



# **INTERNATIONAL EXPERIENCE OF SMALL BUSINESS LENDING AND THE POSSIBILITY OF USING ITS EXPERIENCE IN UZBEKISTAN**

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## **Abstract**

*This paper analyzes the international experience of determining the quantitative and qualitative parameters of small enterprises (SEs), reveals the advantages, factors and functions of small businesses (SBs) in the national economy. The necessity of state support for the development of SBs is substantiated, the economic mechanism, forms and instruments of state support for SBs in developed countries and the national characteristics of their implementation in individual countries are revealed. On the basis of materials from OECD member countries, the state is analyzed, development trends and some lending problems to SBs are identified. Scientific conclusions have been obtained and recommendations have been developed practically aimed at using the accumulated rich international experience in lending to SBs in the conditions of Uzbekistan, taking into account its specific features.*

*Keywords: Small and medium enterprises, SMEs, small and medium businesses, sources of financing and crediting, government support, microfinance*

## **INTRODUCTION**

Small business is the most important subsystem of a market economy, creating the prerequisites for its sustainable development. Small business provides job creation with low capital costs, saturating the market with goods and services, tax revenues to budgets of all levels, employment of the population, promotes the development of human capital, competitive

markets and innovations, improve the standard of living and quality of the population and ensure social stability of society. Small businesses respond flexibly to changes in market conditions and are characterized by rapid turnover of resources, high growth dynamics, market saturation with goods and services, and the formation of a competitive environment. As world experience shows, factors affecting the development of small businesses are: Conditions of demand in the country; Specification of the sectoral structure of the economy and Business climate.

The business climate is to a large extent than the first two factors determined by the policy of the state, and its quality serves as an assessment of the government's work. At the beginning of the XXI century in economics and practice in the method of calculating small business by international economic organizations, instead of "small and medium enterprises", the more developed term "micro, small and medium enterprises" began to be used. Therefore, for emerging market economies, the important role of micro enterprises, which are the most typical representatives of small businesses, is emphasized.

The criteria for referring to "micro, small enterprises" (SE) generally differ between countries and international financial organizations. The main criteria for assigning an enterprise to a small or medium business (MB) are the number of employees, annual sales or annual income, as well as assets and capital. The International Finance Corporation will define small and medium-sized businesses as a registered form of enterprises (organizations) with a staff of up to 300 people and annual sales and assets of up to \$ 15 million. The definition adopted in the EU is widely used, where companies with less than 250 employees belong to the category SE and an annual turnover of no more than 50 million euros or a balance of no more than 43 million euros. In many APEC economies, for combining economic entities to the SE category, a combined approach is used which takes into account the quantitative (number of staff) and qualitative characteristics of the financial and economic activities of an enterprise.

Table 1. Criteria for assigning enterprises to the category of SE in the economies of the world

Economy	Employment				Sale volume				Notes
	Micro	Small	Medium	SME	Micro	Small	Medium	SME	
The USA				<500					Industry and wholesale <100
Canada	1-4	5-99	100- 499	<500					
Japan				<300					

EU	1-9	10-49	50-249	2	10	50	Micro	Balance
				million	million	million	Small	2 million euros
				euros	euros	euros	Medium	10 million euros
								43 million euros
China		<300	<2000	<30	<300			Industry
				million	million			assets: small
				yuan	RME			<40 million
								yuan, medium
								<400 million
								yuan
Russia	1-15	16-100	101-250	<60	<400	<1		
				million	million	billion		
				rubles	rubles	rubles		
Uzbekistan	1-20	21-100	101-250					

Source: Annual Report on European 2013/2014. A partial and Fragile Recovery

In the United States, enterprises in the industrial and wholesale sectors include enterprises whose personnel does not exceed 500 and 100, respectively, and in other sectors annual sales are used as a criterion: enterprises with an annual sales volume of less than 0 belong to small enterprises in the agricultural sector. 75 million US dollars, in the construction sphere - less than 31 million US dollars.

According to Eurostat, Germany is the leader in terms of small business development, such as the number of personnel employed in small and medium-sized businesses and the total turnover of SME companies. In terms of the total number of companies, Italy is in the first place, ahead of Germany by more than 1.5 times, France is in 3rd place in Europe in terms of small business turnover and in second place, after Italy in the number of companies. For the UK and Germany is characterized by a smaller number of companies, but a high turnover.

In accordance with the Resolution of the Cabinet of Ministers of the Republic of Uzbekistan in 2017 "On Amendments to the Classification of Organizations Related to Small Business" in Uzbekistan micro enterprises are small enterprises with not more than 20 people, small enterprises with no more than 100 people, medium-sized enterprises with an average annual number of employees of not more than 250 people.

In Uzbekistan and in Europe, the conditions for doing business by small and medium-sized enterprises vary greatly by region. According to the Presidential Decree of the Republic of Uzbekistan of April 7, 2014 “On additional measures to further improve the investment climate and business environment in the Republic of Uzbekistan” in labor-intensive industries such as food, light, construction materials industry, the average annual number of employees for small enterprises increased up to 200 people, which creates conditions for increasing the number of small businesses operating in these sectors. Consequently, the experience of effective use of regional advantages has a high potential for possible use in the conditions of Uzbekistan. Among the qualitative criteria inherent in small and medium enterprises should be introduced:

- Continuity of ownership and direct management of enterprises;
- The transparency of a small enterprise the size of which allows the owner to be aware of what is happening in the company;
- Special relationship of an entrepreneur with partners, resource suppliers and product buyers;
- Family business.

In modern conditions, small and medium-sized businesses become the main source of ensuring the sustainable development of the national economy.

In developed countries, small enterprises make up about 70-80% of the total number of enterprises (in particular, the USA employs 53% of the total working population in this sector, 72% in Japan, and 50% in EU countries). In the European Union countries, SMEs account for 1% of the total number of enterprises, but at the same time, they provide 20% of the total turnover of enterprises and 17% of the total employment of the population.

In general, the key industry in which small and medium-sized businesses have the maximum development potential is trade. The above circumstances are explained by the fact that, firstly, SMEs in trade reinvest in the local economy 10 times more than large retail chains, which at the same time reflects their large volume of purchases from local manufacturers. Secondly, SMEs contribute to diversification and increase the sustainability of the economy, provide a greater level of employment compared to network companies. Thirdly, they create a variety of assortment necessary for consumers. It is important to support such promising areas as manufacturing, construction, science and engineering.

Micro-enterprises with the number of personnel up to 10 people are the main employer in the European small and medium business. The number of employees in these companies is close to the number of staff in large companies.

Table 2. Sectoral structure of small and medium-sized businesses in Europe, in 2016

№	Sectors	Turnover, billion euros	In percent of total
1.	Minerals	72,6	0,5
2.	Production	2 720,0	18,7
3.	Energy Supply and Air Conditioning	479,3	3,3
4.	Water supply and sewage	146,5	1,0
5.	Construction	1 316,4	9,0
6.	Trade	6 582,3	45,2
7.	Logistics	755,9	5,2
8.	Hotels and catering	447,9	3,1
9.	Information and communication services	584,7	4,0
10.	The property	413,4	2,8
11.	Consulting science and engineering	1 041,6	7,2
	<b>Total</b>	<b>14 560,6</b>	<b>100,0</b>

Source: the report of the institute of analyzing investment politics

<http://xn--80aplem.xn--p1ai/analytics/Malyj-i-srednij-biznes-v-stranah-Evropy/>

This trend is typical for Uzbekistan in particular, in 2018 the share of registered small enterprises and micro firms in the trade amounted to 27.6% of the total number of registered small businesses in Uzbekistan.

Micro-enterprises with a staff of up to 10 people also occupy leading positions in terms of business turnover among SME companies. In second place - medium-sized companies from 10 to 250 people. With such a number, effective work is possible not only in the traditional microenterprise trade and services, but also in many high-tech industries.

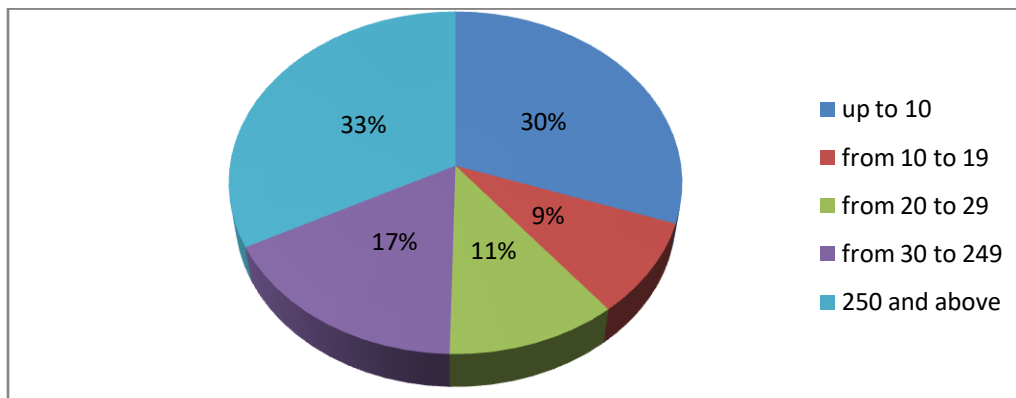


Figure 1. The structure of the European business by number of staff in 2016.

Source: the report of the institute of analyzing investment politics

<http://xn--80aplem.xn--p1ai/analytics/Malyj-i-srednij-biznes-v-stranah-Evropy/>

In 2017, small businesses and private entrepreneurship in Uzbekistan provided employment for 10,588 people or 78.3% of all people employed in the economy.

As the analysis shows, the level of profitability of micro enterprises and small enterprises has undoubted advantages over medium and large enterprises. Considering that a significant part of such microenterprises, in fact, the workplaces of their owners, a large positive role of small and medium business is obvious for the economy of the countries of Europe as a whole.

European experience in organization, development of small and medium business key indicators of improving efficiency and work (labor productivity, profitability of production, etc.) can be effectively used in the development of a long-term, transparent strategy and effective policy for the development of small and medium business in Uzbekistan.

In terms of “turnover per employee”, medium-sized businesses are leaders, outperforming, including big business. The above trend demonstrates the idea that by such an indicator as labor productivity, small and medium-sized enterprises are ahead of big business and work more efficiently.

Using the experience of European medium-sized companies can be a valuable tool for the development of SMEs in Uzbekistan.

Economic efficiency is an important factor in determining a significant proportion of microenterprises of up to 10 people in the European economy. In terms of gross profit margin, before deducting personnel costs microenterprises numbering up to 10 employees lead.

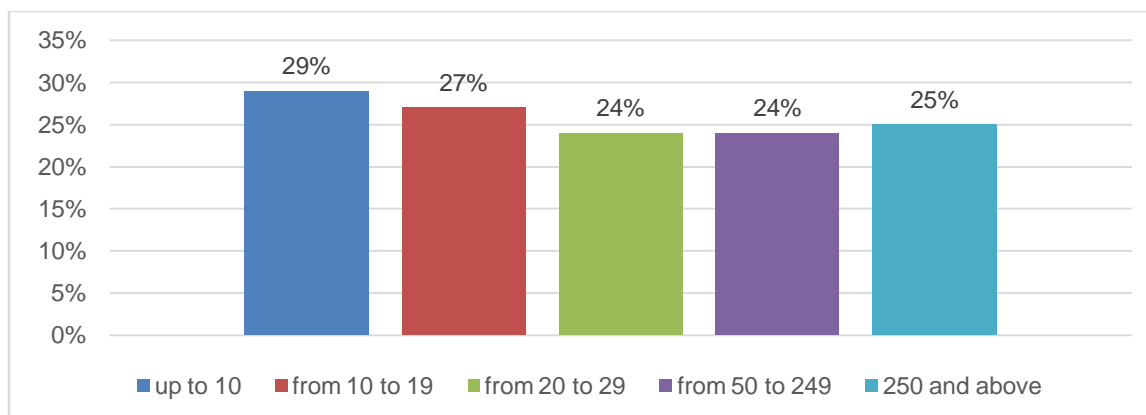


Figure 2. Gross margin before staff expenses (in percent of total, 2016.)

Source: the report of the institute of analyzing investment politics

<http://xn--80aplem.xn--p1ai/analytics/Malyj-i-srednij-biznes-v-stranah-Evropy/>

According to the European Bank for Reconstruction and Development (EBRD), in Kazakhstan there is a large gap between the need of small businesses for loans and their real supply. According to the World Bank Group, this gap is 47 billion dollars. USA.

In leveling the consequences of these barriers, an important role is played by the state policy and concrete measures of state support for SMEs. Government support is a key factor in the formation and support of small and medium-sized businesses. Government support is to provide the following conditions: preferential loans; reduction of tax payments; benefits for rental of premises; SME subsidies; partial compensation of bank rates; increase the classification at public expense; elimination of administrative barriers; provision of sureties. State support for SMEs is carried out in the following forms: financial, property, information and advisory, training, retraining and advanced training of their employees. The tools of state support for SMEs can be divided into direct (aimed at solving the problem of access to finance, fiscal policy measures) and indirect (aimed at creating a comfortable environment for doing business).

The development of the country has a long tradition of stimulating the activity of SMEs and has been supporting small and medium-sized businesses since the 1950s.

Table 3. Responsible organizations and instruments for financing SMEs  
in selected countries of the world. 2016

<b>Countries</b>	<b>Responsible organizations</b>	<b>instruments</b>
The USA	Small business administration	Providing state guarantees for SME bank loans, venture financing
Canada	Business Development Bank of Canada, Export Development Canada	Direct financial support, including the provision of venture financing, support for women's entrepreneurship, and the provision of loans under the small business financing program
Japan	Japan Financial Corporation	Providing long-term loans (start-ups, export activities of SMEs, loans to overcome the effects of external shocks), providing financial assistance to SMEs for restructuring credit debt
South Korea	SmallBusiness Corporation	State guarantees for bank loans to SMEs, lending to SMEs
Russia	Federal Corporation for the Development of Small and Medium Enterprises, SME Bank, Russian Venture Company (RVC)	Lending incentive program, guarantee support for SMEs (National Guarantee System), creation of venture funds for investment in SME projects in the scientific and technical sphere

Source: Financing SMEs and Entrepreneurship 2016. An OECD scoreboard. Federal Corporation for the Development of Small and Medium Enterprises. Russian Venture Company.

To improve the regulation and development of small and medium enterprises in the EU, a system of supranational, transnational and national authorities and organizations has been established. It takes into account the interests of the EU, individual member countries, the opinions of various business organizations, national sectoral and regional structures and associations of small business, chambers of commerce and industry.

In developed countries for a long period of existence of small business accumulated rich experience in lending to SMEs. In Uzbekistan, lending as a mechanism of state support for small enterprises is in its infancy. In this regard, it is important to use the most effective lending instruments for SMEs abroad.

Let us consider the features of the organization of the SME lending mechanism as a form of its state support in various countries in order to identify the most promising options for its use in Uzbekistan.

Long-term problems in financing small and medium-sized businesses limit the creation of new and growth in many countries, as a result of which there is a need for government intervention.

In OECD countries, after several years of growth in new loans to small and medium-sized businesses, this indicator again showed a negative value in 15 out of 25 countries. The average growth rate of the cost of new loans to small and medium businesses declined from 2.6% in 2015 to -5.6% in 2016 (Fig. 3).

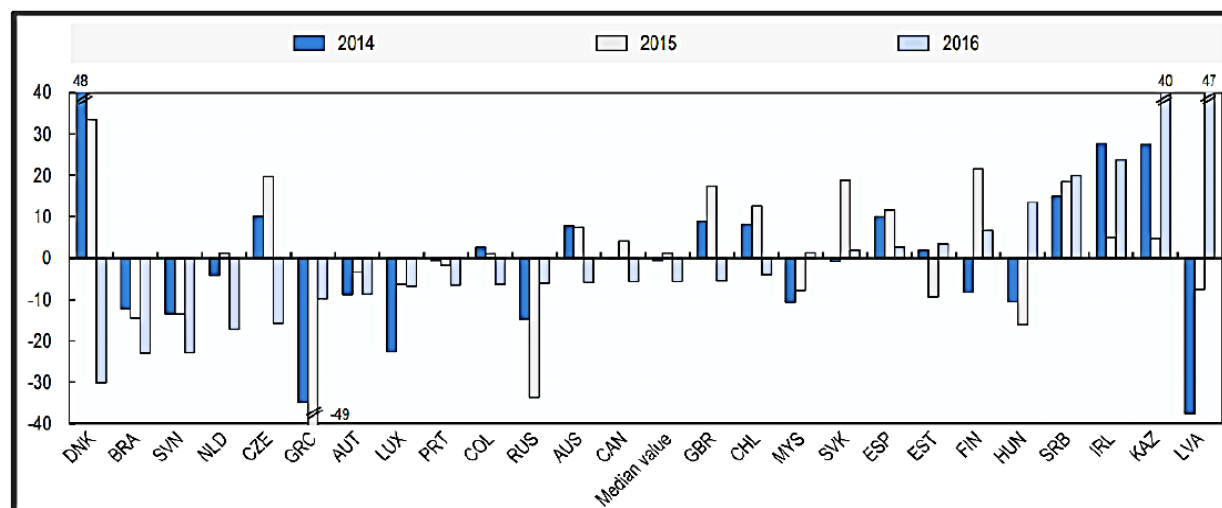


Figure 3. The trend of lending to small and medium-sized businesses (growth rate (%))

Source: the report of the institute of analyzing investment politics

<http://xn--80aplem.xn--p1ai/analytics/Malyj-i-srednij-biznes-v-stranah-Evropy/>



The decline in new loans can be explained by several factors, often related to national conditions. In Australia, Austria, the Czech Republic, the Netherlands and the United Kingdom, the reason for the reduction in the volume of new loans was a decrease in the demand for loans, which in turn is associated with a weak investment dynamics in this sector.

In other countries, such as Greece, Slovenia and Portugal, banking institutions, as it turned out, tightened the requirements for issuing loans to small and medium-sized businesses, as a result of the high level of loan defaults.

In Brazil and the Russian Federation, the decline is due in large part to adverse macroeconomic conditions.

In the prevailing OECD countries, the volume of outstanding loans by small and medium-sized enterprises increased in 24 out of 34 countries. The growth in the volume of outstanding loans depends on the rate of repayment of loans, changes in maturities and fluctuations in overdue debt, as well as on the inconsistency of trends in the available funds and loan flows to small and medium-sized enterprises.

As the data analysis shows, a structural shift in the direction from short-term to long-term lending to small and medium businesses occurs in the loan portfolio of banks. This trend is primarily due to a steady decline in the average value of the share of short-term loans in the period 2007–2016. The increase in profits and the acceleration of cash flow in small and medium-sized businesses will allow them to rely on the internal revenues of current activities, which, in turn, leads to a reduction in demand for external sources of financing.

As evidenced by the data, despite positive changes, structural problems of access to external sources of funding remain, in particular, open firms and start-ups, micro-enterprises and innovative enterprises with an uncertain business model. These enterprises often lack assets that can be easily used as collateral.

## **CONCLUSION**

The analysis of the mechanism of lending to small and medium-sized businesses led to the following conclusions:

- In world practice, a wealth of experience has been gained in the field of lending to small and medium-sized businesses;
- the conducted research shows that in the lending market for small and medium-sized businesses in developed countries (OECD) there has been a reduction in all major indicators of a decrease in interest in credit products. The decrease in interest rates on credit products mainly leads to an increase in the volume of loans issued. Starting from 2016, the volume of

loans provided tends to decrease, the reason for which is the tightening of the requirements for issuing loans to small and medium-sized enterprises;

- analysis of foreign experience in financing small and medium businesses allows us to conclude that in Uzbekistan it is necessary to use more positively the experience of developed countries. This implies the improvement of the regulatory framework, the development of an effective system of external financing that meets the conditions of a comprehensive socio-economic approach using regulatory tools. Further studies shall analyze the impact of tax reforms on SMEs in Uzbekistan.

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