m per participant per year from Phare, the government and the participating banks over a four to five year period. Had this been achieved, it would have been possible to maintain a constant lending programme with reducing capital contributions as the fund became more dependent on recycled repayments. The programme has lost momentum due to the uneven and unpredictable flow of funds. Having developed systems and procedures, provided training for bank and Agency staff and promoted the Support Loan Programme to potential end clients, the effectiveness of the programme has suffered due to this loss of continuity. This was mainly due to the cancellation of the 1996 Financial Memorandum to Slovakia, and delays in securing agreement for the next contribution from the Government.

Efficiency

The initial funds for the programme were allocated in the 1992 Financial Memorandum, which meant that no design work could realistically begin until 1993. Due to the dislocations arising from the partition of the country, it was necessary to establish a new PMU within the National Agency, set up in early 1993. In the circumstances, rapid progress was made to complete the design arrangements and launch the Small Loan Programme in April 1994: by August these funds had been fully dispersed to 133 clients. By the end of November, new, more complex negotiations had been completed for the first tranche of the Support Loan Programme.

The programme achieved a high level of interest resulting in 3-4 applications for each loan awarded. Staff in the RAIC in Nitra believed the appraisal and selection was carried out professionally and the choice of projects that were approved was felt to meet the design criteria. Some of the clients interviewed in the sample felt that the appraisal period took too long. Whilst the average was around 2-3 months, two clients commented that the process took 4-6 months.

Losses arising from late payments have been relatively low. Complete data was available from two banks. By mid 1998, Pol'nobanka, had made 194 loans with a total value of SK 607m (Euro 16 million). There were eight loans which were greater than 6 months in arrears, with outstanding principal amounting to SK 20.9m (Euro 540,000) and unpaid interest of SK 3.9m (Euro 100,000). Together this represented an average loss of 4.1% of the amount lent. Tatrabanka, which has a smaller portfolio, had just one account which was more than 6 months in arrears; total principal and late interest payments amounted to SK 5.4m (Euro 140,000), a loss of 1.7% of total lending. Table 3.4 summarises the number and value of all late payments (regardless of age). On the basis of the data from two of the four banks it would appear that bad debt write-offs averaged around 3.3% of the total portfolio.

Table 3.4: Analysis of late payments (over one month) and bad debts (> 6 months)

Bank	No of Loans Made	Value of loans SK/ (Euro)	Late payers > one month		Bad debts > six months		
			No of late payments	Value and % of late payments	Value of bad debts SK/ (Euro)	No of bad debts	% of loans made
Savings Bank: small loans	133	71.9m (1.9m)	11	3.4m (4.5%)	Na	na	na
Savings Bank: SLP	264	701.3m (18.2m)	64	37.7m (5.4%)	Na	na	na
Pol'nobanka: SLP	194	606.9m (15.7m)	37	24.9m (4.1%)	24.8m (644k)	8	4.1%
Tatrabanka: SLP	83	317.9m (8.2m)	12	5.8m (1.8%)	5.4m (140k)	1	1.7%
Istrabanka	50	163.4m (4.2m)	7	nk	Nk	nk	nk
Total	724	1861m (48.3m)	124	71.8m (4.2%)	30.2m (784k)	9	3.3%

Table 3.5 attempts to calculate the public subsidy costs relating to the Support Loan Programme, which amounted to two tranches of Phare funds (Euro 10.4m), matched with equal contributions from the bank and the government. In the 'first round' (prior to repayments being lent out again), the initial portfolio, amounting to Euro 31.2, was used to make around 367 loans averaging Euro 85,000 (SK 3.26m) for an average loan period of 3 years at 2.5% above the National Bank discount rate. The bank paid the government and Phare/National Agency a deposit interest rate of 6% below the National Bank discount rate, thus providing the bank with a spread of 8.5% to cover its management costs, its share of any losses (53% of the total) and a profit.

Table 3.5: Calculation of public subsidy of Loan Support Programme based on a portfolio of Euro 31.2m, average loan size of Euro 85,000 = 367 loans for three years

Item	Basis of costing	Public sector subsidy: Euro
Technical Assistance	Euro 700,000 depreciated over 8 years	87,000

Interest rate subsidy	The bank received 2/3 of money (Euro 20.8m) at the discount rate less 6%. This represents an average subsidy of 6% x 1.5 years, assuming regular repayments over a three year period	1,872,000
Evaluation of business plans by RAICs	367 plans: 12 hrs per plan @ Euro 10 per hour	44,000
Management costs of the banks	Covered by the 8.5% spread received by the bank	-
Loan write-offs	3.3% of portfolio (Euro 31.2 m) i.e. Euro 1.02m. Under the risk sharing agreement, Phare + government losses = 46.67%	480,000
Total		**2,483,000**

The government and Phare's contribution of Euro 20.8m to the Support Loan Programme resulted in the provision of 367 loans (prior to the re-lending of the repayments), averaging Euro 85,000 for three years. The total public subsidy over the three year period was around Euro 2.48m, as set out in table 3.2 above. Thus the annual public subsidy was around Euro 827,000 which amounts to 4% of the public funds made available. This assumes that the value of the technical assistance is amortised over eight years, that average bad debt write-offs will be similar to the experience of Pol'nobanka and Tatrabanka, and that the banks' management costs and losses are fully covered by the spread of 8.5% received by the bank.

The banks' losses arising from loan write-offs amounted to Euro 620,000; this represents an annual loss of 0.6% (based on the total portfolio of Euro 31.2m), against the spread achieved by the bank of 8.5%. Unfortunately it was not possible to establish the banks' management costs, so it has not been possible to establish what net margin banks were able to make.

Effectiveness (immediate results amongst the enterprises compared to inputs)

Evidence from the banks' statistical reports, backed up by surveys carried out by the National Agency, suggests that in overall terms, most of the support loans are going to an appropriate mix of businesses in terms of size, age and sector. There is also evidence to suggest that these businesses have achieved impressive increases in turnover, profits, tax payments, exports and employment.

We were able to get access to early results of new monitoring work being commissioned by the National Agency. RAIC Managers have been asked to interview all recipients of the Support Loan Programme using a standard questionnaire to learn how their business has developed since receiving the loan. Figures on turnover and growth for 32 loans made in the Zvolen are presented in table 3.6.

Table 3.6: Average turnover and growth of enterprise in Zvolen receiving Support Loans

Number of firms	1993 m SK	1994 m SK	1995 m SK	1996 m SK	1997 m SK	Av growth %
16 firms	13.4	25.1	30.1	43.5	41.7	33%
6 firms	-	5.4	11.9	14.2	16.3	45%
6 firms	-	-	-	5.96	5.85	-
4 firms	-	-	-	-	3.6	-

The oldest 16 firms which were all formed before 1993, achieved an average annual growth rate of 33% per year, which by 1997 represented an average turnover of around Euro1 m. The

6 firms, which started up in 1994, achieved an average annual growth rate of 45%, and a turnover in the fourth year of around Euro 420,000.

The results of the interviews with eight firms receiving loans and the reviews of 9 loan files in the bank are presented as short case studies in Appendix F. Table 3.7 summarises the results of the case reviews and an effectiveness rating (from 5 = high to 1 = low) has been ascribed to each case according to how much we believe each firm's performance has been enhanced as a result of receiving the loan. Firms, that could have obtained a commercial loan from the bank, have been marked down accordingly.

Table 3.7: Summary of review of firms receiving Support Loans

Enterprise	Size of loan Euro (SK)	Product	Assessment	New jobs	Effectiveness rating 1-5
Mr A	6,753 (260,000)	Wooden panels	Would not have started without a loan	7	4
Mr B	20,780 (800,000)	Locksmith	Not started without loan. Wouldn't repay the loan	2	2
Co C	130,000 (5m)	Garments manufacture	Could have obtained loan from bank. Now more competitive	?	2
Mr D	39,000 (1.5m)	Glass wholesaler	Extra stocks. Not within loan criteria. Limited benefits	1-2	1
Mr E	6,500 (250,000)	Car repairs	Without loan not started in business. Self employed	1	2
Co F	58,000 (2.25m)	Car service centre	Could have obtained loan from the bank. Project helped the company to grow	+9	3
Co G	104,000 (4m)	Glass processing	Poor plan. Glass process closed	-	2
Mrs H	130,000 (5m)	Hotel accommodation	No growth or extra jobs	-	1
Mr J	36,000 (1.4m)	Design and production of signs	Loan enabled the business to start. Good growth potential	1 pt	4
9 firms	531,000 (20.46m)			22	2.3

Note: Scale of effectiveness is from 5: high to 1: low

Table 3.7 summarises the results of the assessment together with details of the loans made and an estimate of the number of additional jobs created. In summary, the sample of nine loans amounting to Euro 531,000 created around 22 jobs, and involved a subsidy of 4% from Phare and 4% from the government, each amounting to Euro 21,200. Based on these figures, the net cost per job of the Phare contribution was around Euro 936.

In terms of effectiveness, of the nine firms, two demonstrated above average effectiveness (4) and 2 were well below average (1). The overall effectiveness in terms of the nine firms was rated at just below average with a score of 2.3 (46%).

Impact

All the banks commented on the benefit of enlarging their client base. With a serious shortage of credit and too much demand, there is little evidence that banks had been trying to increase their customer base. There is no evidence to suggest that the Support Loan Programme has had any direct effect on the lending policies of the Savings Bank towards SMEs. However, during the period since the Phare loan programme has been operating, the Savings Bank has introduced a number of improvements in its methods of appraising loans and monitoring repayments, some of which may have been prompted by the Phare programme.

Sustainability

When the programme was established, the funds from Phare and the Government's contribution in the first two phases were transferred as a grant to the National Agency. Changes to the programme require the agreement of the Government and Phare. This may be inhibiting the National Agency from playing a more active role in reviewing performance and ensuring that the design of the programme is modified to meet newly defined objectives which maximise the impact of the fund on SME development. It is important that flexibility exists and is encouraged. The specific operating conditions that were laid down in the 1991 and 1993 Financial Memoranda were appropriate at that date; but it is essential that the design parameters are kept under review and changed to reflect current and future needs of SMEs. The National Agency as the owner of the fund needs to take the lead in this.

The sustainability of the fund in financial terms depends to what extent interest income paid to the National Agency offsets its losses from non-performing loans and the depreciation in the value of the fund due to inflation. Currently, annual losses are averaging around 3.3%, and inflation has been around 6%. This is offset by interest payments to the National Agency of 2.8%. Thus in real terms, the fund is depreciating at a rate of around 6.5% a year (6.0 + 3.3 - 2.8 = 6.5%). Thus it will halve its value in around 8 years.

Summary

Table 3.8: Summary evaluation of the Support Loan Programme

Evaluation Measure	Comment	Rating
Relevance to government policy	Meets a clear need of early stage SMEs seeking loans, when credit facilities are in short supply	4
Relevance of the design	Sound structure for levering funds from the government and the banks. Well integrated with the RAICs and BICs. Insufficient attention to "additionality" criteria	3
Efficiency	Good uptake. Annual public subsidy 8.4% of the fund	3
Effectiveness	Loans going to start ups and enterprises achieving significant growth. But there is evidence that up until the end of 1996, many of these businesses would have been able to obtain commercial loans from the banks.	3
Impact	No evidence that programme has led to changes in bank lending to SMEs	1
Sustainability	Ownership clear and funds revolving satisfactorily, but the value of the funding is depreciating at around 6% per year.	3
Total	The project is well designed and is operating satisfactorily	2.8

3.4 Comments on other Phare Financial Projects

Phare Loan Guarantee Programme

The Phare's contribution of Euro 3m towards the government's Euro 6m Loan Guarantee Programme is described in Section 2.2 and the inputs-output Table 2.4. An interim evaluation of the Loan Guarantee Programme, was being completed under a contract with NADSME, from which the following comments have been drawn. Uptake of the scheme has been well below expectations. In the first four years (1992-95) from 115 applications, 93 guarantees worth Euro 5.6m were made, covering 64% of the value of the loans. In the last three years only 17 further guarantees have been agreed worth Euro 0.75m. The main reason for the lack of utilisation, relates to the lack of confidence in the scheme by the commercial banks, who did not know exactly how much and when they would be paid in the event of a default. This is because, in the original design, the terms of the agreement with the Commercial Banks appear to lie exclusively with the Guarantee Bank, who have been concerned that commercial banks will distort the values of the collateral in their favour. In consequence, in the event of a default, it would appear that the Guarantee Bank will only pay up to 75% of the amount outstanding, after the collateral has been recovered. This results in the commercial banks incurring a loss of at least 25%, which cannot be recovered through the value of the collateral. It has also led to substantial delays in the settlement, as claims on the Guarantee Bank are clearly dependent on the level of recovery of the collateral. Thus to date, there have been 17 defaults worth Euro 640,000 (11% of guarantees made), but repayments of Euro 172,000 have only been made on 7 claims. The Guarantee Bank receives a one off fee of 1-2% from the enterprise (depending on the terms of the loan) and, in addition, charges the Fund a fee of Euro 250 per commission per year + 1/20th of the deposit interest earned by the Fund. The public subsidy relating to the scheme is made up of the following elements:

1. Losses from guarantees made. Claims: 11% Repayments made: 3% over a 6 year period. Assuming that the loan guarantee is outstanding for 3 years, the average loss per guarantee is between 1.5 and 5.5%.
2. Handling fee per guarantee. For an average guarantee of Euro 51,000 for three years, the administrative fee is Euro 3 x 250 = Euro 750 which is 1.5% of the guarantee.

3. Income from deposit interest. At a discount rate of 8.8%, fee paid to Guarantee Bank = 0.4% per year, which is 1.2% for a three year guarantee
4. Inflation. There will be no cost on the assumption that the depreciation of the fund due to inflation is covered by the interest income paid at the bank's normal deposit rate.

The total public sector subsidy per guarantee will be around 4.2-8.2% depending on the final settlement loss, representing an annual depreciation of the fund of 1.4-2.7%. Regrettably, no job generation figures are yet available to enable a comparative cost per job to be calculated.

The interim evaluation for NADSME concluded that the scheme was a failure and recommended that the National Agency should urgently consider how best to reuse the fund.

Micro-credit programme

The background to the pilot micro-credit programme (Euro 220,000), which was launched in March 1997 and inputs-output details are summarised in Section 2.2 and Table 2.5. An interim evaluation by an independent consultant for NADSME is being finalised from which this section is based. The fund was fully dispersed in 12 months. From 109 applications, 47 loans averaging Euro 4,680 were made to enterprises repayable in up to three years at an interest rate of 8.8% (National Bank discount rate + 1.5%). No failures have been reported to date. The evaluation report concluded that the programme met its objectives and that the structure of using the RAICs and the target group of enterprises supported was appropriate. It also made a number of detailed suggestions on the design of the next phase as follows:

- the maximum size of the loan should be increased from Euro 7,000 to 13,000 provided extra jobs are involved;
- businesses should have attended a basic two week training course;
- loan interest should be set according to the purpose of the loan. For investment projects, it should be the National Bank discount rate + 2.5%, and for working capital, the rate should be two times the discount rate.

There is not sufficient information available at this stage to indicate the public subsidy cost of the scheme.

Seed Capital Co

Phare's contribution to the Seed Capital Co is summarised in Section 2.2 and Table 2.6. The impact of Phare's contribution to the Seed Capital Co was evaluated in October 1997 by an external consultant for NADSME. On the 14 investments, four companies are performing well, two though still in business are not performing, and one company has effectively ceased trading due to the apparent miss-use of funds by the proprietor and is now the subject of court action. Six clients were interviewed. All agreed that the Seed Capital Co was helpful, professional and co-operative, provided ideas and support. All except one client felt that the Company effectively monitored their business and their support was essential. The investments have led to 71 new jobs being created and a further 59 jobs are expected: a gross cost of around Euro 5,500 per job (excluding management costs). Most of the clients expect to achieve significant increases in both turnover and profits, and all but one had levered in funds from elsewhere totalling around Euro 1.5 m.

Technical Assistance: Bank Windows Project. (Euro 700,000: 31.5 man months Sept 1996-Sept 1997)

Significantly very little Technical Assistance was provided to either the National Agency or the Bank during the initial design and launch stage of the programme. The Bank Windows project, which was designed to provide this assistance, was seriously delayed and did not start until Sept 1996. This included three long-term experts working in the National Agency, and the head offices of the Savings Bank and Pol'nobanka for one year. Because the provision of technical assistance was not envisaged as an integral part of the credit programmes, the advisers were unable to secure the level of acceptance within the banks that was required. In contrast the adviser in the National Agency played a significant role in helping to develop the work of the Financial Department in relation to the various financial programmes. The delay in their arrival meant that their value and influence in the two banks was much reduced, though it did enable them to monitor the actual performance of the systems that the banks had put in place to manage the loan portfolio. We believe that both the National Agency and the Banks all benefited from having access to an external adviser making periodic visits to help them to monitor the programme and introduce design changes to improve its effectiveness in the light of experience.

3.5 Future options and priorities

Comments on the Loan Support Programme

There is some evidence to suggest that greater economic benefit might have been achieved by adopting a more selective approach towards the choice of clients and projects focusing on long term jobs (rather than turnover) and limiting the scheme to smaller enterprises (to perhaps less than 100 employees) least able to get finance from other sources. Whilst credit facilities for SME development remain very limited, it is important that the National Agency, as the trustee of the fund, plays a more active part to improve the design of the programme to ensure that it makes maximum use of the Support Loan Fund for economic development. It needs to set up measurable job related criteria and develop a more selective approach towards project selection, focusing on those financially viable projects that will give the best pay back for that particularly region.

Another option would be to increase the interest rate (by increasing the margin above the National Bank discount rate). The National Agency for SMEs believes that with inflation at around 6%, the current rate of 11.3% (8.8% + 2.5%) is appropriate, and that the 'commercial' rate of 20-22% currently being charged by the banks reflects a shortage of credit, and is an unrealistic rate for SMEs with investment projects. The danger is that if the interest rate is increased, it may favour lower risk (trade orientated) projects where the period of negative cash flow is shortest. However, if there is not some movement of the interest rate towards the banks' market rate, it may be difficult to convince banks to increase the level of normal lending to SMEs.

Reducing the maximum size of the loan would increase the number of projects being financed. This may not be practical, as the banks, in return for participating financially in the programme, were keen that, for operating reasons, the average loan size should not be too small. From the results, the effect of lowering the maximum project size from Euro 125,000 (SK 5m) to say Euro 100,000 (SK 4m) would effect around 30% of the recipients, but would only result in 10% more projects being funded.

The RAIC's staff expressed concern about the choice of banks for the project. They believed that more banks should be able to have access to the fund, as projects are generally rejected unless the applicant is already a bank client. This was confirmed by the credit officer at the Savings Bank. However, there is a danger that if too many bank branches are involved, they will have more limited experience in running the Support Loan Programme.

Concerns were also expressed about the system of allocating funds. Some RAIC staff felt that the programme could be run better by them. Though this is doubtful on the grounds of cost, conflicts of interest and from an operational perspective, it opens up a broader question. Until a structure is put in place which leads to a greater proportion of local deposits being recycled locally to regenerate the local economy, regional and local economic development will be dependent on policy priorities determined in the capital, where the interests of government and large enterprises tend to be stronger than regional and SME interests.

Conclusions and recommendations

The National Agency needs to initiate discussions with the National Bank and the Ministry of Economy to establish a sound basis for monitoring the flow of credit to the various groups of SMEs on a systematic basis to determine in which areas crowding out and market failure are occurring. From this analysis clearer priorities for each of the Phare Financial programmes can then be set in relation to national priorities and shortcomings that have been identified in the financial market. In particular, greater attention needs to be given, when appraising client applications, to consider whether they could access commercial funds from the market.

The National Agency, as the owner of the Phare funds, needs to put in place more effective methods of evaluating the performance of the various financial programmes on a routine basis to enable comparisons to be made about the relative efficiency and effectiveness of each scheme. If necessary, the National Agency should have the power to alter the operational criteria of these programmes to ensure that they continue to meet defined objectives.

Urgent steps need to be taken to redirect the Phare Loan Guarantee Programme to address weaknesses identified in both the 1996 and 1998 evaluations.

Closer working relationships need to be developed by the RAICs and BICs with banks engaged in managing the Phare loan programmes to assist more enterprises to prepare investment plans and monitor the performance as well as provide advice to those enterprises that receive finance to help them to realise their objectives.

Chapter 4 Evaluation of Institutional Programmes

4.1 Introduction

Three programmes have been included for evaluation. These cover:

- Policy and legislative changes
- The Setting up and development of the National Agency
- The provision of business support services

Log frames and input output tables have been prepared for each programme, from which a sample of projects has been selected for evaluation. The results of the each evaluation are set in the sections below.

4.2 Phare programmes to support Policy Development

Objective, logical framework, project selection and methodology
Phare has provided financial support to the National Agency and a number of representative organisations to encourage the development by government of policies, laws and regulations to improve the environment for SMEs. Phare funds have been used by the National Agency for a wide range of small projects, to support the process of improving the regulatory climate for SMEs. In the time available, it was not appropriate or possible to identify all the small areas of intervention or determine the cost of each. Instead, a more holistic approach has been taken, to make judgements about the overall value of the Phare's support in the area of policy development.

Funding was allocated across relatively broad areas of work without narrowly defined objectives being set for each project. Whilst the funds allocated to other representative organisations can be easily identified, considerable work was undertaken on an on-going basis by staff within the National Agency (much of whose costs were covered by Phare). Comparatively little work involved external foreign consultants, and almost no assistance was provided by Phare under the SME programme for project work within the Ministry of Economy (or any other Ministry).

A Logical Framework has been prepared for the programme relating to SME policy work (see Appendix C) and the key questions are summarised below:

Relevance: did the external assistance focus on the key issues? To what extent was the intervention welcomed and accepted? To what extent did the programme fit into the needs and policies of the country?
Efficiency: what were the costs in relation to the measures undertaken?
Effectiveness: to what extent have changes been made to improve the operating environment for SME development as a result of the intervention?
Impact: has it lead to greater awareness in government about key policy issues effecting SME development?
Sustainability: to what extent will work continue when Phare assistance comes to an end?

Entrepreneurs maintain, and this is not contested in Government that the poor regulatory framework for SME development is a more serious issue than the lack of credit. They identify four issues:

- the frequent changes in laws and regulations, particularly in the area of taxation;
- poor interpretation of laws and regulations, particularly, but not only in the area of taxation;
- the introduction of new laws and regulations that place an unfair burden on SMEs; and
- poor understanding amongst senior government officials of the potential of small firms to create employment provided appropriate incentives are put in place to support the formation and growth of small firms.

The resolution of these problems would have significant relevance to the development of the national economy. The capacity of the SME Department within the Ministry of Economy is very limited, and therefore is reliant on external inputs if the impact on SMEs of new legislation is to be taken into account.

To what extent was the design of the project appropriate?
The objectives included in the section of the 1993 Financial Memorandum, which first allocated funds for institutional development were formulated in rather general terms. It suggested that the National Agency would have five main areas of responsibility including:

- initiating draft policy and strategy for SMEs
- identifying barriers (including legislative) to growth in the SME sector, and put forward proposals to remove them.

It set aside Euro 50,000 to ‘support SME related organisations. Support will include consulting assistance for organisational purposes, equipment and training. The 1995 Financial Memorandum also included funds for policy and programme development: ‘The National Agency will continue in its activities in the area of development and further refine state policy towards SMEs. It will provide direct support for SME and craftsmen associations ....’ The expected outcomes included ‘non government SME organisations will have carried out a number of training activities for their members and will have strengthened its management and organisation....’ ‘policy and strategy will have been further developed through continuous studies and identification of obstacles to SME development.’

It is not clear from the Financial Memorandum what specific outputs were being sought or expected, and to what extent this was based on a prior assessment of the steps that would need to be taken to engage in work relating to policy, legislation and regulation. It would appear that there was an implicit assumption that by strengthening the management of the non government associations they would be able to engage in lobby work. It may also have been assumed by Phare that the National Agency had a remit to engage in policy research and analysis; in fact its capacity in this area has been very limited.

Should Phare be engaged in this work?
Improving the legal and regulatory environment for SMEs and the private sector as a whole is clearly a major priority, which requires a sustained financial, technical and political input over an extended period of time. Arguably it requires a very much greater allocation of resources than either Phare or the National Agency have made to this area to date, if meaningful progress is to be made. However, progress in this area is very dependent on

government support from the highest levels, which was largely lacking between 1994 and 1998.

Efficiency

The main output of the work has been the preparation of an annual publication reviewing the state of the SME Sector and its contribution to the national economy. It also sets out proposals for improving the operating environment for SMEs. Whilst the first edition in 1994 was a significant step forward, providing valuable factual data on the SME sector, the publication is, to some extent limited, due to the lack of independent research setting out the economic case for SME support and analysing the most serious barriers inhibiting SMEs.

A number of more detailed reviews of particular bits of legislation have been undertaken, which in some instances, did lead to modifications of legislation at the drafting stage. The project has also led to improvements in the capabilities of staff in the National Agency and in SME Associations to undertake policy related work.

Effectiveness

There is clear evidence to suggest that despite the limited tangible progress made on legislative issues, the combined effort of the SME representative organisations with the support of the National Agency has led to closer links being established, resulting in a greater level of awareness on a number of key issues relating to SMEs. With Phare technical assistance, preparatory work is currently taking place to prepare a new law on SMEs, with the object of bringing the definition of an SME into line with the EU, setting out more clearly the obligations of the Ministry of Economy to develop State Support for SMEs, charging the National Agency with the responsibility for the preparation of an annual action plan, and establishing an inter-ministerial SME Council.

The most tangible result is the improved allocation of funds to the National Agency for SME development. Three projects worth SK 7m (Euro 180,000) together with the SK 200m (Euro 5 million) for the Support Loan Fund have been allocated in 1998, and the Ministry has proposed a major SME programme costing SK 125m (Euro 3.2 million) for the 1999 budget. But, to date, only limited progress has been made to influence legislative and regulation issues.

The other significant output has been the development of a Medium Term Strategy for SME Support, which has been agreed by the Ministry of Economy. This makes a number of commitments by the Ministry towards SME development including strategic and spending priorities over the three-year period 1997-2000. This has been followed by the Ministry of Economy’s response to the Acquis Communitaire, which includes the Ministry’s commitment to an action plan to improve the operating environment for SMEs.

No significant progress has been made in improving the legal and regulatory environment for SMEs. There have been no significant changes to existing legislation, and no progress has been made to ensure that SME interests are taken into account when framing new legislation, particularly in the tax areas. Aware of the lack of progress in this area, the Ministry secured support from the British Know How Fund for technical assistance to identify SME Regulatory Barriers. One study reviewed how the present lobbying and representation on SME issues could be improved and the second study considered Credit and Financing Mechanisms. The report on lobbying provides some clear guidelines for effective lobbying and greater use of the media.

Impact (spill over effects from meeting wider objectives)
Phare's steady support for SME sector through the work of the National Agency, the network of local business support centres, the representative bodies and by improving access to finance has helped to raise the awareness about the role that SMEs can and should play in the economic regeneration of the country. Without the momentum created by the SME programmes supported by Phare, it doubtful whether the current general level of understanding both in parliament and amongst the main political parties would have been achieved. During the recent general election campaign, for example, all the main parties emphasised the importance of SMEs, but this has still to be translated into effective action.

In the crucial area of legislative reform, the National Agency has acted as a catalyst for a limited number of more detailed reviews of particular legislation by the Parliamentary Commission. Quite apart from the improvements in the capabilities of those involved, the provision of Phare support has raised people's awareness in the National Agency and the SME Associations about the process and the need to become more professional if they are to be successful in arguing for changes to be made.

However, it seems that despite the acknowledged success of the Phare SME Programme, it appears to have made little impact on changing the perceptions about the role of SMEs in the national economy amongst key Ministers in the Meciar government.

Though there does not appear to have been any significant improvement in inter-ministry co-ordination and collaboration on SME issues, there appears to be a growing recognition amongst officials within the Ministry of Economy of the need for a high level SME Council involving senior officials from the main ministries with an interest in SMEs and representatives of SME organisations to act as a forum for SME related issues.

Sustainability
Whilst all the main political parties indicated their commitment to supporting SMEs, it is too soon to judge to what extent this commitment will be translated into relevant actions. As a result of support provided by Phare and other donors to stimulate and support the Ministry, the National Agency and the various SME associations, there are now a greater number of well-informed and articulate advocates for SMEs. However, further work will be required to strengthen capacity, particularly in the area of performance monitoring, policy research and analysis in order to build up the economic and social arguments to support the case for changes in legislation and greater financial support for the SME sector.

Conclusions

Table 4.1: Summary evaluation of the support for policy development

Evaluation Measure	Comment	Rating
Relevance to government policy	Limited support within government, despite its importance to SME development	1
Relevance of the design	Poorly structured programme	2
Efficiency	Tangible outputs, despite the limited resources allocated to this area	3
Effectiveness	Limited achievements in terms of improved legal and regulatory framework	1
Impact	Increased awareness of SME issues amongst opinion formers	2
Sustainability	Limited capacity in the National Agency to sustain this work	2
Total	Limited progress in this critically important area	1.8

It would appear that nobody had realistically assessed what would needs to be done in order to achieve success in the area of policy development and lobbying work. Insufficient attention seems to have been given to:

- the selection of a limited number of priority issues on which progress could be made,
- undertaking the necessary research analysis to ensure that arguments are fully supported,
- planning the 'campaign' to secure the trust and support of key individuals
- implementing the campaign in a professional manner.

Though the strengthening of the various small business associations is a necessary condition, it is not sufficient if the regulatory environment is to be improved. Four factors need to be taken into account: the priority attached to this work, the level of resources available, the standing and competence of those engaged in this work, and the selection of a limited number of relevant and 'winnable' issues in order to build up creditability and practical experience.

Perhaps more progress could have been made if Phare had provided support to strengthening the policy-making capacities within the Ministry of Economy. This would have demonstrated within the Ministry the need for building up research and analysis functions to support SME policy development. At the same time it would have facilitated technical support to the Ministry in its dealing with other Ministries on SME related issues. However, the importance attached by Ministers to SME development (as reflected by the level of public funding available for SMEs compared to large enterprises) appears to have decreased from 1993 to 1998, despite the greater awareness and political support for SMEs in general. There are three main reasons why state support is not greater. Senior members of the Meciar government were inclined to maintain support to large enterprises in the state owned sector. Many of the most senior people had worked in these large enterprises and have only a limited appreciation of the SME sector. And, it appears that the financial and economic argument for greater support for the SME sector has not been made sufficiently forcefully to convince officials in the Ministry of Finance.

Amongst the SME Representative Organisations and the National Agency, further external assistance is needed to help to establish an effective unit with sufficient capacity to undertake research and analysis of SME issues to provide the justification for changes to be made. Those engaged in the lobbying process would benefit from a period of 'hands-on' technical assistance to help them to develop more effective lobbying techniques.

4.3 Phare support for the setting up and development of the National Agency

Objectives and logical framework
The Ministry of Economy set up the National Agency for the Development of SMEs in 1993 to act as a co-ordinating body for all activities which would support the development of SMEs and deliver a limited number of specialist national services.

A Logical Framework to be considered during the evaluation is set out in Appendix D and the key questions are summarised below:

Relevance: does the National Agency fill a recognised gap in the SME support infrastructure?
Efficiency: what was the public sector costs in relation to the value of the services provided?
Effectiveness: was there an improvement in the overall performance of the institutions providing services to support the development of SMEs?
Impact: has it lead to a more SME friendly environment, leading to growth in the provision and quality SME services?
Sustainability: will the National Agency retain its original objectives and continue to function in the longer term?

Phare has provided technical support in the design and setting up of the Agency and on-going funds for running costs under a cost sharing agreement with the Ministry of Economy. Phare has also provided financial support and technical assistance for specific projects. The structure and range of activities of the National Agency are summarised in Section 2.4, and the funding arrangements are set out in Tables 2.8 and 2.9.

In the time available it was not possible to evaluate each component of the National Agency's activities. The evaluation therefore focused on the initial support provided by Phare to assist the National Agency to get established and the provision of on-going financial support by Phare to enable the National Agency to develop its role.

Relevance
To what extent did the programme fit the needs and policies of the country?
There was considerable backing in government in 1992 and 1993 to establish an Agency to co-ordinate work related to SMEs. At that date, the International Financial Institutions and the bilateral donors had no plans to support the development of the SME sector. Without Phare's encouragement it is doubtful whether the Government would have established a National Agency at that date, though a State Guarantee Bank had been set up by the Ministry of Finance. By the time the National Agency had been set up, the explosive growth in the number of self-employed businesses was already well under way. Significantly, in May 1993, within 5 months of setting up the National Agency, the Government approved 'The Programme of Complex Support for SMEs' which including financial support to the National Agency.

Was the design appropriate?
The basic concepts and design of the National Agency have been sound and have provided an anchor around which a significant number of SME programmes have been able to flourish. The Agency is fulfilling a necessary and vital role, providing tangible evidence of the

government's commitment to SMEs, and at the same time leading the development and provision of a range of key information, advisory training and financial services required by SMEs, which are not available 'on the market'.

Whilst there was a debate at the time about whether the National Agency should be established as a State Body or as an independent foundation, it would appear to enjoy the status of being both a state body responsible to the Ministry of Economy for SME development, and at the same time having some financial and managerial independence of Government. This has enabled it to set its own pay structure and recruit a competent and loyal staff. Whilst there have been some changes over the years, few people left the Agency due to the pay structure until recently, when pay has not kept up with the private sector. Whilst this has been possible so long as the National Agency has access to Phare funds, there is still some disquiet in the Ministry that people in the National Agency should be paid significantly more than the civil service.

By 1995, i.e. within two years of start-up, most of the Agency's programmes, which are operating today, had been identified and were under way. Since that date there have been very few structural changes, with the focus being more towards consolidation and extension of existing services and activities, rather than on innovation.

The work of the Agency at the outset was focused in three principal areas - financial tools, advice and information and legal and regulatory reform, all of which continue to be the most critical issues facing SMEs. The balance between these three areas of activity is crucial.

Another important aspect of the design concerns the relationships between the National Agency, Phare and the Ministry of Economy. As with any organisation that is dependent on budget funding which is negotiable on an annual basis, the first priority is to secure the funding necessary to maintain existing programmes. The National Agency has found it difficult to change the balance of its programmes, at a time when there are increasing demands for the services of the National Agency and the Network, its operating income has been falling year on year. Change can only take place either by reallocating expenditures by cutting back on some projects, or by securing additional resources.

The National Agency has experienced a number of difficulties due to several design and operational reasons:

- short time horizon and changing priorities within Phare, as it focuses increasingly on accession related issues
- a lack of strategic focus, either within the Agency, Phare or the Ministry,
- overly dependent financially on Phare funds to maintain recurrent expenditure on projects in the National Agency and in the core work of the Network: currently Phare is contributing around 75% towards National Agency costs (excluding the Network) and a further 40% towards the total cost of the network.
- due to its dependency on Phare for funds, and because the Agency is, to some extent, in 'competition' with other Phare programmes for resources, there has been a tendency for the National Agency to propose programmes to Phare which it believes it could persuade Phare to continue to fund, even though there are other projects which the Agency believes may have a higher priority for the development of SMEs in Slovakia
- a reluctance of the Ministry of Economy to become the main funder of the SME programme as discussed under the conclusions relating to SME policy work

- a reluctance of Phare to make its funding for programmes conditional on greater government participation which would result in greater involvement of the Ministry of Economy in the funding of on-going projects, initiated by Phare
- with the PMU being located in the National Agency, there may have been a danger that Phare has given too much support to the development of Agency-run programmes without perhaps giving technical support to help the Ministry address some key policy, legislative and regulatory issues. This may be because of the somewhat isolated position that the Department of SMEs appears to be in, relative to the National Agency.

The other important design consideration relates to the relationship between the National Agency and the Ministry. Whilst all agree that relationships between both bodies are sound, it is important to ask whether the formation of a National Agency, has tended to eclipse the roles and responsibilities normally played by the Ministry: the National Agency fully understands the limits of its role and deliberately distances itself from policy unless invited to comment. But the Ministry has only a small staff of people to deal with SME issues, it has no direct access to Phare funds and appears to have no budget to commission work. It is reliant on Agency staff, backed up with Agency funded technical assistance to undertake new work, and is dependent on Agency resources being available.

The other area of concern is the lack of an independent unit to undertake research, monitoring and analysis of programmes. This is urgently needed to help the Agency (and Phare) ensure that resources are appropriately targeted. There is also a need to assist the Ministry, the National Agency and the various lobbying groups in the provision of economic evidence to support the case for more funds or for changes in the legislation in favour of SMEs.

Was this an appropriate programme for Phare?

It is generally believed that without sustained external support, the range of interlocking services now in place to support SME development in Slovakia would not have been established. No other donor had the resources or the flexibility to develop such a broadly based support programme. Having established a network of national and local SME support services with Phare's support, it has enabled other foreign donors to participate within an integrated framework avoiding overlap and duplication. From the outset, Phare adopted a holistic view towards the design of programmes for SMEs, playing a more active role in policy-making than normal.

Efficiency

The overall efficiency of the Agency in the design, management and monitoring of projects, assessed in terms of the rate of disbursement of its funds to its partners, has been very good. With an uneven flow of funds from Phare, it appears to have allocated resources fairly and efficiently, and has broadly been successful in managing its cash flow so as to maintain a continuity of funding to its partners responsible for delivery.

The efficiency of the Agency's overall Phare SME programme has lacked continuity due to the frequent changes in the Commission's Task Managers: the Agency has worked with five different Task Managers since 1993 each with their own perceptions and priorities. At the same time, priorities and funding for SME programmes have also been effected by changes in policies and priorities for the overall allocation of Phare funds.

In the time available for this evaluation, it has not been possible to consider the relative value or cost effectiveness of each of the services provided by the National Agency. The evaluation has focused on the resources allocated to the business support network. Whilst basic data was collected on the main projects run by the Agency itself (which is summarised in Section 2.4 above), it has not been possible to carry out a full evaluation of each of these projects. However, it was clear that the National Agency needs to review the relative outputs and value of each of its services to see whether it is appropriate to maintain all of them at the current level.

The staff seemed to be well motivated and generally appeared to have a good understanding of their subject, though, in a few instances, there appeared to be danger that some staff were too focused on administering their projects and not giving enough attention to addressing the priority needs of SMEs.

The main technical assistance took place during 1992 and 1993 during the design and setting up phase. It consisted of a two-year contract involving two full time people to help to establish the pilot RAICs and the Agency. Since that date technical assistance has been almost entirely limited to short term contracts relating to specific Agency projects, generally involving project design, staff training or performance monitoring. There are several areas where the Agency and the network might have benefited from more technical assistance, particularly in the areas of target setting, performance monitoring, forward planning and priority setting.

Effectiveness

Phare's early technical support has made a significant contribution to the establishment of a self sufficient national body for SME development, which has developed the skills and experience to plan, implement and monitor a wide range of SME support programmes. Whilst it has the resources to purchase additional external assistance, by and large, it is now self sufficient and only engages foreign specialists for specific short term inputs, where external experience is thought to be of value.

Now, most of the Phare's support involves the provision of funds to cover operating costs (rather than the transfer of know-how). The main beneficiaries have been the staff in the Agency and the network, who have built up a substantial body of experience as a result of the funding provided by Phare. How far this has been reflected in improved performance of the end customers, the SMEs, appears to vary from project to project. The effectiveness of one the Agency's main programmes, Phare support for the provision of business support services through the RAICs, is reviewed in section 4.4 below.

Impact (spill over effects)

There are many instances where the National Agency has influenced other bodies, (Ministries, banks, employers organisations, foreign donors etc) that SMEs are already a vital part of the national economy, which could play a more significant role, with appropriate support. During the General Election campaign in October 1998, all the main political parties included policies for SME development as part of their manifestos. The work that the National Agency has undertaken directly, and by working with the various unions and associations of entrepreneurs has played a significant part in lifting the profile of SMEs amongst the main political parties.

However, within government, there is little tangible evidence of change, though, there is now a very much greater awareness about SMEs and the special problems they face.

Despite the importance attached by the National Agency to public relations, a number of outside observers felt however, that the National Agency may be in danger of loosing its high profile as an authority on SME developments, which it built up very quickly in the early years. Marketing, public relations and regular work with the media, backed up by sound research, is clearly a function of the National Agency that has to be maintained at a high level if it is to maintain its authoritative position.

Sustainability

The legal structure of the National Agency is clear. The Agency is developing sound departmental structures and management systems, and many of the staff have a good understanding and have gained practical experience in developing programmes for SMEs. The most serious threat relates to funding. It will be increasingly important that the government increases its contribution to the core programmes run by the Agency, to enable the Agency to shift the emphasis of its Phare funded work towards meeting the Acquis criteria and strengthening the competitive performance of small firms.

In the last 12-18 months several senior staff have left the Agency for promotion and salary related reasons. The sustainability of the National Agency is very dependent on being able to recruit and retain staff with a high level of ability, vision and commitment. This will be dependent on the future reputation and standing of the National Agency and its ability to maintain a competitive salary structure.

Conclusions

Table 4.2 below summarises the evaluation of the Phare's support for the formation and development of the National Agency.

Table 4.2: Summary Evaluation of the National Agency for the Development of SMEs

Evaluation Measure	Comment	Rating
Relevance to government policy	Supported and co-funded by Government	4
Relevance of the design	Original design appropriate to the needs and local structure at the time	4
Efficiency	An efficient team with good project management skills, who are successfully managing a wide range of projects according to well developed plans	3.5
Effectiveness	A self-contained organisation which has developed the skills and experience to fulfil its objectives. A critical assessment of its projects is needed to assess which offer the best value for money	3.5
Impact	Has made a significant difference to the raising of SME related issues and has made some improvements to the overall operating environment for SMEs. But there are signs that its influence and profile may be reducing	3.0
Sustainability	Future sustainability will depend on an increased level of funding from the government, which it expects to obtain. Its future will depend on being able to retain high quality staff in key roles. This will depend on the availability and funding conditions so that the National Agency can continue to pay competitive salaries to staff	3.0
Total	**A relevant body playing a useful role in the development of the SME support services**	**3.5**

Note: rating based on EU consultant's judgement, on a scale of 5 (high) to 1 (low)

With scarce resources, the Agency needs to develop a rationale for optimising its resources in order to maintain an appropriate balance between its various activities. There is a danger that the delivery of its own in-house services may take a disproportionate amount of management time and resources, at the expense of those areas where it acts in a development, promotional or facilitation capacity.

In particular, the National Agency needs to give more attention to:

- improving the quality of research and analysis work to inform policy and ensure that the most critical priorities are addressed, particularly in the regulatory and financial areas
- the provision of added value services which meets the needs of the advisory network and strengthens its capacity to work in greater depth with SMEs as part of an integrated local and regional development strategy.

The National Agency will need to carefully work out its relationship with any National Regional Development Body, if one is established. This may not be particularly easy as the background and culture of the people in the two agencies is likely to be very different. Whilst those engaged in regional policy are likely to come from a planning and academic background, staff in the National Agency tend to be more commercially focused.

4.4 Regional Advisory and Information Centres

Objective, logical framework, project selection and methodology

The third programme to be evaluated within the institutional area covers Phare's support for the establishment and running of the RAICs and BICs. The main objective of these centres has been to increase the rate of formation, growth and survival of SMEs in defined local areas by providing information, advice and training on an affordable basis. A Logical Framework has been developed for the Centres with key evaluation questions (see Appendix D).

The evaluation followed the same approach that was adopted for reviewing the Support Loan Programme. One RAIC was selected for the detailed review, and within the RAIC a sample of 7 clients were interviewed. The RAIC at Nitra was selected because it was one of the original pilots, and in terms of performance, the National Agency felt that it was about average.

Nitra Region

One of eight regions, Nitra lies in the South West of the country on the Hungarian border. The region has a population of 715,000, 5,000 companies and 37,000 registered self-employed people. Administratively, there are 345 elected municipalities (15 of which are towns and cities), and seven districts with administrations appointed and administered by the Ministry of Interior, and a new (unelected) regional administration set up in 1996. The region is essentially rural with a large number of small towns and villages. Only 49% of the population are classified as urban: Nitra is the largest town with a population of 87,000.

Though there are not many large enterprises, employment and the economies of many of the small towns are frequently dependent on their survival. Many are still state owned enterprises which have been in decline and may face closure, leading to sharp reductions in purchasing power and increases in unemployment, which has not been fully offset by the small firm sector.

Table 4.3: Size distribution of enterprises in Nitra Region

Size (employees)	Self employed	Legal Entities 0-9	10-99	100-499	>500	Total
Number of enterprises	37,600	6,437	1,295	312	49	8,093
Distribution of employment by size of enterprise	13.5%	5.9%	19.3%	33.5%	27.8%	100%

Note: these figures include 2,095 not for profit organisations and 124 state owned enterprises.

In terms of sectors, the most important are agriculture and food processing (40% of enterprises), manufacturing (30%) and tourism (10%). The region's SMEs are serviced by two RAICs, one at Nitra, covering the major part of the region with branches at two other locations, and a smaller RAIC in Karmono, servicing SMEs in the southern part of Nitra and Trnava Regions. The Nitra RAIC which started operations in 1992, was set up as a legal association with eight members, including Nitra Municipality, the Regional Labour Office, the Entrepreneurs Association, two banks, and two agricultural educational institutions. The RAIC is centrally located in the pedestrian area in the centre of Nitra, though it is difficult to find due to poor signage. The premises are rented on preferential terms from the Municipality and include four offices and a substantial training room. The staff has grow from 2 in 1992 to 5 in 1994 and 8 in 1997/8: now cut back to six people - due to reduced funding - the Director, a deputy, and four consultants, including the book-keeper.

Inputs: funding and technical assistance:

Table 4.3 below summaries the funding and main outputs of the Centre since its formation. Phare has been a major source of funding since its formation, decreasing from 85% at the outset to 43% in 1997. Initially Phare funds contributed towards operating expenses, but after 1995, established Centres entered into annual service contracts, based on agreed outputs (reimbursed at a fixed rate of Euro 10 per hour) up to a maximum budget level. In many instances, these contracts were not made on a regular and consistent basis due to funding delays. In consequence, RAIC Managers have had difficulty in preparing forward plans.

Nitra RAIC has had support from four other sources:

- The Nitra District Administration made a regular contribution of around SK 250,000 (Euro 6,500) per year to cover the cost of two advisers. This ceased at the end of 1996 when the Nitra Regional Administration was set up.
- Contract work for the Regional Labour Office and CEPAC providing training for unemployed people wishing to start a business
- Donations from the City of Nitra (most years) and Peace Corps (in 1994 only)
- Client contribution: these have grown from 6% in the first four years of operation to 18% in 1996 and 1997.

Up until 1997, with a rising income, the RAIC was able to expand by increasing the number of advisers and by opening sub offices. A high percentage of expenditure is fixed (made up of salaries, rent and office overheads) so any major loss of income can only be contained by reducing staff numbers and the capacity of the Centre.

Table 4.4: Income and performance outputs of Nitra RAIC

	1992	1993	1994	1995	1996	1997
INCOME (Euro)						
Nitra District Authority/ Ministry of Interior	1,900	5,300	6,700	5,700	5,500	-
Labour Office		2,400	600	600		
CEPAC Training of unemployed	-	-	-	10,600	16,000	21,300
Local and foreign donors	1,400	-	7,500	300	2,100	1,900
Client income	1,200	1,300	4,600	2,000	14,800	16,000
Phare	24.800	40,000	35,000	32,000	28,000	30,000
Total	**29,300**	**49,000**	**54,400**	**51,200**	**66,400**	**69,200**
% income from Phare	85%	82%	64%	62%	42%	43%
% client income	4%	3%	8%	4%	22%	23%
% other income	11%	15%	28%	34%	36%	34%
Number of staff	2	5	5	6	7	8
Number of advisers	2	4	4	5	6	6
OUTPUTS						
Clients	122	413	624	919	718	723
Proportion of clients which are start ups	70%	69%	35%	57%	73%	66%
Proportion of full paying clients	17%	18%	2%	23%	25%	18%
Clients per adviser	61	103	156	180	120	120
Training courses	4	7	8	7	3	4
Business plans	6	41	79	95	65	81
Business plan evaluation	-	-	79	25	45	17
Small and support loans	-	-	11	8	45	17
New firms formed	2	20	35	53	79	71
New jobs from start ups	5	42	248	182	224	201

Note: In Nitra, in most years total annual income = total annual expenditure, as the RAIC has not made surpluses and has not the reserves to finance deficits.

Outputs
Outputs are determined by client demand, the depth of work involved and the number of staff in the Centre. Whilst start ups has been a prime focus, there has been a significant shift towards existing firms, as reflected by the mix of new clients, around (110 firms), which came to the centre in 1997; 19% were start ups, 32% were established companies with less than 10 employees, 36% were small companies (10-24 employees) and 13% employed more than 25 people. The table below provides details of all the clients handled by the Centre since its formation. The trend has been to develop links with bigger and older enterprises, partly because they offer the most scope for being able to obtain payments for services, (as reflected by the increase in client income). But it also reflects the growing number of established SMEs in the local area, who require different and more sophisticated services.

Table 4.5: Client mix 1992-1998(1) - 3870 cases

Sector	%	Size of enterprise	%	Age of enterprise	%
Production	24	0-9 employees	72	Less than 1 year	62
Wholesale trade	13	10-24	17	2	20
Retail trade	6	25-250	7	3	9
Services	36	>250	4	4 - 8 year old	5
				>8	4

In terms of client mix, 80% are under 2 years old and employ less than 9 people, and only 4% (an average of 23 client enquiries a year are from large enterprises (mainly state or ex-state enterprises) with more than 250 employees and older than 8 years.

Most of the counselling work seems to be reactive: the Centre spends very little on marketing, relying on word or mouth and press coverage. 62% of counselling sessions are information related, the remainder involve the provision of professional advice, particularly relating to start up procedures, legal issues and taxation. The Centre is involved in project work with a small portion of clients (perhaps 15-20%), covering business plans, market studies, Europartinariat, the sub- contract programme and exhibitions.

A significant number of enquiries are funding related. When credit was available through the Support Loan Programme, a greater proportion of time was engaged in business plan preparation and evaluation; over the three years 1995-97, a total of 241 business plans were put together, generally for funding applications, - 42% relating to manufacturing businesses, 20% for trading activities and 38% for services.

The Centre assessed 166 business plans for the banks which resulted in a total of 81 loans (49%), 11 small loans in 1994 (average size Euro 18,000) and 70 support loans (average Euro 80,000) between 1995 and 1997.

Between 1995 and 1997, the Centre has run 9 CEPAC funded training programmes for 129 unemployed people, resulting in 55 people starting a business. The Centre believes that much more could be done if start-up businesses had access to credit facilities. Nitra (as with most other Centres) undertakes very little seminars and training: a function of demand and the availability of staff with training skills.

Relevance
The rationale for the services of the RAICs in Slovakia is both clear and sound. There was very little prior knowledge or experience of setting up in business. But it was recognised that self-employment and small businesses provide a real option for people displaced by the

demise of large state owned enterprises. The aim of the RAICs is to use public funds to subsidise the provision of information, counselling and training services to start-ups and young companies, most of whom would not be able or willing to pay the full cost of such a service. Based on the experience in Western Europe, this, it was believed, would enhance their chances of survival, help some to grow and would stimulate people, particularly those facing redundancy, to consider starting their own business.

Whilst the focus, initially, was towards start-ups, through its funding contracts with RAICs, the National Agency is now encouraging more time to be spent with existing enterprises (both enterprises with growth potential and firms with the ability to pay). Thus in the first half of 1998, the proportion of counselling work with start-ups has reduced from 60% to 30% and with existing firms it has gone up from 40% to 70%. In part, this reflects a national economic priority to increase the number of firms employing more than 10 people, as these, it is believed, are under represented and are more likely to grow through exports and thus create new jobs. However, the success of this strategy will depend on the advisory skills of the centres, and their ability to add value and support the performance of existing enterprises, a job which is more demanding and requires a higher order of business and counselling skills.

The switch to output related funding in 1995 was a positive step. The funding system developed by the National Agency provides sufficient flexibility for each Centre to propose the client mix that best suits its skills base and local needs. The National Agency chose to channel resources for business support services through a limited number of dedicated outlets, rather than putting the service out to competitive tender. This has provided a stability and continuity enabling existing centres to consolidate their position and acquire experience. But with reasonably secure funding, there is a danger that some Centres may have learnt to work ‘the system’ and may have become rather complacent. Some Centres are experimenting with accreditation. Whilst it is aware of the danger of complacency and the value of accreditation, the National Agency is reluctant to intervene too directly as each RAIC is (nominally) run as an independent agency. Up till now, the National Agency has been reluctant to put the contracts out to tender, because it feels that this might lead to short-termism as agencies shift their emphasis towards becoming 'contract hunters'. There is also concern that some areas, which need business support services, would loose out if their Centre was less successful than others in winning contracts.

The structure of the Nitra RAIC as a non profit “legal association” with members drawn from local authorities, educational institutions, the Entrepreneurs Association, banks and the District Labour Office has enabled it to mobilise a number of important local and regional bodies, some of whom have contributed in-kind support to the RAIC. It is important to bear in mind that when the RAIC was established, there were 345 elected municipalities in the region (15 of which are towns) and 6 districts, (administrations funded from the Ministry of Interior) which were subsequently enlarged to 7. In 1996, further local government re-organisation has led to the setting up of the Nitra Regional Administration (encompassing the 7 districts). In 1997, a Regional Development Agency had been established with 30 members, supported by the Regional Development Office of the Regional Administration. But with only a small budget and few staff, its role, to date, has been limited. The RAIC has developed good working relationships with the Regional and District Administrations and the larger municipalities (as well as the District Labour Offices), and is aware that as local and regional programmes develop, it will be important to be closely involved.

The choice of physical location of RAICs has been influenced by the availability of support from local authorities. A RAIC was set up in Nitra, because financial support and a building were provided by the District and the City authorities from the outset. Due to the size of the region and local unemployment pressures, the RAIC has been encouraged to offer its counselling services through sub offices in two other locations.

Efficiency
Comparatively high levels of penetration are being achieved by the RAIC, despite the size of the region being covered, as summarised in the table below. It compares the RAIC's client numbers with start-ups in the region, based on a national average of 30,000 start-ups per year. With 13% of the national population, there would be around 4,000 start-ups a year in Nitra.

Table 4.6: Level of penetration of Nitra RAIC amongst start-ups

	Production	Trade	Services	Total
% new starts nationally	14.9%	35.8%	37.4%	100%
Estimated annual number of start ups in Nitra Region	1072	1,432	1,496	4,000
Start up clients of RAIC 1997	200	76	209	485
% penetration	19%	5%	14%	12%

Given the importance of being attached nationally and locally to supporting manufacturing and service businesses, the levels of penetration in these two sectors is encouraging high.

Excluding the ten week training courses, which take up a considerable amount of advisers' time, each adviser has had a counselling case load varying from 120 to 180 cases per year together with around 14 business plans a year - an average of around 10-15 clients + one business plan a month per adviser.

Table 4.7 allocates the total running costs of the RAIC between 1995 and 1997 across the estimated hourly input for each activity. This is based on the actual figures for counselling in 1997 adjusted for fee paid work, 35 hours per business plan, 12 hours assessing a business plan and 400 hours per training course.

Table 4.7: Unit costs of Nitra RAIC service (1995-7)

	Numbers in 1995-97	Hours per unit	No of hours	%	Total Cost Euro	Average unit cost Euro	Phare subsidy (48%) Euro
Counselling	2,184 clients	1997 data	3,748	22	38,900	Euro 18 per client	Euro 9 per client
Business plans	241 plans	35 hrs/ plan	8,435	50	88,400	Euro 370	Euro 178 per plan
Evaluation of plan	87 plans	12 hrs / plan	1,044	6	10,600	Euro 122	Euro 58 per plan
Training	9 courses 129 students 55 start ups	400 hrs /course	3,600	22	38,900	Euro 300 per participant Euro 707 per start up	Euro 144 per participant, Euro 339 per start up
Total			16,827	100	176,800		

From these figures, the average staff utilisation time on recorded client work is around 54%. This is based on six advisers each working an average of 1,740 hours a year. From these figures the unit costs of counselling, preparing a business plan and training have been estimated. The average cost for advisory work is around Euro 18 per client with the Phare contribution amounting to around Euro 9 per client. The table also provides a clear picture of how the RAIC allocates its time across the main areas of activity.

These costs ignore training inputs by The National Agency staff and foreign experts. Agency staff had access to foreign technical assistance during the start-up phase in 1993 for training and mentoring support in Slovakia and a placement to an Enterprise Agency in the UK. Subsequently, new staff have attended training courses organised by the National Agency. It appears that the RAIC has received no other substantial technical assistance since the start up phase. Over the six-year operating period, 5 staff have left the Centre, an average annual turnover of 15% per year.

Client income has been a feature of the programme since its inception. This has been encouraged through bonus payments to staff, based on the level of private sector income that they attract. Despite this incentive, there is no evidence that it has distorted the client base in favour of paid clients.

Effectiveness

The most important output of the Centre at Nitra has been business plans, which make up around 50% of the workload. During the three years to the end of 1997, 241 Business Plans were developed, 203 new businesses were assisted (including 55 from the training programme) and 46 businesses used the plans to raise money from the banks under the Loan Support Programme. The start ups (most of which will have had access to the Centre's training and help on their business plans) are estimated to have created around 600 jobs, a crude cost of around Euro 212 per job (excluding multiplier and displacement factors).

The Training Programmes being funded by CEPAC Slovakia, have shown particularly promising results in terms of new business formations. In the three years to the end of 1997, there have been 129 participants on 9 courses. 55 people have formed businesses to date; this will increase to around 70-75 businesses, creating around 95 jobs as a number of participants from later courses will also start a business. The crude cost per business Euro 410.

The analysis in table 4.4, above, indicates that the Centre's advice and information services are being used almost exclusively by start ups and young businesses predominately in the manufacturing and service sectors, for whom the service was designed. Regrettably we were unable to analyse the survival and development of the Centre's clients, except those that obtained a Support Loan via banks. So it is not possible to consider with any accuracy the impact of the Centre on the performance of its clients.

The case studies in Appendix G, are based on interviews with six clients of the Centre. They provide examples of the type of assistance that the Centre has provided its clients. The effectiveness of the Centre is summarised in table 4.8 below:

Table 4.8: Effectiveness rating of firms receiving services from the Centre

Enterprise	Product	Service provided	Assessment	Rating 1-5
Mr P	Advertising/ design studio	Business plan for finance	Acceptable business plan for the bank; but the client opted for lease finance	2
Mr Q	Bakery	Equipment did not meet client's needs	The Centre helped the client to resolve serious legal problems and raise a second loan, without which he would have failed	5
Company R	Lights and controls	A growth firm with export prospects	Centre encouraged the company to participate in Europartinariat, leading to new export contacts	3
Mr S	Coffins	Information	Values the Centre as a source of information	3
Company T	Road trailers	Wanted foreign contacts	Attended Europartinariat which was helpful	3
Business U	Computer training	Start up advice	Made good use of Centre for information, advice on legal structure and help in preparing a business plan to raise money from the bank.	3
Total	**6 businesses**			**3.2**

There seems to be no undue pressure on demand for the Centre's services, so that they have not had the need or opportunity to target their time on those businesses likely to give the best pay back, in terms of growth and jobs. This suggests that perhaps not sufficient resources are being allocated to marketing and promotion. This situation would change if the Centre put more time into following up its key clients and offering diagnostic services and mentoring advice, particularly to those businesses who are at an early stage in their development.

Impact

The role of the Centre as a source of advice and information for small businesses is gradually becoming better known in the region, as evidenced by the steady growth in enquiries since its formation. The Centre however acknowledges that its profile and reputation locally could be improved. Marketing and promotion have only been possible when funds were earmarked for this activity. The RAIC felt that the National Agency needs to do more to promote the services of the network.

The main impact of Phare funding has been to provide an opportunity for RAIC staff to build up a body of experience as advisers and trainers through providing services to start ups and existing companies.

The Phare funding formula provides for, and encourages RAICs to build up a body of external experts whom it can engage to assist clients with specialist problems. Though the budget has not been large, it has ensured that the RAICs have developed networks of private sector specialists. Nitra have built up a network of around 15 experts to whom it will regularly refer clients.

The RAIC's use of the CEPAC training programme to help unemployed people into business has had a significant impact on promoting the opportunities of entrepreneurship, particularly in communities faced with major plant closures. However, apart from the extended start up programmes, little progress seems to have been made to run entrepreneurship workshops, seminars and courses to enhance awareness and owner managers and staff in the basic skills of business management.

Through its work in different parts of the region, the RAIC has become increasingly aware of developments in the local and regional economy. But neither the RAIC, nor the various administrations have yet undertaken any economic assessment work leading to the development of local economic priorities and plans for their areas. With the greater importance now being attached to regional economic development, the RAIC is in a strong position to contribute.

The RAIC works closely with the region office of the Entrepreneurs Association and to a less an extent with the regional office of the Chamber of Commerce, particularly on export related issues. It also promotes and makes use of some of the services provided by the National Agency, the most relevant of which are the Support Loan Programme and the Euro Info Correspondence Centre. Attempts were made to promote the Spin off Programme with large enterprises in the region without success. The Nitra RAIC makes little use of the Subcontract Exchange Slovakia, Entrepreneur Information Service or the Seed Capital Company.

Sustainability
Since the formation of the advisory network, staff in both the National Agency and in Nitra were clear that to fulfil its remit, the RAIC/BIC network would be dependent on public funding. Whilst the European Commission and the Government arrived at an agreement about the funding of the National Agency, the funding position of the network has always been an area of uncertainty. In 1995, the National Agency prepared an assessment on the network and put together proposals designed to address the funding issue, but this was never taken up by Phare or the Ministry of Economy. The issue was again raised in the Evaluation of the Phare SME Programme in June 1996. Until now, no money has been allocated to the network by the Ministry of Economy, partly, it would appear, because there has always been money for the network from Phare and other sources.

Unlike the funding for the Support Loan Programme, Phare has never attached any conditionality to the funding for the Network. Though initially painful, conditionality would have strengthened the bargaining position of the National Agency in persuading the Ministry of Economy to establish a regular budget allocation for the network.

By intelligent planning, the National Agency has tried to maintain the annual funding to the RAICs at a prudent level, so as to maintain a balance of unspent resources to counter a lack of allocation (as occurred in 1996 when there was no Financial Memorandum for Slovakia) or cash flow delays. The National Agency expects that the current allocation in the 1997 Financial Memorandum will be fully disbursed by around May 1999. Both Phare and the National Agency have recognised the need to resolve the uncertainty; a review has recently been commissioned to make recommendations on the issue of sustainability of the Network.

Meanwhile, with the encouragement of the National Agency, the RAICs are already taking precautions to try to increase their workflow from larger enterprises able to pay. Though it is trying to secure more fee-paying work, the Nitra RAIC is not happy about this approach as it believes that its remit is to meet the demands of entrepreneurs unable to pay the full market price. Whilst Nitra’s private sector earnings have increased, and now account for 23% of income, there has been no significant difference in the output or client mix. But unless it can find a way of maintaining its current level of income, it will have to reduce in size and limit its work with its primary target group of clients.

The legal structure of the RAICs would appear to be sound. They provide a framework for greater participation by the Regional, District and larger Municipalities as they become more actively engaged in local and regional economic development.

Conclusions

Table 4.9 below summarises the evaluation of the Phare's support to the formation and development of the RAICs.

Table 4.9: Summary Evaluation of the Regional Advisory and Information Centres

Evaluation Measure	Comment	Rating
Relevance to government policy	Supported by Government (without funding)	3
Relevance of the design	Original design appropriate to the needs and local structure at the time	4
Efficiency	Tangible outputs	3
Effectiveness	Effectiveness based on interviews with six enterprises	3.2
Impact	A primary focus for SME development in the local area, which has secured the support of other relevant bodies	3
Sustainability	Future sustainability will depend on the availability of public sector funding.	2
Total	A relevant body playing a useful role in the development of the local and regional economy	3.0

Note: rating based on EU consultant's judgement, on a scale of 5 (high) to 1 (low)

The network represents a major development achievement, which would not have happened without Phare's support. But its survival will depend on an orderly withdrawal strategy being worked out with the Government if it is to continue its public service role of providing services to start ups and very young enterprises. Shortly before the October election, the Ministry of Economy agreed in principle to include, for the first time, a provision of SK 17m (Euro 450,000) in their 1999 budget bid. If the bid is accepted, this would contribute around 30% to the cost of the RAICs and BICs.

The National Agency and the RAIC Managers are confident that with a change of government and with the emphasis from Brussels on regional development and programmes to strengthen the competitiveness of SMEs, a solution can be found. The National Agency believes that all the RAIC managers are very committed to the public service role of the network and none are contemplating the development of their RAICs as fee paying consultancy operations.

The RAICs and BICs will need to position themselves carefully with respect to the new Regional Development Agencies, who may get substantially increased powers and funding through the European Structural funds. With regional development programmes likely to be run by planners and infrastructure specialists and directed from another Ministry, staff in the National Agency and RAICs, will need to become familiar with the broader issues of economic development. Whilst the RAICs have an advantage of being established in each region, unless they broaden their horizon, they could find themselves marginalised by these new bodies.

There is perhaps too much emphasis, in the reporting system, on overall numbers with insufficient attention being given to the types of clients and depth of services being provided. New reporting arrangements should enable the National Agency and Centres to give more attention to monitoring the level and results of follow up work with existing clients (particularly start ups and loan cases), to assess the progress of the Centre's priority group of clients (particularly in terms of survival and growth). Currently, Centres are assessed and rewarded if they meet targets in terms of the number of information/advice sessions regardless of the nature and depth of work being undertaken. Whilst they clearly need to respond to all information enquiries, Centres need to be encouraged to work more with those enterprises that are likely to have most impact in the local economy, in terms of jobs and sectors, as well as work in those priority areas where the need is greatest.

Up till now, most of the National Agency contracts with the RAICs are of an equal value. The National Agency should now be considering whether resources could be better utilised by allocating them according to the needs of the regions (size, enterprise potential etc), and the comparative performance of the RAIC/BICs. A regular independent monitoring and impact assessment study should be commissioned, which considers the economic performance of the Centre, including the real benefits to end clients, enabling Centres to be compared. That comparison might then be one of the factors that determines how future resources should be distributed. It could also lead to the setting up of benchmarks to enable each Centre to compare its performance with the best and with itself, over time. The comparative value of training and counselling needs to be considered to see whether the balance in resources between them is still appropriate.

Now that the network has been established the National Agency and the RAICs need to consider what additional services are needed by their clients and which organisation is best placed to undertake this work on behalf of the network. A start has already been made in the area of quality, where the RAIC at Poprad has taken the lead on ISO 9000 and become the first certified centre, with two other Centres offering ISO 9000 advice and training.

Chapter 5 Conclusions and Recommendations

In this final chapter, we review what stage SME development in Slovakia has reached and identify opportunities and priorities where the European Union could further assist the development of SMEs as part of its strategy to accelerate transition and lead to accession to the EU.

When account is taken of the historical development of the post war Slovak economy towards large state owned enterprises engaged in heavy industry, engineering and armaments, the progress in terms of entrepreneurship and small business development has been quite remarkable. However, when viewed against the needs of the country to develop competitive export orientated enterprises, there is still much to be done. In viewing future priorities, the recent OECD Forum on Entrepreneurship and Enterprise Development's Guidelines and Recommendations have been used as a framework for assessing future options and priorities. Our comments are set in the context of the EU priorities relating to accession and regional economic development, and the recent EU/EBRD horizontal financing facility which was approved earlier this year.

The Guideline has been structured around the following key topic areas:

- Financial Instruments for New and Small Businesses
- Institutionalisation of Enterprise Development Policy
- Tax Policy for Small Business
- Rule of Law and Regulation
- Advisory Services for New and Small Businesses

Financial Instruments

Insufficient attention is being given by the Ministries of Economy and Finance, the National Bank and the National Agency for SME Development to set up and monitor on a regular basis, the patterns of credit flowing to SMEs at different stages of development. Whilst there is limited anecdotal information there is no sound knowledge of what is taking place. For example, it is not possible to determine to what extent there is evidence of market failure in different parts of the country, or in certain industrial sectors and whether this is due to a reluctance of banks to lend small amounts of money, the price and terms or a lack of demand from bankable businesses. Without this base line information, it is not possible to target public sector interventions and assess its effect. This is particularly important in the context of accession, as currently there is a need to target support on those enterprises, which have the capacity to compete effectively within the Single Market.

The availability of credit for micro firms and small firms continues to be a constraint on economic development. There is a good case for enlarging the Support Loan Programme, involving a risk sharing partnership between Phare, the government and four banks providing term loans. These loans offer good value for money compared with loans made in other countries on the grounds that with a three to one leverage and the links established with the

RAICs to help companies become 'investment ready', the net cost to Phare (after taking account of losses and the interest rate subsidy) has been relatively low. It could be improved by introducing a clearer additionality clause in the lending conditions, which would ensure that loans went to those firms unable to raise funds from the banking sector.

Some banks may show interest in the EU/EBRD Horizontal SME facility, as there appears to be an overall shortage of credit due to a lack of funds in the banking system. But it is not clear to what extent the banks will in practice use this money, bearing in mind that they are required to carry 100% of the risk. If the programme is introduced in Slovakia, there would be advantages in linking the National Agency and the RAICs into the programme to ensure that they take an active part in helping enterprises prepare their business plans and monitoring performance subsequently, providing advice and support as required as was done with the EBRD's Small Loan Programme in Russia.

There is a strong case to expand the micro credit programme, which was piloted through three RAICs. There are no micro credit facilities to help self employed people to get into business and the sums of money are too small for it to be covered by the SME horizontal financial facility. This would be particularly important in those regions facing growing unemployment arising from the privatisation and restructuring of the large state owned enterprises. The RAICs and BICs are well placed to administer the scheme along the lines developed in Hungary, where small businesses get considerable benefit from being able to obtain business advice, training and a small loan from a single agency.

A critical appraisal is needed to establish how the loan guarantee fund can be adjusted to ensure that it has the backing of the banks and plays a more effective role in providing guarantees to bankable projects where there is a shortage of collateral. One option would be to develop loan guarantees as part of regional development programmes.

There is evidence of a shortage of small amounts of equity capital (i.e. less than Euro 150,000 per investment) for seed money for new projects, venture funding for growing firms and development of capital where the level of fixed investment is modest. One option is to develop the Seed Capital Company, which was started with Phare resources. The fund needs to be enlarged so that it can offer much larger deals. It also needs to work more closely with the RAICs to promote an understanding of the role of equity funding and identify 'investment ready' projects for the Seed Capital Co. It may be necessary to train specialists in the larger RAICs to play this role.

Tax Policy for Small Business

Comparatively little progress has been made to secure the backing of the Ministry of Finance in reviewing and developing coherent tax policies to reduce the burden of taxation on small businesses. Significantly almost no Phare resources have been allocated to this critical work despite the impact of taxation policy on SME development, based on the principle that the government will potentially collect more revenue if the tax policies are structured to encourage the enterprise sector to flourish. Progress needs to be made on improving the tax climate by simplifying the rules applied to these businesses, reducing the compliance burden and promoting transparency and stability of the tax regime. This can be achieved by reducing the number of taxes, eliminating small taxes which cost more to collect that they raise in revenue, ensure that the overall tax burden is less than about 50% and avoid complex rules and procedures. If the burdens of taxation are too great, it will encourage too many businesses into the shadow economy, which is counter productive to the tax authorities, as it may lead to a reduction in total tax revenue. More needs to be done to publicise tax policies amongst SMEs, and pressure needs to be placed on the Ministry of Finance to reduce the number of changes in the tax system, recognising that SMEs lack the time to master and comply with all the tax obligations. More needs to be done to train local tax offices in compliance so that more uniform and transparent standards are developed which take account of the skills and capability of SMEs to meet fulfil the tax rules.

Whilst progress has been made in improving the representational arrangements, there is now a need for this to be recognised within Government. Efforts need to be made to structure closer working and genuine consultation arrangements between the administrators of the tax regime and SME representative organisations in order to identify system improvements which will result in greater tax compliance. In these discussion s, greater attention needs to be given to extending tax exemptions where the level of tax collected is below the cost of collection, thus reducing the overall burden without significantly reducing the revenue generated.

EU assistance in this vital area would be valuable, perhaps through a horizontal programme involving several countries where the review and reform of taxation rules and regulations has proved to be particularly difficult. Up till now despite interventions by staff from the Ministry of Economy and NADSME, comparatively little progress has been madein persuading the Ministry of Finance of the relationship of tax reform and enterprise development. With the financial support from the EU, greater emphasis would be placed on this area, which could result in a step change in the climate for SME development.

Institutionalisation of Enterprise Development Policy

Slovakia has made significant progress in establishing structures for the development of SME policies, through the work of the SME Department in the Ministry of Economy, and, with Phare support, the establishment of NADSME together with the strengthening of the representative organisations. There is now a case for enlarging and strengthening the research and policy development capacities both within the Ministry and NADSME, clarifying their relative roles and responsibilities, and establishing closer working relationships in practice so that both are following a common agenda. Whilst the ‘State of SMEs in Slovakia’ is a valuable starting point, there is now a need for much more thorough research and evaluation to assess specific policy and regulatory issues effecting SMEs.

There is also a need for more research to identify how SMEs could play a greater role in the national, regional and local economies and pin-point the main barriers that are hindering development, in terms of size and age of enterprises and particular sectors with greatest growth potential. Targets in terms of output, numbers and jobs need to be set to evaluate the contribution of specific policies and initiatives against which resources can be allocated.

To improve the interface between SMEs and government departments, there is a need to establish a high level SME Council with the capacity to initiate inter-departmental task teams to review, co-ordinate and develop more appropriate rules and regulations which impact on SMEs.

There is an urgent need to ensure that the national, regional and local SME infrastructure is now reviewed and integrated into the new regional structures being developed with support from the EU, to enable the country to access and harness the EU's Structural Funds. It will be important to distinguish between the broader strategic roles of Regional Development Bodies and the operational and focused remit of RAICs and BICs. In future it will be necessary that the regional development bodies and local government, with EU backing, play a more active role in determining policy priorities of the RAICs and BICs in their area. With the reduced availability of Phare funding for RAICs though NADSME, regional and local bodies will need to provide a significantly larger share of their funding and at the same time ensure that their work is more closely monitored to ensure that the limited public sector funding available is used to undertake work of greatest benefit to the development of their region.

It will be necessary to strengthen the capacity of the Ministry and NADSME to collect relevant statistics and commission specific research to monitor the structure, performance and needs of SMEs, as a precursor leading to the refinement and development of SME policies. An example identified above relates to the availability and uptake of bank credit by SMEs at different stages of development.

Rule of Law and Regulation

Much work is still required to harmonise and simplify laws and regulations to facilitate enterprise. It is necessary to focus in particular on those laws and regulations, which give too much discretion to enforcing officials and result in bureaucracy and corruption. One area offering scope for early action is the need to review the complicated and time consuming procedures relating to business start ups, covering registration, licensing, tax, employment and national insurance procedures, many of which could be simplified or integrated into a single process. A programme of reform needs to be developed by the Council for SMEs (see above) based on collaborative work by ministry officials, NADSME and SME representative organisations to review and bring forward fully worked out solutions to reduce unnecessary 'red tape'.

Compliance is necessary if there is to be fair competition. Policy makers need to distinguish between minor misdemeanours and major infringements when reviewing legislation. Greater account needs to be taken between the difference between the informal economy (where businesses operate in the law but may be in breach of minor administrative regulations), the grey economy (where the activities are legal but there is some non compliance - often in the area of taxation) and the black economy where illegal and criminal activities are involved.

Greater attention is needed to improve the implementation of the law through a strengthening of the commercial judicial systems. Without a sound process for dealing rapidly with contract disputes, payment disputes and insolvency SMEs are particularly vulnerable to corruption and illegal trading. And this has a serious impact on their ability to borrow money from financial institutions.

Advisory Services for SMEs

With Phare support a sound network of advisory services has been established, but its future direction and funding is not secure. The most critical issues relate to long term financial sustainability, the range of services available and their quality. If they are to continue to perform the vital role of providing information, advice and training to start ups and micro and small firms who lack the resources to pay the full cost, then some form of public funding is essential. But it may be better to make the subsidy in the form of a voucher of a grant to the SME, with the RAICs charging the full cost of providing their services, so that both parties and more aware of the cost and value of the services on offer. This should involve a mix of central and local funding to ensure that the RAICs and BICs develop as local institutions accountable to local and regional communities within a national framework. All users of the service should be asked to contribute something to ensure that they attach value to what is being provided. The charge should reflect the nature of the support required and the stage of development of the enterprise. A more rigorous approach needs to be taken by the National Agency to ensure that they are obtaining value for money in relation to the contract that they place with the network. This would help to identify shortcomings in the quality and performance of the RAICs and identify where additional training would be beneficial. NADSME needs to commission independent regular surveys amongst SMEs to establish their information, advisory and training needs, identify gaps in provision and assess the effectiveness of the current network of private providers, the RAICs and the BICs.

There is a need for the National Agency to consider the benefits of introducing individual and centre accreditation as a means of raising the quality of the services on offer by RAICs. There is also a need for RAICs to have access to more specialist and higher quality staff to undertake higher level work targeted at the most successful firms in the region, who need to strengthen their competitive position in readiness for the Single Market. EU funding needs to be provided to NADSME and the Export Agency to develop joint programmes with the RAICs, the BICs and private sector consultants targeted at accession related issues, including product development productivity, quality, standards, export marketing strategy and procedures.

Appendix A

Evaluation methodology and approach

The Logical Framework Approach

The Logical Framework (LF) approach has become the *de facto* EC standard for project design, monitoring and evaluation. It is now widely used throughout most of the EC's domestic and external aid programmes. The LF is simply a method of classifying a chronological series of events in a project. It distinguishes between various stages in the production process that leads to the achievement of the objectives: preparation and design, delivery of inputs, activities, delivery of outputs, achievement of immediate and wider objectives, sustainability of achievements over time. One of the main advantages of the LF is that is forces the project designer - and the evaluator - to define these events and make their occurrence verifiable by means of a set of objective indicators and assumptions. This facilitates monitoring of implementation arrangements and evaluation of achievements. In fact, a general set of evaluation criteria can be readily derived from the 'project logic' reflected in the LF, as shown in Table A1.

The central point in the classification of events are the ***outputs*** of projects. Outputs are the final deliverables, the point at which the responsibility of the project management stops. In the case of institutional reform projects, outputs usually consist of trained human resources and proposals for legal, regulatory and organisational reform. Implementation of the reforms is usually not the responsibility of a project team; it is up to owners and decision makers in the beneficiary institution to do so. Some projects may include support in the implementation phase, but final responsibility for implementation can never be attributed to an external consultant or expert.

Outputs are generated by means of ***inputs***, which are used in activities. The Phare programme mainly delivers technical assistance inputs. In some cases, complementary equipment deliveries may also be included. Financial and physical investment inputs are, so far, rather limited under the Phare programme, although they may be important for some projects.

The ***efficiency*** criterion evaluates the transformation of inputs into outputs, both in quantitative (where feasible) and qualitative terms. These relate to such issues as the rate of disbursment, the number of people/organisation who have received the input (finance or know how) in relation to the public sector costs involved.

Once outputs have been delivered, they should contribute to the achievement of project objectives. Standard LF's identify objectives at two levels: immediate and wider objectives. More levels can be inserted where useful. Objectives should be formulated within reasonable 'distance' from the outputs. If not, too many noise factors will come in between and verification of the correlation between outputs and objectives becomes impossible.

Effectiveness assesses the extent to which outputs contribute to immediate objectives. Thus for financial projects or technical assistance (in terms of advice, training or information provision) to what extent did the support result in improved performance of the organisation that received the benefit?

Impact assesses the extent to which outputs contribute to wider objectives. In what measurable ways did the improvements in the recipients' performance result in wider, spill-over effects, such as providing a demonstration effect, raising awareness?

The ***sustainability*** criterion assesses the extent to which this impact is sustainable over a longer time horizon, particularly when Phare technical or financial assistance has come to an end.

Table A1: Logical Framework and derived Evaluation Criteria

Project Logic:	Evaluation criteria:	Indicators for institution building/reform projects:
Sustainable over time	**Sustainability**	Long-term viability factors
⇑		
Wider objectives	**Impact**	Spill over effects beyond the immediate recipients
⇑		
Immediate objectives	**Effectiveness**	Measurable changes in the recipient's performance as a result of the input
⇑		
Outputs	**Efficiency**	Amount of work undertaken, numbers of participants, and rate of disbursement in relation to the inputs
⇑		
Inputs		Time, effort and public sector cost of the inputs

Relevance Criterion

Apart from a project level evaluation, the LF methodology also allows for a programme or policy level approach, revolving around the *relevance* criterion. There are three aspects to relevance:

a) an assessment of the overall programme, including its project level components, with respect to the needs, policies and strategies of the country: *to what extent did the project meet the needs and priorities of the country?*

b) an assessment of the appropriateness of the programme and its projects: *to what extent was the design of the project appropriate?*

c) an assessment of Phare's comparative advantage in carrying out this programme: *should Phare be engaged in this work?*

Using these principals, logical frameworks have been constructed for each type of project being assessed: financial programmes, the provision of policy advice, support for the development of National Agencies, and the provision of business support services through Business Support Centres and through Business Innovation Centres. In each case the logical framework has been reconstructed to define the project, its inputs, outputs, immediate objectives and wider objectives. Against each evaluation criteria, the log frame sets out the key questions to be considered, verifiable indicators that should be used and the sources of information according to the summary table below:

Table A2: Standard Log frame table used for the Evaluation

<table>
<tr><th>Objectives</th><th>Evaluation Questions</th><th>Verifiable indicators</th><th>Sources of information</th></tr>
<tr><td colspan="2">Description of the project</td><td></td><td></td></tr>
<tr><td colspan="2"></td><td></td><td></td></tr>
<tr><td colspan="2">Inputs</td><td>Indicator</td><td>Sources of information</td></tr>
<tr><td colspan="2"></td><td></td><td></td></tr>
<tr><td>Outputs</td><td>Efficiency of programme</td><td>Indicator</td><td>Sources of information</td></tr>
<tr><td></td><td></td><td></td><td></td></tr>
<tr><td>Immediate results</td><td>Effectiveness (on performance)</td><td>Indicator</td><td>Sources of information</td></tr>
<tr><td></td><td></td><td></td><td></td></tr>
<tr><td>Wider objectives</td><td>Impact (spill over effects)</td><td>Indicator</td><td>Sources of information</td></tr>
<tr><td></td><td></td><td></td><td></td></tr>
<tr><td colspan="2">Relevance and design</td><td>Indicators</td><td>Sources of information</td></tr>
<tr><td colspan="2">To what extent did the programme fit into the needs and policies of the country?</td><td></td><td></td></tr>
<tr><td colspan="2">To what extent was the design appropriate?</td><td></td><td></td></tr>
<tr><td colspan="2">Was this an appropriate project for Phare?</td><td></td><td></td></tr>
<tr><td colspan="2">Sustainability</td><td>Indicators</td><td>Sources of information</td></tr>
<tr><td colspan="2"></td><td></td><td></td></tr>
</table>

Appendix B

Log Frame: Phare Financial Programmes for SMEs

Objectives	Evaluation Questions	Verifiable indicators	Sources of information
Description of the project			
Access to external sources of finance by SMEs, including • Grants • Micro loans • Small loans (generally on a longer term basis) • Guarantees for loans • Equity funds			
Inputs		**Indicator**	**Sources of information**
Phare cash contribution and terms of lending Co financing by Bank or Government Technical assistance to enhance credit management skills Possible involvement of Business Support Agencies in assisting clients to prepare business plans or provide a monitoring service to the bank		Standard input table summarising the conditions of the loan Inventory of alternative sources of finance	Bank records Country Reports
Outputs	**Efficiency of financial programme**	**Indicator**	**Sources of information**
Finance to SMEs	Level of subsidy Appraisal process: how well did the selection of enterprises conform to the project design?	Comparison of revenues and all costs	Input-output table + interview with the bank
Immediate results	**Effectiveness (on enterprise performance)**	**Indicator**	**Sources of information**
Improved economic performance of SMEs	Has the investment led to an improvement in the performance of firms receiving finance? Did the improved performance justify the use of subsidised credit?	Increases in investment, employment, outputs and profits.	Interviews with selected firms, inspection of loan files and feedback from credit officers

	Were the firms receiving funds the most appropriate?	Target market for fund The level of demand List of applications and selection process. Could the firms have received funds from other sources? Why did they seek funds from this source? What if they had not managed to obtain finance?	Bank data and interviews with enterprises
Wider objectives	**Impact (spill over effects)**	**Indicator**	**Sources of information**
Improved access to external finance by SMEs	Learning and demonstration effects within the firms receiving finance	How has their attitudes towards finance changed as a result of having to negotiate and repay a loan?	Questions to firms, their advisers and the credit officer
	Learning and demonstration effects leading to changes in lending policies of bank (and other banks)	More active lending/co funding by bank and government	Questions to bank on their lending policy
	Lower transaction costs in bank	More professional approach to credit management	Questions to bank on whether their credit management has improved, and reduced spreads now being sought
	Larger client base for the bank (through lowering risks and demonstrating creditworthiness etc)	Greater access of clients to market based finance	Questions to bank (how many Phare clients become clients of the bank)
	What effect did the programme have on the market (volume and price) for financial services to SMEs?	Did it increase competitiveness or distort the market?	Questions to the banks and managers of other financial programmes
	Has this project contributed to a greater understanding in Government, agencies, and small firms about the role of financial for SMEs?	Improved understanding of the critical issues	Interviews with Ministry, Foundation, and Banks
	Has this project led to the government, donors and banks introducing more effective financial programmes?	Introduction of better designed financial programmes	Review the design of most recent financial programmes

Relevance and design	Indicators	Sources of information
To what extent did the programme fit into the needs and policies of the country		
• how relevant is the project to the needs of the country?	Country analysis	Questions to banks, and Ministry
• to what extent was the project at variance with other government policies (particularly in relation to the provision of subsidised finance to a small number of enterprises)?	Country analysis	Ditto
• to what extent does the project address a real funding gap?	Country analysis	
• to what extent did the provision of finance 'crowd out' other sources, and to what extent was it additional?		Ditto
To what extent was the design appropriate?		
• choice of instrument,	Consultants assessment	Country report
• target group of enterprises	ditto	Country report
• risk profile of project	ditto	Questions to bank
• timing of delivery	ditto	Country report
• choice of institution and terms of the agreement	ditto	Input output table
• ownership rights of the Phare sourced funds	ditto	Questions to bank, Ministry and delegation
• pricing and other conditions to the end client: is the implied subsidy justified	ditto	Input output table
• potential role of co-financing from government or financial institution	ditto	Input output tables and questions to bank and Ministry
Was this an appropriate project for Phare?		
• what other options should have been considered to improve the flow of finance to SMEs?	Assessment by consultants	
• what were the opportunity costs of the project from Phare's point of view	ditto	
• to what extent has there been overlap and duplication with other donors	Country analysis	Country report

Sustainability	Indicators	Sources of information
Financial sustainability of programme	Positive internal rate of return, net of donor and government support If not, what rate is the fund being depleted, how long will it survive?	Bank data on the financial performance of the programme
Clear and satisfactory arrangements for the ownership and management of the programme to continue to fulfil its original aims and objectives following the ‘exit’ of Phare	Is it clear who owns and is responsible for the money donated by Phare to the programme? Is there a clear decision making structure for the management of the fund?	Interviews with bank and Ministry Review the legal agreement for the fund and changes that have been made
Soundness of the management of the fund without further technical assistance	Competence of the team managing the fund	Interviews with the Bank

Appendix C

Log Frame: Phare support for the provision of policy advice

Objectives	Evaluation criteria	Verifiable indicators	Sources of information
Project description			
Provision of TA to government and ministries responsible for SME development or where their operations likely to impact on SME development (positively and negatively)			
Inputs			
Cost of TA (salaries and expenses); equipment and premises restoration;			
Outputs	**Efficiency questions**	**Indicator**	**Sources of information**
Policy advice, promotion of SME concept in government, draft legislation, SME "events".	Total cost of advice against measures undertaken	Cost of programme	Delegation, government, ministries.

Immediate objectives	Effectiveness	Indicator	Sources of information
To point to areas where government can make major contribution to SME development; to improve the "SME-friendliness" of other business undertaken by government.	Government implements direct SME supporting measures, including new legislation; government changes its operations in other areas to reflect need to support (or not to frustrate) SMEs development	Quality and quantity of new government measures; quality and quantity of amendments to other government operations.	Government, ministries, delegation
Wider objectives	**Impact**	**Indicators**	**Sources of information**
To make the overall environment in which government operates more "SME-friendly" and increase the responsiveness of SMEs to this environment.	Government is more "SME-friendly" and SMEs respond to this new working environment.	Audit of government activities; SME sector's assessment of governments degree of "SME-friendliness"; degree to which SME sector responds to governments new measures and framework for operating ("take-up").	Government and ministries; survey of business attitudes to government; SME's knowledge of and response rate to government measures.
	Relevance	**Indicator**	**Sources of information**
	Was advice of a better quality than internal advisors; was it simply a substitute for an internal appointment; did the use of an ex-pat create more resistance to "SME-friendly" measures or less; was it ignored because of "free market" stance of government.	nature of advice offered (standard solution or something new); response of government departments to advice; working relationships of advisor with domestic SME advisors.	government; advisory measures; interviews with domestic advisors; assessment of government programmes.
	Sustainability	**Indicator**	**Sources of information**
	Will the measures survive a change in government? Is domestic support for nature of measures growing? Degree to which measures are perceived to be "imposed from outside"	measures have continued after change in government; extent to which domestic SME advisors have accepted the measures as "best practice".	Government; interviews with other domestic advisors.

Appendix D

Log Frame: Phare support for a National Agency

Objectives	Evaluation criteria	Verifiable indicators	Sources of information
Project description			
The establishment of a national level co-ordinating and promotional body for SME development, which is also meant to liase with, and support, the network of LEAs also established with Phare support.			
Inputs			
TA, Phare financial contribution for running costs, leveraged co-financing arrangement with government.			
Outputs	**Efficiency questions**	**Indicator**	**Sources of information**
Providing support to government, NGOs, and others engaged in SME development; provision of support for LEA network; co-ordinating international assistance.	Level of subsidy included in the programmes	Total cost of the support.	PMU, FMs.

Immediate objectives	**Effectiveness**	**Indicator**	**Sources of information**
To improve the operation of institutions involved in SME development, including network	Performance (visibility, strategic role, implementation) of individual institutions supported by The National Agency improved; performance of network as a whole improved	change in performance of those institutions receiving The National Agency support (before and after; with and without); performance of network (sustainability)	PMU, The National Agency, interview programme of institutions having received The National Agency support.
Wider objectives	**Impact**	**Indicator**	**Sources of information**
To improve the overall climate for SME development in the country.	Existing SME support infrastructure improves; economy considered more "SME friendly"; growth of private sector support.	Number of SME development programmes and institutions now on offer thanks to The National Agency; number of supportive government measures/laws/acts introduced thanks to The National Agency; quantity and quality of relations with network.	The National Agency, LEAs, ministries
	Relevance	**Indicator**	**Sources of information**
	Does the National Agency fill a recognised gap in the SME support infrastructure.	Level of national provision of business support services co-ordination; number and extent of activity contacts with other institutions, including LEAs	The National Agency; government departments; LEAs.
	Sustainability	**Indicator**	**Sources of information**
	Will the National Agency retain its original objectives; who is going to accept long term responsibility for it.	Changes in original objectives and target client group; plans for alternative funding.	The National Agency, government departments.

Appendix E

Log Frame: Phare support to Regional Advisory and Information Centres

Objectives	Evaluation criteria	Verifiable indicators	Sources of information
Project description			
Establishment of a network of Business Advisory/Support Centres, targeted at start-ups and assisting the unemployed into business, and also addressing regional development issues (e.g., major plant closures).			
Inputs			
Phare financial contribution, leveraged co-financing arrangement with government, TA to support business advisors deliberate involvement as channel for Phare loans and grants.			
Outputs	**Efficiency questions**	**Indicator**	**Sources of information**
Business advisory support, training support, marketing activities	Level of subsidy included in the programmes	Total cost of the support to the BAC, including per client	The BAC, particularly central agency (if exists).

Immediate objectives	**Effectiveness**	**Indicator**	**Sources of information**
To improve the management performance of SMEs, to increase the chances of access to finance for SMEs supported by BAC	Performance of SMEs supported by BAC improved, improved access to finance for those SMEs supported	performance of those SMEs receiving Phare support, access to finance of Phare supported SMEs	BAC, central Agency, interview programme of local entrepreneurs having received Phare support.
Wider objectives	**Impact**	**Indicator**	**Sources of information**
Improving the performance of the SME sector, establishing better access to finance via BACs, stimulating the development of private sector support programmes, raising awareness of the entrepreneurship option.	Overall performance of SME sector improves, SMEs gain greater access to finance, demonstration effects upon private sector business support services.	Aggregate effect of SMEs supported, greater amount of financial support to SMEs, changes in capacity of private sector business advisory services,	BAC, central Agency (if exists), survey of private sector business advisory capacity,
	Relevance	**Indicator**	**Sources of information**
	Does the BAC fill a gap in the service provision, does the BAC duplicate private sector services, are private sector services precluded from developing because of the Phare support to the BAC, is the BAC willing to support high risk - high social return SMEs	Level of private sector provision of business support services, price of BAC services compared to market price, the number of SMEs supported which would have been willing and able to access private sector support, BAC client portfolio.	BAC, central Agency (if exists), interview survey of BAC-supported entrepreneurs
	Sustainability	**Indicator**	**Sources of information**
	Will the BAC retain its original objectives, who is going to accept long term responsibility for the BAC,	Changes in original objectives and target client group, user fee income as a percentage of total income (current and planned), plans for alternative funding,	BAC, BAC client portfolio,

Appendix F
Summary of Interviews with Enterprises with Phare loans

Mr A, in 1994, planned to set up as a licensed trader to make wooden panels, door and window frames for local builders. He needed funds to purchase additional equipment and materials. He visited 4 banks; at 20% interest rate it was too high, but they all turned him down due to poor collateral. At the Savings Bank, they suggested the Small Loan Programme. He got the RAIC to prepare a business plan, and within 3-4 months obtained a loan of SK 260k (Euro 6.7 million) for three years, secured by his family house (120% of the loan). He now employs 7 people and claimed his turnover has increased from 6m in 1995 to 12m in 1997. In 1995, he was also able to obtain a grant of SK 300k (Euro 7,800) from the Labour Office for taking on the extra staff.
Savings Bank: The accounts suggest that performance figures were significantly lower. His target was a turnover of SK 1.5m (Euro 39,000) and a profit of SK 199k (Euro 5,000); in fact he had a turnover of SK 0.9m (Euro 23,000) and lost SK 64K (Euro 1,600). Similarly, in 1996, he expected a turnover of SK 2.1m (Euro 55,000), but achieved only SK 1.1m (Euro 29,000). Despite this reduced performance his loan repayments have been on time.
Assessment: without the loan it is doubtful whether he would have started in business. New jobs created: 7 .

Mr B, a licensed trader used the proceeds from the sale of a flat to set up as locksmith in 1993 to provide and fit locks for builders. After seeing an advertisement, he applied to the Savings Bank, prepared his own business plan and obtained a loan of 800k in July 1994 to buy premises and machinery, which were used as collateral with his family house (cover SK 8m: Euro 200,000). He didn't bother to apply for funds from other banks because they would not accept his home as a collateral. His business has expanded from a turnover of SK 1.25m (Euro 32,000) in 1996 to SK 1.5m (Euro 39,000) in 1997 and hopes to do SK 2m (Euro 52,000) in 1998. He now employs 3 people part time according to the workload. He has since opened a restaurant in rented premises and a tennis court.
Savings Bank The bank confirmed that in 1994 he had a turnover of SK 1.6m (Euro 40,000)and made a loss of SK 368k (Euro 9,500). The bank experienced payment problems in 1995. Through the National Agency, the RAIC was asked to trace Mr B. The bank started court proceedings in Jan 1996, obtained an execution in May and the order was released in 1997 for the repossession of his family apartment. This led to a negotiation. He is now repaying the loan.
Assessment: without the loan he would not have been able to buy his own premises, and probably would not have had the resources to set up the other businesses. The economic benefits of the loan appear to be marginal. Extra jobs about 2 (equivalent)

Company C, set up in 1992 as a producer of sweaters, 25% for local market, and 75% acting as a contract manufacture for EU customers. The business has grown from 20 people in 1992, and now employs 202, and had a turnover in 1997 of SK 140m (Euro 3.6 million). It has obtained six short and medium term loans at interest rates from 16-20% from the Savings Bank and Tatrabanka and a DM loan from Deutche Bank. He saw an advertisement for SLP, got the RAIC to do a Business Plan and obtained a SK 5m (Euro 130,000) loan for 3.5 years from Tatrabanka for machinery and premises., which were used as collateral.
Tatrabanka: no interview
Assessment: It seems fairly clear that the SLP substituted for commercial bank funds. The loan has enabled him to consolidate the business and continue to expand. The new equipment will have improved his efficiency and long term survival. But it appears to have displaced local funds? Jobs: Difficult to quantify

Mr D, a licensed trader, has been engaged in wholesale distribution of glass wear in Czech and Slovak republics since 1991. He needed funds for extra stocks and working capital, but banks were not happy to use his house as a collateral. The RAIC helped introduced him to the Post Bank, as a special case, and within 2 months, obtained SK 1.5m (Euro 39,000) repayable over four years at an interest rate of 15%, secured by his house and his premises. His business has grown from SK 1.5m (Euro 39,000) turnover in 1991 to 35m (Euro 900,000) in 1997, and now employs 10 people.
Post Bank: no interview
Assessment: Difficult to justify this case. It is a pure trading activity, the extra jobs will be limited and it is not clear that performance will be significant improved. Perhaps + 1-2 jobs

Mr E, a licensed trader, who was unemployed, wished to start a car repair business and needed equipment. In 1997, the Labour Office suggested the Small Loan Programme, the RAIC prepared the Business Plan, and after half a year, he obtained SK 250,000 (Euro 6,500) from the Savings Bank, secured by his family house. Employing none, turnover has increased from SK 200k (Euro 5,000) in 1995 to SK 350,000 (Euro 9,000) in 1997. After the Bank tried to change the terms of the loan, he decided to pay it off. He would have been prepared to pay a higher interest rate for the money: perhaps up to 14-15%.
Assessment: Without the loan he may not have started the business. But it is not very successful and employs nobody else, but the loan is quite small. 1 job created.

Company F is a motor dealer in Nitra which started in 1992 and expanded from 2 to 14 people. It wished to move from rented premises and buy premises in a better location to establish a repair shop. It has been a customer of the Savings Bank since 1992. It heard about the SLP from his dealer network. The RAIC helped to prepare a BP for a loan of SK 5m (Euro 130,000).
Savings Bank: Due to a lack of allocation, SB offered a Support Loan of SK 2.25m (Euro 58,000) at 13.5%, and a commercial bank loan of SK 2.75m (Euro 71,000) at 17.5%. The plan and actual performance is set out in the table:

Turnover	**1995**	**1996**	**1997**
Plan	10.7m	28.2	28.2
Actual	3.2m	43.3	72.3
Profit			
Plan	0.9m	1.9m	2.0m
Actual	-0.2m	0.2m	0.4m

The business was making a loss but the Bank felt it had a good perspective. It rated the risks: Economic situation 98%, quality of the business 20%, collateral risk 20%, and other loans 20%. The owner's capital represented 11%, the anticipated return on assets 27%, and collateral cover 166%. The bank indicated if there was no SLP at the time of the application, they would have lent this client the money from their own resources at 17.5%, if SLP.
Assessment: The business has done well. But SLP was clearly substituting for more expensive commercial funds at the time that the loan was made.

Company G: Review of the Savings Bank files: employing 3 people obtained SK 4m (Euro 100,000) at 13.5% for 1.5 years from the Savings Bank in May 1995 for machinery for a glass factory, which planned to take on 6 extra people. The business plan showed a ROA of 29.7% and profits : loan interest + repayment of 1.03. Projected and actual figures were as follows:

Turnover	**1994**	**1995**	**1996**	**1997**
Plan		20m	22m	23m
Actual	4.4m	12m		
Profit				
Plan		3.5m	4.9m	5.3
Actual	+0.8	-1.8m		

In Dec 1995, the business obtained a second short-term loan of SK 2m (Euro 52,000) at 17% for materials. There was no cash flow attached to the plans. Due to low cost imports from the Ukraine, the factory was closed and became a distributor. The Bank believed it would have offered the business the loan if the SLP was not in place, because the business could provide a good collateral: the premises worth 8.6m (200% of loan).
Assessment: It is clear that the business would have been able to obtain a commercial loan from the Bank. The plans and cash flow forecast were not well done or assessed. The company returned to the bank for money in Dec 1995, which the Bank agreed to provide. The performance of the business subsequently was poor.

Mrs H: review of the Savings Bank file. Ran a family restaurant in a small town facing severe economic problems. She wanted to extend the building and provide accommodation. She obtained SK 5m (Euro 130,000) in Feb 1997, secured by the building and some land (93%).

Turnover	**1995**	**1996**	**1997**
Plan			8.4m
Actual	10.6m	7.0m	1.4m
Profit			
Plan			1.9m
Actual	-2.0m	-0.4m	-1.1m

Despite the record, the bank was not unhappy with the risks: economic risk 60%, quality of business risk 30%, collateral risk 0% and other loans risk 0%, overall average risk: 36% rating as a 2 (top rating =1). Being a cash business profit is difficult to interpret. The reason for the drop in sales was due to the sale of a second hotel, and the closure of the restaurant to do building repairs.

Assessment: Finance for property for a service business. Will it create many/any more jobs. In 1997 they would not have been able to obtain a loan from the bank.

Mr J is a licensed trader set up a business with SK 80,000 (Euro 2,000) to produce advertising signs and name plates. Before starting he obtained a loan from the Saving Bank for SK 1.4m (Euro 36,000) for 2.7 years in 1996 to purchase metal working equipment, secured by the machinery and his family apartment (84% cover). The RAIC produced his business plan and has continued to provide advice.

Turnover	**1996**	**1997**	**1998**
Forecast	2.5m	2.9m	3.2m
Actual	0.8m	1.7m	
Profit			
Forecast	180k	110k	90k
Actual	71k	-40k	

Though he has not reached his turnover and profit targets, he is rated as a successful business. He employs no other people, though the business has the potential in the future

Assessment: a good example of a small credit being used to enable a new business service to be provided, with the potential for growth.

Appendix G
Summary of interviews with enterprises advised by the RAIC in Nitra

Mr P is a licensed trader who set up an advertising and design studio in late 1995. When he tried to get a credit, the bank referred him to the Regional Centre to get help in preparing a business plan. Though he said the plan was well done, he ended up using leased finance to purchase his computer equipment. He would not have been able to pay for the service at that time; when he was referred by the bank. He had never heard of the Regional Centre and did not know of a consultant who would be able to help him.
Assessment: the Centre did a sound job on the Business Plan, but perhaps it could have suggested using lease finance? The case confirms a concern expressed by the Regional Centre that it is not better known.

Mr Q, a licensed trader established a bakery in 1995 and now employs 6 people. He had raised a commercial loan from the Savings Bank to purchase equipment. He hit serious problems because the equipment did not meet the specification that he required, and at the same time, the bank were requiring their loan to be paid off. At the suggestion of the Bank he went to the Regional Centre for advice. The Adviser together with a private lawyer helped him to re-negotiate the contract and secure a second loan from the bank, partly to pay off the first. Without the RAIC's support, he feels he would not be in business now. He strongly advises that all firms taking out a loan with the bank should seek the RAIC's advice. He feels that he would benefit from on-going advice on economic and tax affairs, legal issues and analysis of the market.
Assessment: the client made good use of the Centre, which helped him to resolve his legal and financial problems.

Company R was formed in 1992 to manufacture lights and electronic controls for lighting systems, with over 60% exported, mainly to EU countries. It employs 65 people, of whom 58% are handicapped and 85% are women - a part of its philosophy. Turnover has increased from SK 1.6m (Euro 41,000) in 1993 to SK 90m (Euro 2.3 million) in 1997, and investments were SK 4m (Euro 100,000) in 1996, SK 15m (Euro 400,000) in 1997 and SK 25m (Euro 650.000) in 1998. Initially the owner financed the business himself and did not manage to get his first bank loan (SK 15m: Euro 400,000) in 1997, because he could not meet the collateral needs of the bank. At the suggestion of a friend he met the RAIC, who encouraged him to attend a Europartinariat to help build contacts in western markets. It was very successful and he participated in 4 events. He also goes to the RAIC from time to time if he needs information on legislation. He feels that the RAIC provides good advice for start-ups and small companies doing business in the region, but it is less suitable for larger companies, who need access to more specialised information
Evaluation: the RAIC did a good job in encouraging him to participate in a Europartinariat.

Mr S is a licensed person engaged in the production of coffins since 1990 and now employs 18 people. He did not know what his turnover was, but is making a profit. Starting small, he has since bought premises and machinery. He got to know of the Agency though a friend, and recommends his friends who need a business plan to visit it. He himself has not had any major problems so has not needed to use their services, except to obtain information from time to time.
Assessment: a skilled tradesman who has steadily built up the business, but has not had any major problems which have led him to seek the advice of the Centre.

Company T was formed in 1991 and employs 115 people in the manufacture of road trailers, 93% of which are exported. He first used the Centre's services in 1995, attending a Europartinariat which he found useful to build up contacts. He is also a member of the Subcontract Exchange of Slovakia which has tried to find clients for him in France. Subsequently he has sought the Centre's advice on a customs problem. He is focused on overseas markets as foreign clients are more reliable. He sought credit to purchase a factory, but did not use the Centre on that occasion.
Assessment: a rapidly growing company that the RAIC has been able to offer The National Agency programmes to help develop SMEs to develop foreign contacts.

Business U is partnership formed in 1993, involving a husband and wife who run a computer training business, which also develops software applications. Turnover has increased from SK 50,000 (Euro 1,300) in 1993 to SK 250,000 (Euro 6,500) in 1997. When they started they had no knowledge about business and the procedures to get started, they read about the RAIC in the newspaper and went to seek their help. They got a lot of useful information and advice on the best legal form. Subsequently, they got the RAIC to help them prepare a business plan to raise money from the Bank. Though they went to two banks they were not successful, but managed to get a small amount of money from the labour office. If the RAIC did not exist, they could not afford to use a private consultant, but would probably seek help from the District Labour Office or the Director of the School.
Assessment: a typical start up case which made good use of the RAIC's services.

Appendix H

People consulted during the Evaluation

Institution	Name	Function
EU DG1A	Mark Priestley	Task Manager
EU Delegation, Slovakia	Sven Kuhn Von Burgsdorff Dusan Dobrovsky	First Secretary Phare Co-ordinator
OMAS Consortium	Raffaele Boldracchi	Team Leader
Ministry of Economy	Stefan Turan	Director Enterprise Policy and Regional Policy Department
Ministry of Interior	Gejza Petrik	Director of Local Government Dept.
National Bank of Slovakia	Victoria Muchova	Department of Statistics
Office for the Strategy of the Development of the Society, Science, and Technology of the Slovak Republic	Marta Simkova Peter Reiner Jarmila Karova	Director, International Co-operation Adviser Project manager Member of the team
National Agency for the Development of SMEs	Juraj Majtan Nina Heckova Zuzana Cigankova Darina Kaluznikova Katarina Kellenbergerova Ctibor Bohac Karol Stranai Marian Jasic Igor Kovacik Jan Gregor Vladimir Janco Stefan Szabo	General Director Director(s) Dept. Economy and Administration and PMU Director of Financial Support Programme Director of Regions and Training Specialist, Dept of Regions & Training Director of Dept of Co-ordination Programme Manager Manager Subcontracting Exchange Expert: subcontracting exchange Manager Spin Out Project Euro Information Unit
Technology and trade Information Promotion System (TIPS)	Petra Autova	National Co-ordinator
Seed Capital Co	Marta Midarikova	Specialist
Phare Slovakia Export Development Programme	Jan Jezo Nahor Meenam	Director of Export Information Centre PMU Director Team leader
Savings Bank	Peter Turek Anna Madericova Peter Vojtassak Eva Dankova	Deputy General Manager Head of credit department Deputy head of credit dep. Phare project co-ordinator
Slovak Chamber of Commerce, Bratislava	Martin Hrivik Jan Vlcko	General Secretary Secretary to the President
Entrepreneur Association of Slovakia	Miroslav Knitl	President
Post Privatisation Fund: Manager: Framlington/ CET	Andre Wavre	Managing Director
Pol'nobanka	Miroslav Strokendl Boris Kupkovic Lenka Lucanska	Director, Loan Department Head of Commercial Loans Credit Officer
Slovak Guarantee Bank	Gabriela Sedlakova Gabriela Miklosova David Luptak	General Director Director of Department of Bank Strategy and Concepts Manager
BIC Bratislava	Roman Linczenyi	General Director
RAIC Nitra	Dusan Sliznik	Manager
Savings Bank, Nitra	Maria Bachanova Martin Volke + Credit Staff	Branch manager Bank Officer
Nitra City Administration	Jozef Lanak	Head of regional development
Regional Development Agency, Nitra Regional Administration	Emil Lorinc	Head of Regional Development Programme

Regional Chamber of Commerce, Nitra	Miroslav Masarik Juraj Csano	Director Head of foreign relations
Commercial Enterprises in Nitra	13 Enterprises	Owner manager/General Director
EU Consultants	David Irwin Simon Armstrong Jacques Pronk	Project North East (Evaluation of Seed Capital Fund) Consultant (Policy development) EBN (Evaluation of the BICs)

Appendix J

Papers and Reports Reviewed

1 Reports and papers from NADSME

DG1A Financing Memoranda and Country Reports:
FM: SR 9302
FM: SR 9404
FM/COP 1995
FM/COP 1996 + preliminary inputs by NADSME
FM/COP 1997 + preliminary inputs by NADSME + Sectoral Operation Programme: SME Development
COP 1998 preliminary inputs by NADSME

NADSME Work programmes:
SR 9302 Work programmes 1-8
SR 9404/01 Work programmes 1-8
SR 9509 Work programmes 2-6
SR 9702 Work programmes 1-2

NADSME Annual Reports: 1994-97

State of SMEs in Slovak Republic, NADSME, 1994, 1995, 1996, 1997

B Fernandez, J. Gregor and I Kovacik, Report on the Subcontract Exchange of Slovakia 1994-96, July 1996

Subcontract Exchange of Slovakia, Catalogues of Slovakia of Partner SMEs

Euro Info Correspondence Centre, Reports on activities, 1994-1998

NADSME Spin Off Programme

Henry Siegel Statistical Analysis of Information Submitted from RPICs and BICs in Slovakia, NADSME, Nov 1996

Simon Armstrong Proposal for a State Medium-term policy for the support of SMEs, NADSME 1998

2 Papers from the Ministry of Economy and other Ministries

State Medium Period SME Support policy Ministry of Economy, Dec 1996

Act No 100/1995 National Council State Support of SMEs May 1995

Ministry of Economy: Enterprise plc Lobbying and representation, Final report, Nov 1997

Ministry of Economy: Enterprise plc Credit and Financing Mechanisms, Final Report, Nov 1997

Ministry of Economy: Extracts from the National Programme of Slovakia to meet the Acquis Communitaire, Section 16: SMEs, Section 21: Regional Policy and Co-ordination of Structural Funds

Office for the Strategy of the Development of the Society, Science and Technology, The Current State of Implementation of the Slovak Regional Policy, Nov 1997

3 Papers from Representative Organisations

Slovak Chamber of Commerce Annual Report 1997

P Kopal Doing Business in Slovak Republic, Slovak Chamber of Commerce, 1996

Entrepreneurs Association of Slovakia, Background Paper, 1998

Entrepreneurs Association of Slovakia, Survey of all activities in 1995 and 1996, Final report 1997

4 Papers on Finance and banking

Study on Seed Capital Fund, Bratislava, prepared by BIC Brabant for EC Phare Sept 1993

Bank Windows Project: 4th Quarter and Final Report September 1997

Private Equity and Venture Capital in Slovakia, Country Policy Paper, EVCA and Slovak Venture Capital Association, 1996

David Douglas, Mutual Support Credit Institution - Slovakia, Final report, WMEB June 1998

D. Zemanovicova, R.Tkacik, J. Merica, Bankruptcy Regulation in the Slovak republic, CPHR, Dec 1995

Adela Hoskova: Foreign Capital in the Economy of Slovakia, National Bank of Slovakia 1996

National Bank of Slovakia: Annual Reports 1993-97

Savings Bank Annual Report 1996 and 1997

Poľnobanka Annual Report 1996

Anton Marcincin: Restructuring Banks in the Slovak Republic, CPHR, December 1997

5 Reports from International Financial Institutions

OECD Economic Survey Slovak Republic 1996

OECD Workshop on Financing Newly Emerging Private Enterprises in Transition Economies, Country Note by the Slovak Economy, Jan 1998

UNIDO-SME Policy research Slovak Republic, NADSME with additional notes by Jane Rindl, Durham University Business School 1996

World Bank: Slovakia Country Economic Memorandum:
Draft Working Paper No 4 Financial Sector 1997
Draft Working Paper No 3 Enterprise reform in the context of EU Accession

6 Reports from Nitra

RPIC Nitra Business Plan for 1998

RPIC Nitra Strategic Plan for 1997 - 1999