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It is better to Remain Small and Invisible. Informal Barriers to the Development of Small and Medium Enterprises in Belarus[1]

Part I[2]

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Abstract

This paper is focused on informal relations between state authorities and business, which exist in a peculiar Belarusian economic system, where the competition remains restricted, and the public sector based on large companies continues to play a crucial role. The author argues that the Belarusian public authorities have developed a broad set of informal rules which allow them to extract resources from small and medium private enterprises (SMEs) and control the expansion of the private sector. He also argues that as long as informal extractive institutions designed and maintained by the state remain in place, the improvement of formal business regulations alone will not produce the expansion of the SME sector. In author's opinion, an extra-legal extraction of funds and informal discrimination against small and medium private enterprises are embedded in the logic of the centrally planned economy, which Belarus has preserved after the fall of the Soviet Union. This dissertation may also help to understand how SMEs operate in many other economies of the post-Soviet area and what obstacles to the development they face.

Keywords: institutional sociology, informal institutions, small and medium enterprises, Belarusian economic system, economic transition, regulatory reform.

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[2] The second part of this paper will be published in the next issue of the Warsaw Forum of Economic Sociology

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Introduction

In modern market economies small and medium enterprises (SMEs) are perceived as the backbone of the economy and drivers of economic growth. In the European Union countries, they generate almost 60% of the GDP and employ over 66% of the labor force (European Commission 2014). Small and medium enterprise easy adapt to the changes in macroeconomic situation. They work in highly competitive environment with limited amount of resources. It makes them more innovative, efficient and more responsive to the changing demand (Bąkiewicz 2012; Matejun 2007). Therefore the governments of many countries believe that the development of small and medium enterprises will make their economies more flexible, innovative and resistant to crises (Thurik 2008).

The role of the small and medium business becomes even more important in times of market reforms and structural changes. SMEs absorb labor force released from inefficient big enterprises. They make the economy more diversified, fill in the gaps in demand, and contribute to the de-monopolization of the economy. Finally, small and medium enterprises create a large class of small owners and provide a stable ground for market economy (Lewandowski 2002). The European institutions and the governments of the EU member states declare the support of small and medium enterprises being one of their priorities in economic policy.

The governments of many post-Soviet countries also declare the support of the SMEs as one of their main economic priorities (Commonwealth of Independent States 2014). One of these countries is Belarus. However, the institutional environment the Belarusian SMEs operate in significantly differs from the Western market economies. Belarus remains one of the less transformed economies in the post-Communist area. About 70% of Belarusian GDP is produced by the state-owned sector (EBRD 2015).

Small and medium enterprises are far from being a backbone of the national economy. Their share does not exceed 26% (Belstat 2015a: 13). The number of SMEs and their contribution to the GDP is steadily growing since mid-2000s. However, the development of Belarusian SMEs is constraint by numerous obstacles, resulting from the peculiar nature of the economic system. This research can help in understanding of how small private enterprises are functioning in 'hybrid' economies of several post-Soviet countries.

Researchers usually focus on the barriers of legal or macroeconomic nature preventing Belarusian SMEs from growing. The main subject of present research, however, is the barriers of other type – namely informal ones. I argue that extra-legal practices imposed on Belarusian small and medium enterprises by the state authorities demotivate entrepreneurs from developing their business. The negative impact of extortionist practices widely used by state officials is not less considerable then the impact of the state regulations or unstable macroeconomic environment.

Information about the phenomenon of informal barriers was drawn from 32 semi-structured interviews with Belarusian entrepreneurs operating in more than 10 fields of economic activity (transportation, manufacturing, restaurant business, IT, wholesale and retail trade, advertising, design, construction etc.) and 9 interviews with experts in the economic field (business analysts, economists, journalists and lawyers). The interview study was based on a statistically non-representative stratified sample. A sampling frame was based on such variables as a field of economic activity, place of residence, number of years in business and firm's size. Among 32 business owners and experts interviewed from December 2013 to September 2016, 5 respondents are representing medium firms, 9 – small firms while 18 are representing microenterprises. They operate in urban and rural areas in 5 regions of the country (Capital city of Minsk as well as Viciebsk, Brest, Hrodna and Homiel regions)

This paper consists of 3 chapters. In the Chapter 1 I will describe the development of small and medium business in Belarus in the years 1991–2015. On the basis of available statistical data I will compare the structure of the Belarusian SME with the structure of SMEs in the neighboring EU countries. It will help to identify the anomalies which emerged as a result of the Belarusian government's policy towards small enterprises.

In the second chapter I will describe main informal practices of the state authorities which hamper the development of small and medium enterprises in Belarus. I will try to explain why Belarusian local officials extract resources from local business and what role this informal extraction plays in Belarusian economic system.

Third chapter of the paper will be dedicated to the adaptation practices. I will show how Belarusian entrepreneurs accommodate the unfriendly business environment. Finally, in the conclusion I will sum-up main findings of the research and try to explain how the informal institutions designed and maintained by the state will affect the development of SMEs in the near future.

1. Small and Medium Enterprises in Belarus: History, Figures, Problems

1.1. Development of Small and Medium Enterprises in Belarus, 1991–2015

At the beginning of 1990-s Belarus, as other post-communist countries, experienced a rapid expansion of small and medium enterprises. The legal base regulating the relations between the state and business was largely missing. State laws and regulations were either rapidly changing or were extremely outdated. Nevertheless, the number of firms as well as the number of employed in emerging SME sector was constantly growing (Yelovskikh 2005: 10). As the Figure 2 shows, just in three years, from 1992 to 1995 the number of SMEs tripled: it jumped from 69.9 thousand to 208.2 thousand.

The policy towards SMEs and the whole private sector radically changed after the election of Alexander Lukashenka as a president (1994) and subsequent consolidation of his power in 1996. The government started to restore the command economy system. It started to isolate private firms from the state-owned sector and subordinate the interests of private business to the interests of the centralized economic system. The entry barriers to the market were raised, the number of legal acts regulating economic activity was dramatically increased and the cooperation between the state enterprises and private SMEs was almost banned (Daneyko, 2001).

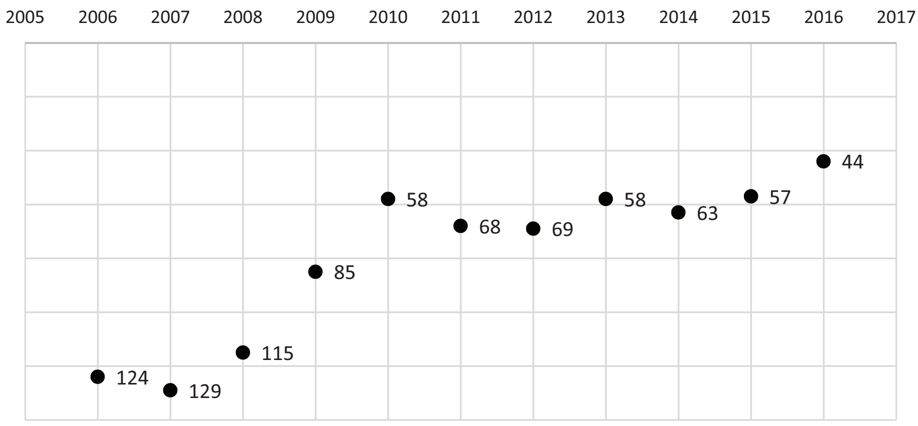
The Belarusian authorities intentionally restricted the growth of the SME sector. The most important instruments designed to limit the SMEs expansion were a complicated registration procedures and a big number of licenses. In 1996–1999 several campaigns of 're-registration' of the private enterprises took place. As a result, the number of private firms dropped by 30% (Daneyko, Pelipas, Rakova 2003: 19; Rumyantseva 2002: 105).

Before 2008 legal barriers were considered to be the major obstacles to the SME development in Belarus (Daneyko, Pelipas, Rakova 2003; Yelovskikh 2005). A priority given by the Belarusian authorities to big state-owned enterprises and discrimination of private firms were well reflected in the state regulations. Long, complicated and costly procedures of business registration, high number of licenses and permissions, heavy tax burden, price regulation, excessive attention of the inspection bodies hampered the development of private firms (Pelipas, Rakova,Chubrik 2007: 32).

Energy shocks (increase in prices of oil and gas delivered by Russia) which Belarus experienced at the beginning of 2007, made the government revise its policy towards SMEs. State officials understood that an economic model based on big enterprises benefiting from Russian energy subsidies and exporting mainly to the Russian market had exhausted its potential (Pelipas, Rakova, Chubrik 2007: 8). They were desperately looking for new resources able to ensure the stability of economic system and political regime. Foreign loans, a money emission as well as an expansion of private sector were seen as sources able to provide the government with necessary funds.

In 2008–2011 Belarusian authorities carried out significant regulatory reforms. They simplified the registration of new firms, tax collection procedures, abolished the majority of licenses, loosened the price regulation and significantly reduced the number of inspections (Pelipas, Rakova 2010; Pelipas et al. 2013: 39). Belarus significantly improved its position in thein the Doing Business ranking – World Bank's research project measuring the regulatory burden for SMEs. Belarus jumped from 129th place in 2007 to 58th in 2010.

Figure 1. Position of Belarus in the Doing Business ranking



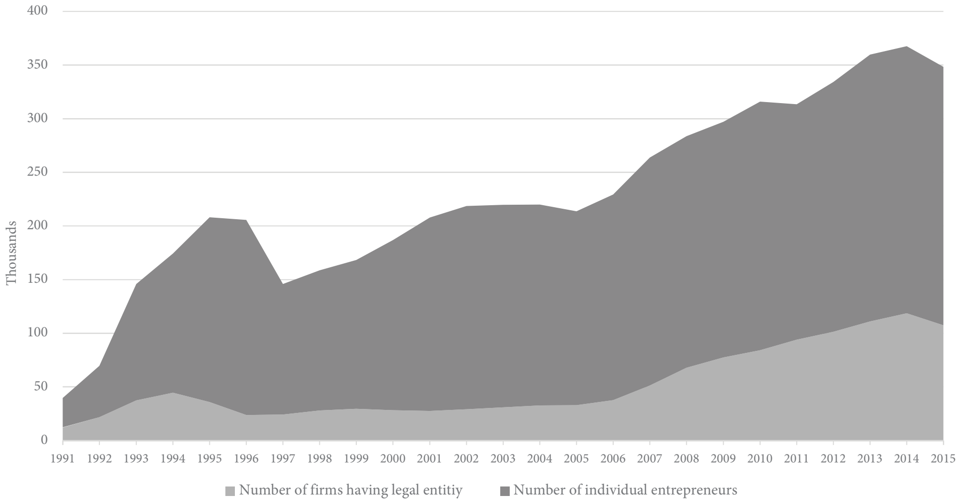
Source: World Bank 2016.

By the end of 2010 the President of Belarus adopted the Directive No. 4 'On development of entrepreneurship and stimulation of the business activity'. State authorities took the commitment to strengthen property rights, abolish price control, remove the barriers to the competition, reduce the tax burden and reduce the number of administrative procedures. Belarusian government also promised to significantly reduce the frequency of inspections (President of the Republic of Belarus 2010).

In December 2012 an ambitious Program of the state support of the small and medium entrepreneurship for the years 2013–2015 was adopted. The government declared to 'put Belarus on the leading positions in the international rankings concerning the competitiveness, business environment, innovativeness and effectiveness of state regulations' (Ministry of the Economy of the Republic of Belarus 2013). State authorities planned to increase the SMEs share in the GDP up to 30% and the number of SME employees up to 1.8 million (Pelipas et al. 2013: 64).

However, a significant business liberalization started in 2008, did not result in the expansion of the SME sector. In 2008-2014 the number of the small and medium firms increased by 29%, but the share of SMEs in the GDP during this period increased by less than 5% (up to 25.3% of the GDP). The number of employed in SME sector remained the same (Belstat, 2015a: 14–15). Macroeconomic instability of the years 2011–2015 is not enough to explain such stagnation. Several Belarusian experts argue that neither domestic not foreign entrepreneurs did not consider the regulatory reforms in Belarus as credible and substantially improving the rules of the game (Pelipas et al. 2013: 43).

Figure 2. Dynamics of the SME sector in Belarus in 1991–2015



Source: Kovalyov and Rakova 2004; Belstat 2016.

1.2. What is Small Business? Definition of the Small and Medium Enterprises in Belarus and the European Union

Before analyzing statistical data it is important to describe the differences between SME statistics in Belarus and the EU. The data provided by the Eurostat and Belarusian National Statistical Office (Belstat) are not fully comparable. The European Commission defines an SME as a business which employs less than 250 staff, has annual turnover less than 50 million euro or/and annual balance sheet total less than 43 million. The European Commission's definition divides SMEs into 3 categories which are described as follows:

Table 1. Quantitative criteria of belonging to SME sector used by the Eurostat

Company	Employees	Turnover	or	Balance sheet total
Micro	<10	≤ 2 million euro		≤2 million euro
Small	<50	≤10 million euro		≤10 million euro
Medium	<250	≤ 50 million euro		≤ 43 million euro

Source: European Commission 2014.

Any entity meeting these criteria is classified to the group of small and medium enterprises, irrespectively of its legal form. In the European Union even individual entrepreneurs who are not a legal person are counted as enterprises (European Commission 2015a: 9). Another important criterion of belonging to SMEs is the firm's independence. It means that the category of small and medium enterprises does not include subsidiaries of large companies or enterprises which are controlled by public bodies (European Commission 2015a: 7).

It is important to note, that the EU law clearly excludes state enterprises from the category of SMEs. The European Commission definition do not qualify to SMEs any enterprise where 25% or more of the capital or voting rights are owned or controlled by public bodies. This decision of the EU legislators is based on the assumption that 'public ownership may give certain advantages to enterprises, notably financial, over other enterprises that are financed by private capital' (European Commission 2015a: 19).

The Belstat's definition of small and medium enterprise is based on the Law on supporting small and medium enterprises from July 2010. The law defines 4 categories of actors as SMEs. The first one is individual entrepreneurs registered in Belarus. They perform economic activity as physical persons and do not have legal entity. In January 2008 individual entrepreneurs were forbidden to hire employees except from their family members (National Civic Association Perspektiva 2013). In May 2014 the right to employ was given back, however the number of employees was limited to 3 persons (President of the Republic of Belarus 2014). According to the Belarusian law, individual entrepreneurs are not considered being 'organizations'.

The second category is 'micro-organizations'. It includes commercial organizations having legal entity and employing less than 15 people. The third category of firms is called 'small organizations'. It includes entities employing from 15 to 100 people. Finally, the fourth category called 'medium enterprises' encompasses all firms employing from 101 up to 250 people (National Assembly of the Republic of Belarus 2010).

As one can see, the Belarusian definition of SMEs tells only about a firm's size. It does not impose limits on the firms' turnover and does not require firm's independence. Therefore the Belarusian National Statistical Office includes into the category of SMEs firms which depend on larger entities, e.g. subsidiaries of large companies or members of holdings. Belarusian journalist Dmitry Zayats (2013) points out that 80% of Belarusian SMEs' exports are the exports of fuel, petrochemical and chemical products as well as the exports of potassium fertilizers. It means that Belarusian statistics include to the SME sector oil and potassium traders. Such firms employ few personnel but have a very high turnover and income. They are usually subsidiaries of large state-owned companies, such as Belarusian Potash Company JSC or state petrochemical concern Belarusneft (Zayats 2013).

Another particularity of Belarusian statistics is the inclusion of state-owned enterprises into the category of SMEs. It makes the comparison between SME sectors in Belarus and the EU even more difficult. As several Belarusian economists (Yelovskikh 2005: 5; Shekhova 2001: 8) emphasize, the state-owned enterprises are hard to be called commercial firms, because they do not face entrepreneurial risk. The maximization of profit is not the main goal of many Belarusian state-owned enterprises. They are heavily subsidized and put into privileged conditions as compared to the private firms. In many cases the public sector is their sole and permanent customer. Therefore the official SMEs statistics are far from showing us a real contribution of the small private firms to the national economy.

A stratified random sampling made in 2013 for the survey carried out by the International Finance Corporation (IFC 2013) showed that 20% of Belarusian SMEs having legal entity were state-owned (the public authorities controlled over 50% of the assets of these enterprises). The share of the SOEs was particularly high among the middle-size firms – 57%. 30% of small enterprises and 19% of microenterprises also belonged to the state (Shcherbina 2014: 23). However, if one calculates the share of state-owned enterprises among all SMEs (which comprise not only legal entities but also individual entrepreneurs) this share will fall down to 6.4% (author's own calculations based on Belstat 2015a: 433).

It is important to note that in this study the EU's definition of SMEs is applied. Under small and medium enterprises I understand private firms having from 1 to 250 of staff, irrespectively of their legal form, which are not being subsidiaries of larger companies and fit into the limits of turnover and balance sheet total defined by the European Commission. The Belstat's definition of small and medium enterprises is very similar to the definition applied in Russian Federation. Another Belarusian neighbor Ukraine since 2012 uses the definition of small and medium business provided by the European Commission.

1.3. Small and Medium Enterprises in the European Union and Belarus: Differences and Similarities

According to the Belstat data, in Belarus in 2014 there were 363,160 small and medium enterprises (Belstat 2015a: 14, 68 and 433). They provided jobs to 1.5 million persons, i.e. to the one third of all employed in the economy. 114,208 enterprises or 31.4% of all SMEs were registered as legal entities, whereas 248,952 (68.6%) where individual entrepreneurs. The contribution of the SMEs to the Belarusian GDP was estimated at the level of 25.3% (Belstat 2015a: 13).

As one can see from the Table 2, the share of SMEs (both private and state-owned ones) in Belarusian economy is very similar to the share of the small and medium enterprises in neighboring post-Soviet non-EU countries. Belarus, Ukraine and Russia have also almost identical density of SMEs. An average size of Belarusian SME is slightly higher than in Russia and very similar to the Ukrainian one. Ukraine overcomes Belarus in terms of SMEs' share in the employment, but falls behind in terms of SMEs' contribution to the GDP. The experts argue that a real contribution of Ukrainian small firms to the national economy is much higher. Strikingly low share of SMEs in the Ukrainian GDP may result from a very large shadow economy, i.e. unreported economic activity of enterprises and mass informal employment (Chornij 2014: 3).

Table 2. Main characteristics of the SME sector in Belarus, Russia and Ukraine in 2013

Country	Number of SMEs per 1000 inhabitants	Share of SMEs in GDP (%)	Share of SMEs in employment (%)	Average size of an SME, persons
Russia	39.0	21	24.8	3.2
Ukraine	37.8	15	38.0	4.3
Belarus	38.0	26.1	32.9	4.2

Sources: Belstat 2015a; Commonwealth of Independent States 2014; Global Affairs Canada 2015; Chornij 2014; State Statistical Office of Ukraine 2014.

However, in order to identify the barriers and disproportions in the development of the Belarusian SME sector, it is much more important to compare its characteristics with the SME sector in the neighboring EU countries. Unfortunately, the differences between the EU and Belstat methodology do not allow direct comparisons. In order to make them possible the author had to make several adjustments of the data provided by statistical offices.

The European Commission tries to exclude from its studies of SMEs all financial institutions and institutions which functioning may not be based on market principles. Therefore the EU's analysis of small and medium enterprises, such as the SME Performance Review, focus only on the firms operating in a so called 'non-financial business economy'. By this term the EU statisticians understand all sectors of economy except for agriculture, fishing, forestry, government services, and such largely non-market services as education, health and cultural activities (European Commission 2015b: 3). Such methodology allows to make comparisons across the EU countries very easily. However, it makes difficult to compare the EU Member States with the countries which do not belong to the European Union.

In order to compare the performance of Belarusian SME sector with the SME sector in the neighboring EU countries, I excluded fromthe Belstat statistics all the economic entities operating in agriculture, forestry, fishery, financial sector, education, healthcare, public administration as well as 'communal, social and personal services' (e.g. culture and entertainment). The tables below present the figures for the year 2013. This is the latest year for which both the Eurostat and the Belstat provide the most complete data.

Table 3. Main characteristics of the SMEs in non-financial business economies of Belarus and neighboring EU countries in 2013

Country	Number of SMEs per 1000 inhabitants	Share of the SMEs in the value added (%)	Share of SMEs in employment (%)	Average size of an SME, persons	Number of large enterprises per 1000 inhabitants
Estonia	47.2	75.2	78.1	5.0	0.12
Latvia	48.1	68.4	78.3	4.8	0.10
Lithuania	48.5	68.3	76.3	4.6	0.10
Poland	38.7	50	67.8	3.8	0.08
EU 28	44.0	57.8	66.9	4.0	0.09
Belarus	**35.2**	**26.1**	**43.8**	3.9	1.12

Source: Own calculations based on European Commission 2015c; Belstat 2015a; Belstat, 2015c. For Belarus the data about the share of SMEs in GDP are provided.

The Table 3 compares the contribution of the SMEs to the non-financial business economy in Belarus and neighboring EU countries. As one can see, in Belarus the density of small and medium enterprises (both state-owned and private ones) is 20% below the EU average. It is 27% lower than in Estonia, Latvia and Lithuania. The employment in the SME sector in Belarus is 35% lower than the EU average and 44% lower than in the Baltic States. One should remember that the statistics concerning Belarusian SMEs operating in the non-financial business economy include the enterprises affiliated with larger entities, e.g. factories being members of holdings or subsidiaries of large companies. Being eliminated from the calculations, they will decrease both the density of SMEs and the employment in SMEs operating in non-financial business sector.

Unfortunately, the Belstat publications do not provide such important data as the value added produced in different sectors of economy, and the contribution of the SMEs to these sectors. Therefore the table above presents the contribution of the SMEs to the GDP of Belarus and not the contribution of SMEs to the value added in the non-financial business economy. These data have only illustrative character. Nevertheless, Belarusian experts admit that the contribution of the SMEs to the GDP in Belarus is about 2.5 times lower than the EU average (Pelipas et al. 2013: 21).

The difference in the average size of a SME operating in non-financial business economy in Belarus and its Western neighbors is not so striking. An SME in Belarus equals an average small firm in Poland or EU average, and is only about 15%-20%

smaller than in Lithuania or Estonia. However, the SME sector in Belarus is much more polarized. The share of individual entrepreneurs (entrepreneurs having no employees) in the Belarusian non-financial business sector is 71%, whereas in Estonia it is 45%, in Latvia 48%, in Lithuania 53%, in Poland 67% and the share of enterprises with no employees in the European Union as a whole is 57% (Belstat 2015a; Eurostat 2016). These figures suggest that in Belarus there are not enough enterprises of intermediate size between atomized individual entrepreneurs and quite developed and large firms having up to 250 employees.

The last column of the table does not directly concern the SME sector; nevertheless, it deserves readers' attention. As one can see, the concentration of big enterprises in the non-financial business economy of Belarus is more than 10 times higher than in the economies of neighboring EU countries. Such figures prove the opinion that Belarus still much more relies on big state-owned enterprises than the countries with developed market economies.

An analysis of the distribution of SMEs across different sectors of activities allows to clarify further differences in the development of SME sector in Belarus and the EU countries. Again, in order to make such a comparison, one should make some adjustments of statistical data. The classification of economic activities used by the National Statistical Office of Belarus is similar to the classification used by the European institutions, however it is less detailed. Enterprises and public administration institutions in the Belstat classification are divided into 17 groups while the Eurostat classification contains 21 divisions (Belstat 2012). In order to compare the distribution of Belarusian and EU's SMEs across the areas of economic activity, several groups of enterprises from the Eurostat classification were merged. The proximity of the two classifications allows to make such merger with little harm to the accuracy of estimations.

Namely, the division 'Electricity, gas and water supply' from the Belarusian State classification of economic activity corresponds to two divisions from the Eurostat classification: 'Electricity, gas, steam and air condition supply' and 'Water supply; sewerage, waste management and remediation activities'. The Belstat's division 'Transportation and communication' also corresponds to two Eurostat divisions: 'Transportation and storage' and 'Information and communication'. Finally, the Belstat division 'Real estate activities and consumer services' in the following tables corresponds to three divisions of the Eurostat classification: 'Real estate activities', 'Professional, scientific and technical activities' and 'Administrative and support services'. Starting from 2016 the National Statistical Office of Belarus uses the international classification of economic activities identical with the Eurostat classification. It will make comparisons much more detailed and precise; however, statistics gathered according to the new methodology are not expected to be published until 2017 (Belstat 2012).

Unfortunately, the lack of data about the value added produced by the Belarusian SMEs in different areas of activity complicates the comparisons between the SME sectors in Belarus and the EU. Therefore the performance of Belarusian small business will be analyzed on the basis of the distribution of small firms across the sectors of economy and the structure of employment in the SME sector.

Table 4. The distribution of SMEs operating in the non-financial business economy in Belarus and the EU in 2013 across the sectors of activities

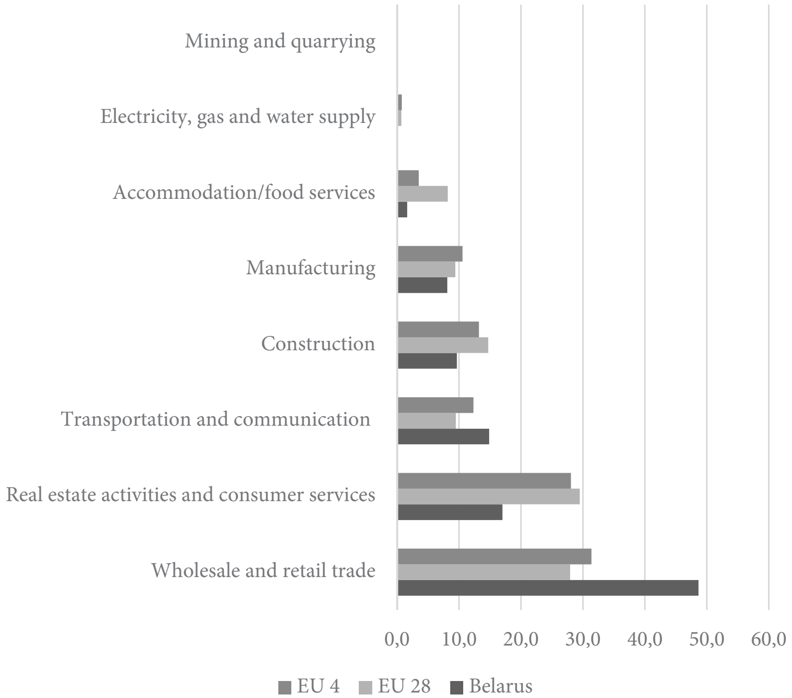
Country	Mining and quarrying	Manufacturing	Electricity, gas and water supply	Construction	Wholesale and retail trade	Accommodation/ food services	Transportation and communication	Real estate activities and consumer services
Estonia	0.2	10.2	0.8	14.3	24.1	3.8	13.8	32.8
Latvia	0.2	9.8	0.9	9.2	28.4	3.6	12.3	35.6
Lithuania	0.1	10.6	0.8	14.3	39.3	3.3	9.3	22.4
Poland	0.1	11.7	0.6	15.2	33.8	3.3	13.9	21.4
EU 28	0.1	9.4	0.7	14.7	27.9	8.2	9.5	29.5
Belarus	0.02	8.1	0.03	9.7	**48.7**	**1.6**	14.9	17.0

Sources: European Commission 2015c; Belstat 2015a; Belstat 2015c.

The Table 4 shows the distribution of SMEs across 8 areas of economic activity which compose the non-financial business economy. The percentage of small firms working in particular sectors in Belarus is compared with the percentage of SMEs operating in the same sectors in the whole European Union (EU 28) and 4 EU neighbors of Belarus: Estonia, Latvia, Lithuania and Poland. As one can see, the share of SMEs working in the wholesale and retail trade in Belarus is almost 40% higher than in its Western neighbors and the EU as a whole.

Almost a half of Belarusian non-financial SMEs perform trade activities. The number of firms operating in the second largest area of activity – the real estate and consumer services – is almost 3 times smaller. The Figure 3 visualizes the differences between Belarus and the EU countries which concern the shape of SME sector.

Figure 3. The structure of activities of SMEs operating in the non-financial business economy in Belarus, EU4 (Estonia, Latvia, Lithuania, Poland) and the EU 28 in 2013



Sources: European Commission 2015c; Belstat 2015a; Belstat 2015c.

In Estonia, Latvia, Lithuania, Poland and the EU 28 the distribution of SMEs differs from the distribution of small firms in Belarus. In the EU countries the share of small and medium enterprises operating in trade is only 30%. On the other hand, the share of firms operating in the real estate and consumer services in the EU is higher than in Belarus. While in the 4 EU neighbors of Belarus about 28% of SMEs perform this kind of activities, in Belarus the share of small firms operating in real estate and consumer services reaches 17%.

One may suppose that the share of SMEs operating in the real estate and consumer services in Belarus is smaller due to the smaller number of firms providing technically advanced services. In the Eurostat classification such types of activities are put into the category 'Professional, scientific, and technical activities' (e.g. scientific research and development, public relations, market research, management consultancy activities etc.) and 'Administrative and support services' (e.g. the activities of call centers, organization of trade shows, employment agency activities, rental activities etc.). However, an insufficiently detailed classification of economic activities used by the Belstat does not allow to identify precisely the cause of smaller presence of the firms providing real estate and consumer services in the SME population.

Another difference between the SME sectors in Belarus and the EU may be found in the accommodation and food sector. The share of firms running hotels and restaurants among Belarusian SMEs is more than twice lower than among SMEs in the Western neighbors of Belarus and 5 times lower than in the whole EU.

The analysis of employment shows similar, although less pronounced differences in the shape of SME sectors in Belarus and the EU. As one can see in the Table 5 and Figure 4, the share of SMEs performing trade activitiesis 25% higher in the employment in the Belarusian SME sector than in the EU countries. At the same time this difference in employment is smaller than the difference in the number of firms (40%). It allows to suggest that the Belarusian SMEs working in wholesale and retail trade are, as a rule, smaller than their Western colleagues. At the same time an average SME operating in the construction sector in Belarus is bigger than its counterpart in the EU countries. The same can be said about the firms operating in the real estate activities and consumer services.

The analysis of employment confirms another observation made during the analysis of the distribution of the SMEs across the economic sectors. The small and medium firms operating in accommodation and food services play much smaller role in the Belarusian SME sector than in the SME sectors of the EU countries. The share of hotels and restaurants in the employment in non-financial SME sector in Belarus is about two times smaller than in the employment in the non-financial SME sector in the EU.

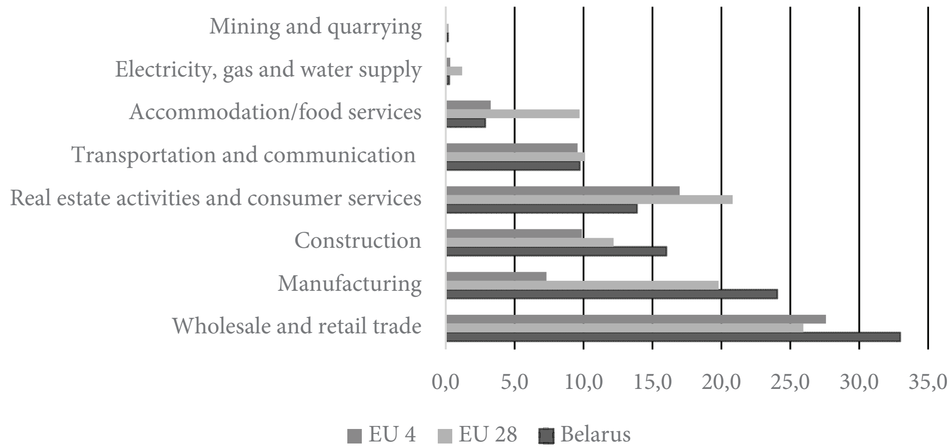
As it has been already mentioned, the share of *private* enterprises within the Belarusian SME sector remains unknown due to the non-transparent definition of private enterprises applied by the Belstat. Therefore the comparisons made above cannot provide precise information about how the structure of the *private* SME sector in Belarus differs from the structure of SME sector in the neighboring EU countries.

Table 5. The structure of employment in the SMEs operating in the non-financial business sector in Belarus, EU4 (Estonia, Latvia, Lithuania, Poland) and the EU 28 in 2013

Country	Mining and quarrying	Manufacturing	Electricity, gas and water supply	Construction	Wholesale and retail trade	Accommodation/ food services	Transportation and communication	Real estate activities and consumer services
Estonia	0.6	25.1	1.7	13.1	21.8	5.9	14.0	17.8
Latvia	0.6	20.0	2.1	12.5	26.4	5.7	13.3	19.4
Lithuania	0.4	21.4	2.2	12.6	29.4	5.1	14.5	14.4
Poland	0.4	24.5	2.3	13.1	30.7	3.6	10.8	14.6
EU 28	0.2	19.8	1.2	12.2	25.9	9.7	10.1	20.8
Belarus	0.2	24.1	0.3	16.0	33.0	2.9	9.7	13.9

Sources: European Commission 2015c; Belstat 2015a; Belstat 2015c.

Figure 4. The structure of employment in the SMEs operating in the non-financial business sector in Belarus, EU 4 (Estonia, Latvia, Lithuania, Poland) and the EU 28 in 2013



Sources: European Commission 2015c; Belstat 2015; Belstat 2015c.

However, some information about the structure of the private SME sector in Belarus may be drown from the comparison between single-person enterprises in the EU and individual entrepreneurs in Belarus. Until 2015 Belarusian individual entrepreneurs, by the majority of their characteristics, corresponded to the Eurostat category of sole entrepreneurs – single-person enterprises having no employees. Therefore, individual entrepreneurs were the only group of genuinely *private* enterprises which could be used as proxy-indicators for the whole private sector.

The comparison between the distribution of individual entrepreneurs in Belarus and sole entrepreneurs in the EU, however, confirms all previous observations. Private microenterprises in Belarus are disproportionately concentrated in trade. The share of small private firms operating in technically advanced services in Belarus is much lower than in the EU. The entrepreneurs running hotels and restaurants are underrepresented in the individual entrepreneurs' population as compared to the EU countries (European Commission 2015c; Belstat 2015a; Belstat 2015c).

The analysis of the number of Belarusian SMEs, their economic activities and the employment in the SMEs operating in the non-financial business sector allows to conclude that Belarusian small business significantly differs from the SME sector in the developed market economies. These differences concern not only the size but also the shape of the SME sector.

The contribution of Belarusian SMEs to the national economy is about two times lower than in its Western neighbors. The actors who determine its structure and define 'the rules of the game' are not SMEs but the government and large state-owned firms. Although the SME sector in Belarus provides jobs to more than one third of the population, its share in the employment remains significantly lower than in Belarus's Western neighbors. The Belarusian SME sector is more polarized than the SME sectors in the neighboring EU countries. It contains higher proportion of single-member enterprises which, according to some experts, have much more limited ability to innovate and grow as compared to other SMEs (Gagacka 2008: 93).

The Belarusian SME sector is not just a 2 times reduced copy of the SME sector in the EU countries. As compared to the Estonia, Latvia, Lithuania and Poland, the Belarusian SMEs are disproportionately concentrated in the wholesale and retail trade. Belarusian entrepreneurs are much more reluctant to provide sophisticated services as well as run restaurants and hotels. The causes which make Belarusian entrepreneurs to choose less complicated and capital-intensive spheres of activity will be described in further chapters of this research.

1.4. Legal and Macroeconomic Barriers to the SME Growth in Belarus

Such indicators as high concentration of the SMEs in retail, weaker orientation on providing technically advanced services, small contribution to the GDP as well as relatively small share in the employment allow to suggest that Belarusian SMEs face serious obstacles to grow and to transform into efficient productive business.

Before 2008 legal barriers were considered to be the major obstacles to the SME development in Belarus (Daneyko, Pelipas, Rakova 2003; Yelovskikh 2005). A priority given by Belarusian authorities to big state-owned enterprises and discrimination of private firms were well reflected in the state regulations. Long, complicated and costly procedures of business registration, high number of licenses and permissions, heavy tax burden, price regulation, excessive attention of the inspection bodies hampered the development of private firms (Pelipas, Rakova, Chubrik, 2007: 32).

However, regulatory reforms undertaken by the government in 2008-2011 significantly improved the situation. In the 2016 Doing Business ranking Belarus occupies the 44 position – just behind Belgium and Hungary. The ranking's authors estimate that Belarusian laws impose fewer barriers on the development of private firms than the regulations in Italy, Cyprus or Turkey. Belarus is on the 7 position in the world according to the easiness of registering property and on the 12 position in the world according to the ease of opening a firm (World Bank 2016).

The surveys carried out by the Institute of Privatization and Management (Tochitskaya, Skriba, Shimanovich 2011; Pelipas et al. 2015) as well as the International Finance Corporation (IFC 2013) among Belarusian SMEs confirmed that in the recent years the importance of legal barriers has decreased. The number of entrepreneurs declaring, that inspections, permissions and licensing procedures seriously impede the SMEs growth, dropped by half (see the Table 6). Such regulatory barriers as complicated tax administration procedures and frequent inspections remained among the most important ones, although their position dropped (IFC 2013: 9).

Since 2010 the majority of SMEs put macroeconomic factors on the top of the list: inflation, inadequate exchange rate policy and macroeconomic instability. Entrepreneurs also mention 'difficult access to finance' and 'instable legislation'. Different surveys conducted among Belarusian entrepreneurs in recent years provide very similar list of barriers to the business activity (IFC 2013: 9; Akulova 2012: 7).

Table 6. Percent of SMEs who consider administrative procedures as impediments for doing business in 2009 and 2012 (%)

Administrative procedures	2009	2012
Inspections	53.0	35.0
Tax administration	51.8	29.9
Obtaining permits	45.8	29.1
Price controls	41.8	28.8
Licensing	33.8	13.4

Source: International Finance Corporation 2013.

The surveys regularly carried out by the IPM among the state-owned and private SMEs having legal entity show that since 2010 the list of legal and macroeconomic barriers remains largely unchanged. During the survey entrepreneurs are asked to assess the importance of 20 'problems' of doing business in Belarus, enumerated in the exhaustive list. In 2015, similar to 2014, Belarusian SMEs declared that the following legal and macroeconomic barriers were the most important:

1. High inflation
2. Foreign currency market regulation
3. High taxes
4. Complicated tax procedures
5. Difficult access to finance
6. Inefficient government regulations
7. Corruption
8. Instability of the government policy
9. Theft and stealing
10. Rigid labor market regulations (Pelipas et al. 2015: 59).

However, the importance of particular barriers depends very much on the way of asking questions. Asked about the strength of *regulatory* impediments alone, also enumerated in the closed list, Belarusian entrepreneurs put tax procedures only on the 9 position. Top positions are occupied by:

1. Rent charges for premises
2. Red tape and complicated administrative procedures
3. Inadequately high penalties for infringements

4. Complicated certification procedures
5. High number of inspections (Pelipas et al. 2015: 19).

The IPM researches show that Belarusian entrepreneurs continue to feel discriminated as compared to the state-owned enterprises. They declare that the discrimination is the most visible in the attitude of the inspecting bodies, amount of property rents, requirements needed to meet in order to obtain permissions or licenses, inequality of prices for the row materials, access to credits, access to public procurement contracts as well as in the attitude of the courts (Pelipas et al. 2015: 17).

Moreover, in 2015, after a severe crisis broke out, Belarusian entrepreneurs declared that the discrimination increased as compared to the previous years. The highest was increase in the number of firms declaring that they had faced discrimination in getting permissions and licenses, in prices of raw materials and in access to the public procurement (Pelipas et al. 2015: 18).

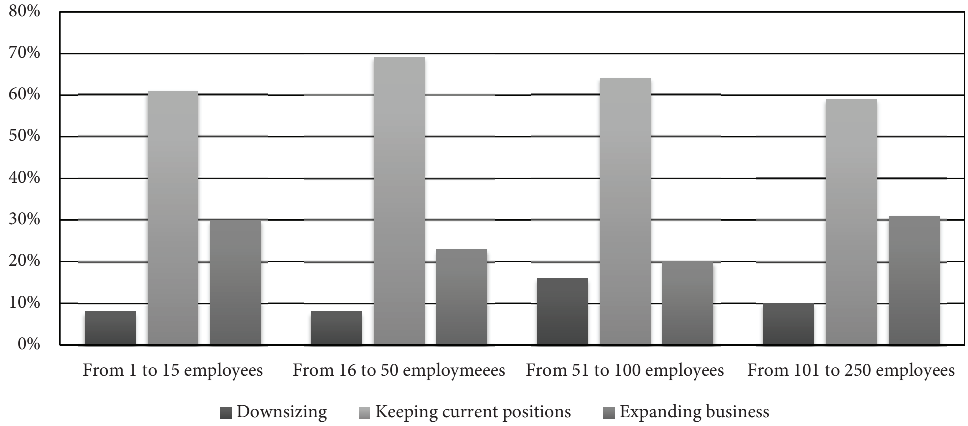
While the authors of the Doing Business ranking analyze mainly the legal acts affecting the business activity, the surveys conducted by the IPM and the IFC allow to see much wider range of barriers. They highlight the impediments resulting from unstable economic situation, long bureaucratic procedures and excessive activity of inspecting bodies. However, these surveys cannot fully explain why the SME sector in Belarus did not expand after the improvement of the regulatory environment. One may suppose the influence of other factors which are not covered by these researches.

One of these factors may be hostile activities of the state bodies which neither fall into the category of actions legitimized by law nor into the category of crime. More specifically, one should analyze extra-legal activities of the state institutions which aim is to subordinate private businesses or to hamper their development. While a significant number of legal barriers were removed in 2011–2013, extra-legal, informal barriers imposed by the state institutions could remain in place.

The surveys of the entrepreneurs realized by the IPM provide evidence of the suspicious attitude of the SMEs towards the state. For instance, they show that Belarusian SMEs remain reluctant to asking for the state support. Although 62.7% of respondents declared the need in external resources and 65% of respondents heard about the possibility of getting subsided loans from state-controlled financial institutions, only 6.7% of respondents used them (Pelipas et al. 2015: 39). A significant part of the respondents declared that there were 'more acceptable' sources of financial support, than the loans which interest is extremely low – it equals the National Bank's refinancing rate (Pelipas et al. 2015: 40). According to Pavel Daneyko (2001: 58) such paradoxical situation when entrepreneurs prefer to take very expensive commercial loans or illegal loans rather than to engage into cooperation with the state clearly signify that this cooperation induce very high transaction costs. And these costs must be higher than the costs of illegal or commercial credits.

The surprising unwillingness of Belarusian SMEs to grow may be another indicator of significant barriers which are not captured by any previous studies. The IPM surveys undertaken in 2014 and 2015 show that the bigger and older firms in Belarus feel better than the younger and smaller ones. They assess their economic situation as more stable and perceive the competition on the market as weaker. However,despite weakening competition, the willingness to expand diminishes with the increase of the firm's size (Pelipas et al. 2014: 14; Pelipas et al. 2015: 13).

Figure 5. Development strategy of Belarusian SMEs in a short-term perspective, depending on the firm's size



Source: Pelipas et al. 2015.

Such progressing 'laziness' may be explained by a simple increase in number of state enterprises in the analyzed group of SMEs. However, it can hardly explain the jump in enthusiasm among the largest firms (having more than 100 employees) where the share of SOEs is the biggest. Another explanation of this phenomenon may be that growing over a certain size imposes additional risks and increases the costs of doing business, which not every firm is ready to face. Those entrepreneurs who managed to overcome such invisible barrier due to their unique skills are much more optimistic about their future. The explanation of this phenomenon may be found not in the macroeconomic situation or formal regulations, but in the informal logic of the economic system where private sector is clearly subordinated to the state-controlled economy. A more detailed analysis of these disincentives to grow will be presented in the Chapter II.

A series of in-depth interviews with Belarusian entrepreneurs was used to identify some barriers to the development of Belarusian SMEs which fell out of the scope of previous researches. In the following chapter, a particular attention will be payed to the informal rules through which the state regulates the development of the small and medium private enterprises.

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