OECD Studies on SMEs and Entrepreneurship

RUSSIAN FEDERATION

KEY ISSUES AND POLICIES

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Foreword

The government of the Russian Federation has recently stepped up its attention to the promotion of small and medium-sized enterprises (SMEs) considerably, by taking actions to create a more competitive business environment and introducing public programmes to tackle barriers in areas such as skills, finance, and innovation. Russian SMEs currently represent less than 30% of the workforce, but the government's intention is to increase this to 50% by 2020.

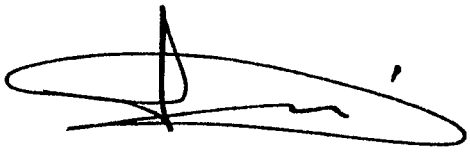
The SME Act of 2007 was an important milestone. It increased the state budget allocated to the federal SME support programme, enabling a range of new programme measures to be introduced including entrepreneurship centres offering business services to SMEs and entrepreneurs, technoparks, innovation centres, business incubators, training and marketing centres, consulting centres and export centres. The Act also brought simplified tax accounting rules, privileged procedures for SMEs to purchase privatised state property for business use, and an accelerated process of reform in the areas of administrative, regulatory, competition, and public procurement policy. At the same time, the government acted to facilitate the access to SMEs and entrepreneurs to finance through new investment funds and leasing companies, loan guarantees to commercials SME lending and the establishment of the SME Bank, as an arm of Vnesheconombank, the public development bank.

These measures are very important for economic growth and job creation. Nonetheless, the Russian Federation still suffers from a significant gap in the scale of its SME and entrepreneurship activities compared with OECD countries and other emerging economies, demonstrated by a low business start-up rate, few SMEs per head of population, limited employment in SMEs, and weak SME innovation and growth performance. To tap into the benefits of SMEs and entrepreneurship for job creation and social inclusion, competition and efficiency, and innovation and exports, further reform will be needed, while the policy investments that are made will need to be appropriate, effective and efficient. This report reviews the situation and the key policy challenges and makes recommendations for further policy development in the Russian Federation.

One key issue concerns how the population at large views entrepreneurship. A significant shift towards more positive attitudes will be critical to motivate large numbers of people to start up enterprises. High levels of informality in the economy are another concern given the tax implications and the tendency of such businesses to remain inefficient and small. The business environment also needs to be the focus of further improvements aimed at increasing competition, reducing the administrative and tax burden on enterprises and better exploiting the Russian science base through the development of a firm-centered, market-oriented innovation system. Furthermore, despite recent progress, the volume of bank credit to SMEs remains low by international standards, and SME loan turndowns and interest rates are high.

In addressing these challenges, policy makers should focus not only on individual policy actions, but also on designing a more strategic approach to SME and entrepreneurship policy. This approach should identify and respond to the policy needs of different types of entrepreneurs and SMEs in an integrated manner, and should exploit the strengths of both national and regional governments.

The OECD is pleased to be able to contribute to the emergence of a much more substantial and competitive SME economy in the Russian Federation by supporting the Russian government's policy assessment and reflections and identifying priorities and opportunities for action. To this end, this report offers a systemic overview of where the government could intervene to overcome barriers in the business environment, in SME financing and in the existing set of policy and programme arrangements at national and local levels. The OECD will continue to offer its support in the coming years through monitoring progress and offering various in-depth proposals for policy actions.



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Organisation for Economic Co-operation and Development

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The information within the report is based on responses to a Fact-Finding Questionnaire completed by the Russian authorities, information gathered during OECD study missions to the Russian Federation, a range of OECD international comparative data and further information gathered from secondary sources. Important operational support for the work was provided by Eugeny Tcherbakov of *Vnesheconombank* and Natalie Minaeva of the Russian Federation Ministry of Economic Development.

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Abbreviations and acronyms

ASI	Agency for Special Initiatives
BRIC	Brazil Russia India China
CEO	Chief Executive Officer
CFE	Russia Centre for Entrepreneurship
CIS	Commonwealth of Independent States
EACEA	Education, Audiovisual and Culture Executive Agency (of the European Commission)
EBRD	European Bank for Reconstruction and Development
ECA	Eastern Europe and Central Asia
EU	European Union
FAS	Federal Antimonopoly Service
FASIE	Foundation for Assistance for Small Innovative Enterprises
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
GEM	Global Entrepreneurship Monitor
HEI	Higher Education Institution
IEA	Inter-regional Economic Association
IFC	International Finance Corporation
ILO	International Labour Organisation
IMF	International Monetary Fund
IPR	Intellectual Property Rights
KTP	Knowledge Transfer Partnership
MED	Ministry of Economic Development
MFI	Micro Finance Institution
NGO	Non-Governmental Organisation
OECD	Organisation for Economic Co-operation and Development
OPORA	Russian non-governmental organisation representing SMEs and entrepreneurs
R&D	Research and Development
RIA	Regulatory Impact Assessment
RSBF	Russia Small Business Fund
RUAEE	Russian Association for Entrepreneurship Education
RUB	Rouble

RVF	Russian Venture Fund
SEZ	Special Economic Zone
SIORA	Russian Agency for Support of Small and Medium Business
SME	Small and Medium-sized Enterprise
SOE	State Owned Enterprise
STI	Science Technology Innovation
TEA	Total Entrepreneurial Activity
UAE	United Arab Emirates
UK	United Kingdom
UNCTAD	United Nations Conference on Trade and Development
USA	United States of America
VAT	Value Added Tax
VC	Venture Capital
VEB	Vnesheconombank
WEF	World Economic Forum
WTO	World Trade Organisation

BASIC STATISTICS OF THE RUSSIAN FEDERATION

(2013, unless otherwise noted)

LAND AND PEOPLE			
Population (millions) 2014	143.9	Inhabitants per sq. km	8.4
Population under 15 (percentage) 2014	16.5	Area (thousand sq. km)	17 098
Population over 65 (percentage) 2014	13.3	Life expectancy at birth: men, 2012	64.6
Latest 5-year average population growth (2009-2014, percentage)	0.15	Life expectancy at birth: women, 2012	75.9
LABOUR MARKET			
Employment (millions) 2013	67.8	Unemployment rate (percentage of labour force, end-year) 2012	5.5
By sector (percentage of total)		Long-term unemployed as a percentage of the unemployed	31
State and municipal enterprises and organisations	28.4	Self-employment rate (percentage)	7.3
Private sector	60.0	Tertiary educational attainment 25-64 year olds (percentage, 2011)	53.5
Mixed form of ownership/Other	11.6		
By branch (percentage of total)		Inhabitants in major cities (millions, estimated) 2014	
Industry	17.6	*Moscow*	12.1
Agriculture and forestry	9.5	*St. Petersburg*	5.1
Construction	8.4	*Novosibirsk*	1.5
Services/Other	64.5	*Yekaterinburg*	1.4
GOVERNMENT/ADMINISTRATION			
Bicameral Parliamentary system (The Federal Assembly)		Regional government	
Council of the Federation (upper house)	169 seats	Subjects of the Federation, of which:	83
State Duma (lower house)	450 seats	*Republics*	21
Number of registered political groups in the State Duma	4	*Krais (territories)*	9
		Oblasts (regions)	46
		Autonomous oblast	1
		Autonomous okrugs (areas)	4
		City of Moscow	
		City of St. Petersburg	
PRODUCTION			
GDP (RUB billion, current prices)	66 190	GDP growth (percentage)	1.3
GDP per capita (USD, current prices, current PPP, estimated)	25 366	Average GDP growth (2010-2013, percentage)	3.4
Inflation rate: all items (percentage) 2014	7.8	Long term interest rates (percentage) 2014	8.46
Inflation rate: food (percentage) 2014	10.3		
PUBLIC FINANCE			
General government revenue (percentage of GDP) 2012	40.7		
General government expenditure (percentage of GDP) 2012	38.7		
FOREIGN TRADE AND FINANCE			
Exports of goods and services (USD billion) 2014	472.2	Exports of goods and services as a percentage of GDP 2014	30.02
Imports of goods and services (USD billion) 2014	403.1	Imports of goods and services as a percentage of GDP 2014	22.87
THE CURRENCY			
Monetary unit: Rouble			
Currency units per USD (period average):			
Year 2013	31.8		
Year 2014	38.4		

Source: OECD National Accounts database *http://dx.doi.org/10.1787/na-data-en*, country profile of Russian Federation *http://data.oecd.org/russian-federation.htm*, and trade in goods and services database *http://data.oecd.org/trade/trade-in-goods-and-services.htm*, and Russian Federation State Statistics Service, Russia in Figures 2013, *http://www.gks.ru/wps/wcm/connect/rosstat_main/rosstat/en/figures/population*.

Executive Summary

The state of SMEs and entrepreneurship in the Russian Federation

There is great potential to accelerate economic growth, job creation and diversification in the Russian Federation by lifting its rate of business creation and the numbers and competitiveness of its small and medium-sized enterprises (SMEs). There are substantial gaps to be made up with most OECD countries and a range of other emerging economies. Less than 30% of the Russian Federation workforce is employed in SMEs compared to more than 50% in every OECD country. Only 5% of the Russian Federation's adult population is currently involved in starting or running a new business compared with 16% in China and 18% in Brazil. Only 5% of Russian Federation SMEs undertake any type of innovation, compared with typical rates of around 50% in OECD countries. The Russian president has set ambitious targets to increase the contribution of SMEs to the Russian economy, including growth in the share of GDP generated by SMEs from 25% in 2012 to 50% in 2020. This report examines how government policy can help achieve these objectives.

Areas for improvement in framework conditions

High levels of product market regulation and state involvement in the economy, including a large share of state-owned enterprises in production, make it difficult for new private firms to enter parts of the market. And although the administrative burden has reduced greatly thanks to recent reforms, which cut the average number of days required to start a business from 43 in 2004 to 15 in 2014, there are still significant obstacles in areas such as construction permits, export and import permissions and obtaining electricity. There are also widespread perceptions of corruption in business transactions, which reduce incentives to start and run small businesses and the ability to plan and invest. Entrepreneurial attitudes and competences also need to be spread across the population. Three-quarters of non-entrepreneurs in the Russian Federation doubt that they have sufficient knowledge and experience to undertake entrepreneurial activity. SME workforce skills also need to be improved; in 2012 only 20% of Russian Federation adults participated in any formal or informal training, compared to an average of approximately 50% in OECD countries. And SMEs and entrepreneurs in the Russian Federation still have relatively poor access to bank loans, which constrains their investment and reduces their ability to handle short-term liquidity problems.

Good policy foundations to build on

A positive momentum is being built up by public policy on the road to a more entrepreneurial Russian Federation. The 2007 federal SME Act introduced a stable and supportive SME and entrepreneurship policy framework including clear guidance on policy objectives, the types of actions to pursue, and the responsibilities of different government actors. The federal budget for SME and entrepreneurship programme actions

was substantially increased from RUB 3.9 billion in 2008 to 23 billion in 2014. Wide-ranging competition and privatisation programmes have been launched, administrative and regulatory simplification has been advancing rapidly, and a business development services support infrastructure has started to emerge. *Vnesheconombank* (VEB), the public development bank, is also making a major contribution to improving the access of SMEs and entrepreneurs to credit by making substantial state lines of credit available for SME lending to partner banks and in 2014 a new federal credit guarantee agency was established.

Increasing the programme emphasis on the capabilities of SMEs and start-ups

Support for start-ups is essential if large volumes of new SME and entrepreneurship activity are to be stimulated. However, alongside the current provision of start-up grants and loans, more emphasis is needed on complementary training and information on entrepreneurship for those interested in business creation. In addition, there is substantial expenditure on blanket plant and equipment subsidies in the current federal SME support programme. These subsidies do not appear to be the most effective tool available for supporting the take-off of existing SMEs. Instead, greater emphasis should be given to actions that support the capabilities of SMEs and entrepreneurs to develop new markets and innovate in their product, services and production methods. At the same time, new federal programmes should be considered for raising awareness of the benefits of entrepreneurship in the population, introducing entrepreneurship teaching across the education system, promoting high-growth enterprises and developing local SME supply chains around large firms and inward foreign direct investors.

More incubators and business development services centres

To support a greater policy focus on building the capabilities and strategies of SMEs and entrepreneurs, a step up should be made in the level and quality of business development services on offer in the Russian Federation. Basic training and advice services should be offered to a large population of entrepreneurs and potential entrepreneurs given the need to substantially raise the level of business start-up in the Russian Federation. Such basic services could be provided through expanding the resources of the entrepreneurship centres as well as by exploring on-line support. In addition, more intensive business development services should be offered for firms with strong growth potential alongside financial support. For example, business incubators could offer increased company diagnosis, advice, and consultancy for entrepreneurs and SME managers in manufacturing and knowledge intensive business services with growth potential. The density of business development services facilities including business incubators, innovation centres and export centres is very low in the Russian Federation in comparison with other countries and with the number of enterprises to serve and the size of the geographical area to cover. Effort is therefore needed to increase their numbers. This will require both direct federal and regional government investments and new partnerships with business service centre promoters from the private and non-profit sectors. At the same time, the quality of the incubators and business development services centres should be increased by introducing a wider range of mentoring, consultancy and advice services in the incubators, improving performance monitoring of all the centres and supporting the professional development of their managers, staff and consultants, and creating a national first-stop shop entry point into the business services system.

Better access to finance

New measures should also be developed to improve the access of SMEs and entrepreneurs to finance. On the supply side, an important step forward has been taken with the creation of a federal credit guarantee agency in 2014. It is important that the roll out of its activities be informed by robust evaluation results and reference to international good practices in the design and operation of loan guarantee programmes. A further critical intervention still needs to be put into action, namely building up a central repository of credit information on individuals and businesses, including all their transactions with state-backed finance bodies, and making the information accessible to all potential lenders and investors against payment of a fee. This will help overcome lack of information to potential lenders to assess credit risk, which is one of the most important constraints to SME lending in the Russian Federation. In addition, more support should be given to increasing the inter-bank trading of SME loans, encouraging the development of a more substantial business angel sector and securing the legal rights of minority investors. The governance of the micro finance sector should also be strengthened, including measures to reduce the sway of "payday lenders" with excessively high interest rates. The public development bank, *Vnesheconombank*, has an important role to play in each of these areas. In addition, its range of financial products should be expanded in the areas of loan guarantees, equity participation and hybrid debt-equity instruments.

There is also a need for action on the demand side to improve the financial knowledge and skills of entrepreneurs. This will help improve the quality of applications for lending and other types of finance. *Vnesheconombank* can also play a critical role in this respect, by driving forward new financial education programmes for businesses and lenders.

Reaching out across the regions

Achieving ambitious targets for national growth in SMEs and entrepreneurship, and achieving objectives for balanced spatial development, will mean stimulating improvements in local regulations and programmes that spread across the Russian Federation's regions. The availability of competitive federal government co-funding of regional SME and entrepreneurship programmes is an important instrument that helps promote local action and align it with federal priorities. However, many regions do not participate in key federal programmes. More flexibility in the rules for participation and increased dialogue between weaker regions and the federal government would help. Consideration could also be given to new fiscal arrangements that could allow sub-national governments to retain more of the gains from increased business taxes. It must also be recognised that the Russian regions are very diverse in their conditions for SMEs and entrepreneurship, which requires some variation in the nature of the programme support that they provide. There are many examples of local programmes that are well adapted to local needs. This can be given a boost by federal actions to support the more widespread development of distinct regional development strategies.

Chapter 1

Assessment and Recommendations

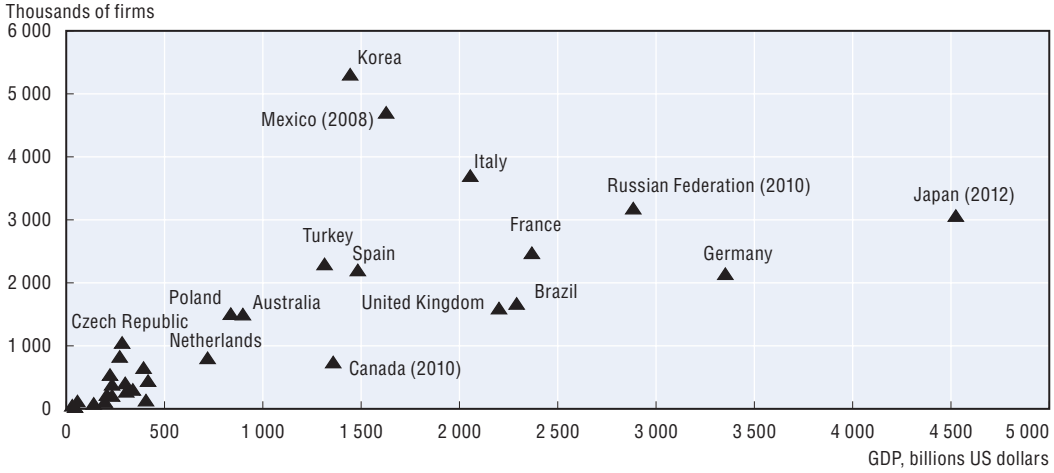
SME and entrepreneurship performance

Shortfall in the scale of SME activity

One of the most distinctive features of the Russian Federation's SMEs is their relatively small contribution to the economy compared with other OECD countries and emerging economies. In real terms (i.e. excluding significant numbers of enterprises that are registered but not in operation), there were only 3.2 million operating businesses in the business sector in the Russian Federation in 2010. By international standards, this is a relatively small figure when juxtaposed with the size of the economy (Figure 1.1). Italy, Mexico and Korea, for example, each have more businesses than the Russian Federation although the total outputs of these countries are smaller. The rate of 31 registered enterprises per 1 000 working population in the Russian Federation is well below that of the OECD countries, and is low in comparison to rates of 67 in Mexico and 102 in the United States.

Figure 1.1. **Number of enterprises and GDP**

2011 or latest available year



Note: Figures refer to the number of operating enterprises in the business sector, excluding the agriculture and government sectors. They include registered enterprises and the self-employed.

Source: OECD (2014) Entrepreneurship at a Glance 2014, Paris. *http://dx.doi.org/10.1787/entrepreneur_aag-2014-en*. Figures for Russian Federation from Rosstat SMEs in Russia (2011).

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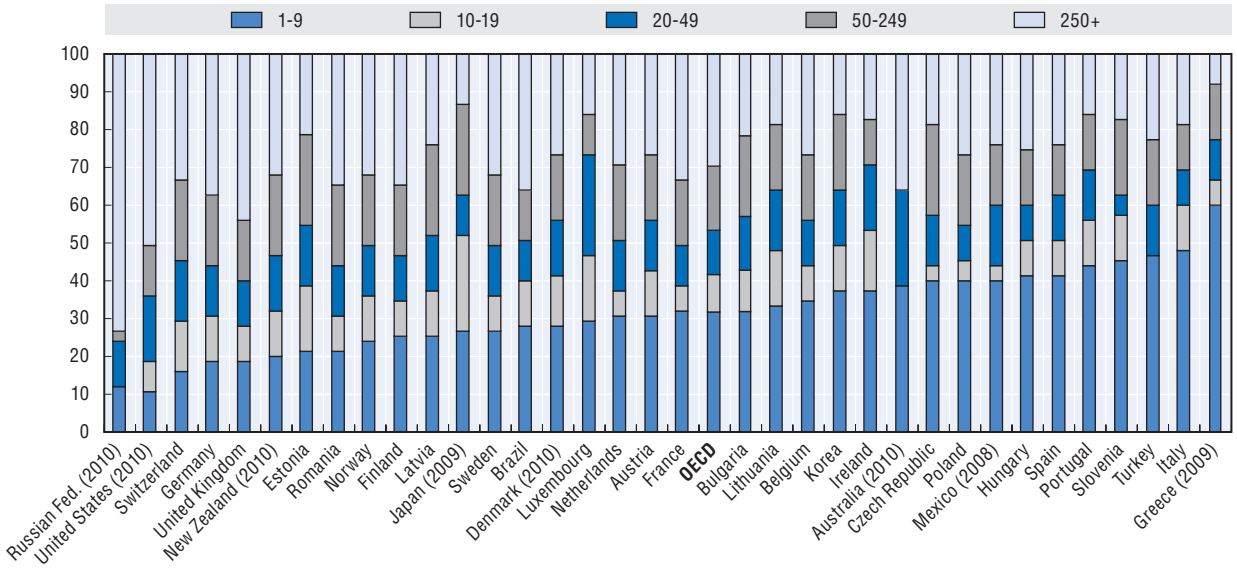
The shortfall in SME activity also shows up in employment figures. The Russian national statistical office estimates that SMEs and the self-employed in the business sector in the Russian Federation provided more than 18 million jobs in 2010. Although this is a substantial figure, at just under 30% of total employment, the employment share of SMEs in the Russian Federation was well below that of key comparator countries (Figure 1.2) such as Germany (65%), Mexico (74%) or the OECD average (71%). The proportion of business employment in small firms (defined as 1-15 employees in the Russian Federation) at 13% is smaller than that of employment in small firms (defined as 1-9 employees) in almost all OECD countries.

Figure 1.2. **Share of employment by enterprise size class**

Percentage values, 2011 or latest available year



Note: Data refer to the business sector, excluding the agriculture and government sectors. The size-class breakdown 1-9, 10-19, 20-49, 50-249, 250+ provides for the best comparability given the varying data collection practices across countries. Some countries use different conventions: the size class "1-9" refers to "1-10" for Mexico; "1-19" for Australia and Turkey; the size class "10-19" refers to "11-50" for Mexico; the size class "20-49" refers to "20-199" for Australia and "20-99" for the United States; the size class "50-249" refers to "50-299" for Japan, "51-250" for Mexico and "100-499" for the United States; finally, the size class "250+" refers to "200+" for Australia, "300+" for Japan, "251+" for Mexico and "500+" for the United States. Figures for Russian Federation: «1-9» refers to 1-15; «20-49» refers to 16-100 «50-249» refers to 101-250.

Source: Entrepreneurship at a Glance 2014, OECD Publishing. *http://dx.doi.org/10.1787/entrepreneur_aag-2014-en*. Figures for Russian Federation from Rosstat SMEs in Russia 2011 and Rosstat databases.

StatLink *http://dx.doi.org/10.1787/888933271709*

Acting forcefully in making up the gap in SME density and employment is a major challenge for institutions in the Russian economy, but one that could have dramatic impacts on job generation and income growth as well as diversification from natural resources exports.

Low output and investment

National statistics indicate that Russian SMEs accounted for only 32% of enterprise sales in 2012. While not strictly comparable with international data, this proportion is well below the more typical figure in OECD countries of around two-thirds of business value added generated by SMEs. In addition, national statistics indicate that SMEs were estimated to account for only 7.6% of the total fixed capital investments of businesses and 23.5% of the fixed assets of the total enterprise sector in 2012.

Weighting to non-manufacturing sectors

SME activity in the Russian Federation is strongly weighted towards wholesaling and retailing, hotels and restaurants, transport and communications, construction and electricity, and the consumer-oriented real estate, renting and business services sectors. By contrast, manufacturing SMEs represented only 7% of all SMEs and only 13% of total SME employment. At the same time, less than 20% of manufacturing employment in the Russian Federation was in SMEs, compared for example with 49% in the United States, 51% in Mexico, 52% in Brazil, 61% in Poland, 71% in Korea and 76% in Italy and Bulgaria.

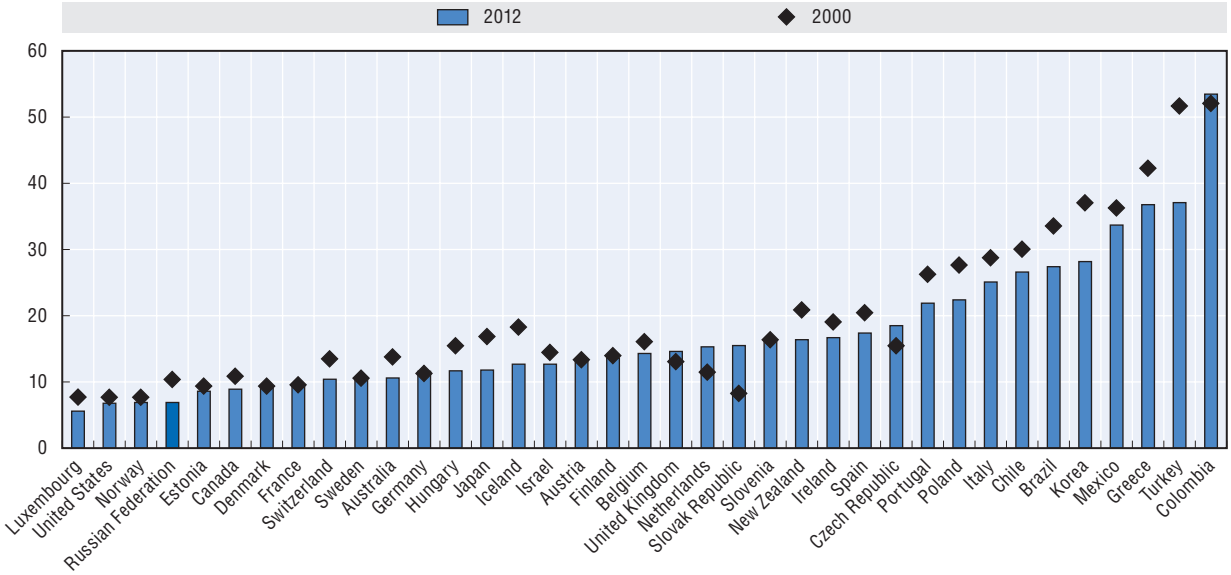
The weighting to non-manufacturing sectors is concerning given the relative potential of manufacturing in the Russian Federation to drive export growth, supply chain growth and long-run productivity growth.

Low self-employment

Only 6.9% of workers were formally registered as self-employed in the Russian Federation in 2012, whereas the average for OECD countries is 17.0% (Figure 1.3). Moreover, the share of self-employed in the Russian Federation declined between 2000 and 2012.

Figure 1.3. **Share of self-employment in total employment**

Percentage, 2012 and 2000



Note: Figures for Brazil and Columbia are for 2001 not 2000; figures for Chile France and Luxembourg are for 2011 not 2012; figures for Australia, Canada, and United States for do not include incorporated self-employed.

Source: OECD Annual Labour Force Statistics Database *http://dx.doi.org/10.1787/lfs-data-en.*

StatLink *http://dx.doi.org/10.1787/888933271712*

Low start-up rate

A high business start-up rate is needed to fill the Russian Federation's SME shortfall and renew the enterprise stock with more efficient and innovative enterprises. However, according to the Global Entrepreneurship Monitor (GEM), just 2.4% of the Russian Federation's adult population was engaged in trying to establish a new business in 2014. This compares to an average of approximately 8.2% in efficiency-driven economies, and rates of 3.7% in Brazil and 5.5% in China for example (Table 1.1). The new business ownership rate is also very low (i.e. running a business that has been operating for more than 3 months but less than three and a half years).

On the other hand, the Russian economy is very inclusive of women entrepreneurs. According to GEM, women accounted for approximately 44% of nascent entrepreneurs, 40% of new business owners, and 47% of established entrepreneurs in the Russian Federation in 2010.

Table 1.1. **Entrepreneurial activity rates in efficiency-driven economies, 2014**
Percentage of adult population

	Nascent entrepreneurs	New business owners
Argentina	9.5	5.2
Barbados	8.5	4.2
Bosnia and Herzegovina	4.5	2.9
Brazil	3.7	13.8
Chile	16.6	11.1
China	5.5	10.2
Croatia	6.0	2.0
Hungary	5.6	3.9
Latvia (2013)	8.1	5.3
Lithuania	6.1	5.3
Malaysia	1.4	4.6
Mexico	12.7	6.4
Panama	13.1	4.1
Peru	23.1	7.3
Poland	5.8	3.6
Romania	5.3	6.2
Russian Federation	2.4	2.4
Slovak Republic	6.7	4.4
South Africa	3.9	3.2
Thailand	7.6	16.7
Trinidad and Tobago	7.5	7.4
Turkey (2013)	5.5	4.7
Uruguay	10.5	5.8

Note: Nascent entrepreneurs are currently involved in starting a business either as owners or co-owners. New business owners are currently owners, owners or managers of businesses that are less than 42 months old.

Source: Singer, S., J.E. Amorós, and D.M.Arreola (2015), Global Entrepreneurship Monitor 2014 Global Report. Babson College, Universidad del Desarrollo, Universiti Tun Abdul Razak, and Tecnológico de Monterrey.

StatLink http://dx.doi.org/10.1787/888933272252

Negative perceptions about the feasibility of entrepreneurship

Increasing the business start-up rate is likely to require improvements in attitudes towards entrepreneurship. Although two-thirds of Russian adults consider that entrepreneurship would be a good career choice, there are several problematic areas. For example, GEM reports that only 27% of adults perceived good opportunities for starting a business in the Russian Federation in 2014, compared with averages of 42% and 39% in efficiency-driven and innovative-driven economies respectively. Critically, only 3.5% of those Russians not involved in entrepreneurial activity reported that they intended to start a business within the next three years, compared with an average of 23% for other efficiency-driven economies. More than 70% of Russians who were not entrepreneurs believed that they did not have the skills and competences to start a business.

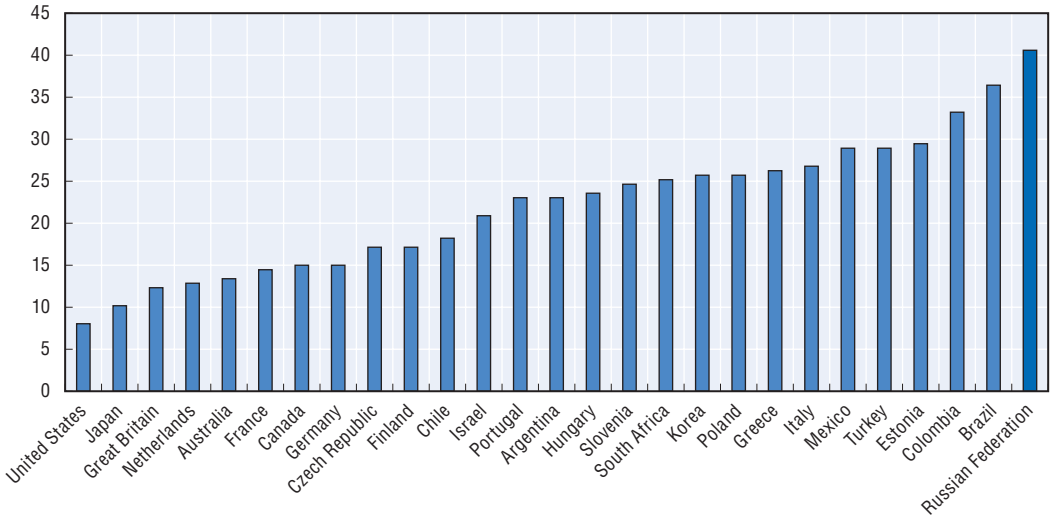
Large informal economy

Some of the gap in formal SME and entrepreneurship activity in the Russian Federation, as counted in official business registers, is the reflection of a relatively large informal sector. Although difficult to quantify precisely, estimates from an International Labour Office (ILO) survey suggest that the Russian Federation may have had 7.78 million undeclared jobs in the informal sector in 2011, representing some 12.1% of non-agricultural employment. Using an alternative approach, the Schneider measure suggests that as much as 40% of

economic activity in the Russian Federation could be informal in nature, significantly greater than in OECD countries and many other emerging economies (Figure 1.4).

Figure 1.4. **The estimated scale of the informal economy, Schneider definition**

Percentage of economic activity, 2007



Source: OECD (2011), OECD Economic Surveys: Mexico 2011, OECD Publishing, Paris. *http://dx.doi.org/10.1787/eco_surveys-mex-2011-en* based on International Labour Office (2011). Statistical Update on Employment in the Informal Economy, International Labour Office, Department of Statistics.

StatLink *http://dx.doi.org/10.1787/888933271740*

While many people in the Russian Federation can at least access employment opportunities through informal entrepreneurial activity, the cost is relatively low productivity, low incomes, poor working conditions, and foregone public sector tax revenues.

Low SME innovation rates

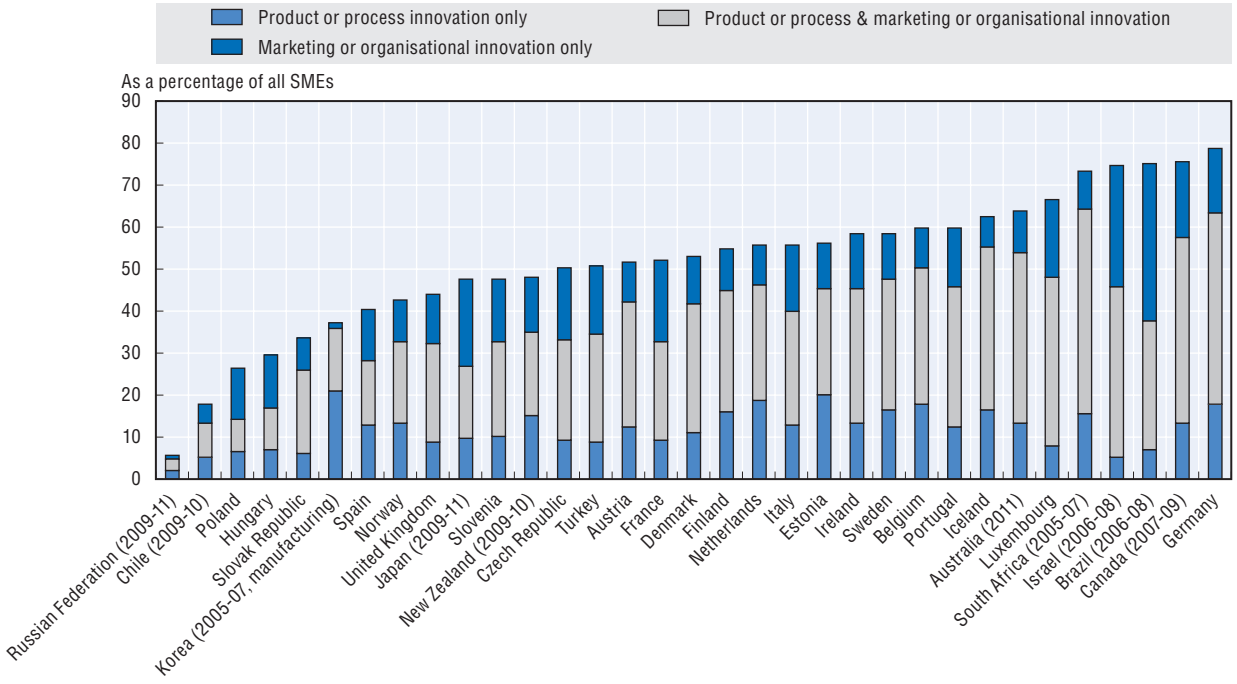
As shown in Figure 1.5, less than 6% of Russian SMEs reported involvement with innovation activity of any kind (product, process, marketing or organisational) in 2009-11, compared with an average of around 50% in OECD economies. Similarly, the government's 2011 SME Census found that only 1.6% of SMEs made specific expenditures on innovation. The GEM 2012 survey also found that more than 70% of Russian entrepreneurs offered products and services that were not that new for consumers, and 94% did not use newer technology in their business activity. These low innovation rates are likely to be an important drag on SME productivity and competitiveness.

By contrast, by 2012, two-thirds of Russian Federation businesses were using their own websites according to the IFC/World Bank Enterprise Survey, compared with less than one-half in Eastern Europe and Central Asia and in Upper Middle Income countries.

Importance of high-growth enterprises

In most economies, a small number of high-growth enterprises play a major and highly disproportionate role in job creation. Better data are required to assess the performance of the Russian Federation in terms of generating high-growth enterprise. While there is no direct measure available of the proportions of actual high growth enterprises, there is some information available from the GEM survey on growth aspirations. GEM indicates that early-stage entrepreneurs expecting to create more than 20 jobs within five years of

Figure 1.5. **Innovating SMEs by type of innovation**
2008-10 or latest available years



Source: OECD (2013), Innovation types by firm size, 2008-10: As a percentage of all SMEs and large firms, in OECD Science, Technology and Industry Scoreboard 2013, OECD Publishing, Paris. DOI: *http://dx.doi.org/10.1787/sti_scoreboard-2013-graph165-en*.

StatLink *http://dx.doi.org/10.1787/888933271752*

business start-up represented 0.46% of the adult population in the Russian Federation in 2014, which compared relatively well, for example, with Brazil (0.40%) and Mexico (0.28%), although it is considerably behind the rates of 1.01% in China and 2.89% in the United States. It is important that these high-growth potential entrepreneurs in the Russian Federation are given the opportunities to achieve their ambitions.

Key policy recommendations on SME and entrepreneurship performance

- Increase numbers of SMEs and their employment through a combination of extensive measures aimed at increasing the level of entrepreneurship across the population and more targeted and specialised support for growth-oriented entrepreneurs and enterprises.
- Promote growth of manufacturing SMEs in particular by increasing the focus of SME programmes on innovation, exporting and investment in physical and human capital and setting targets for the participation of manufacturing SMEs in these programmes.
- Promote positive attitudes to entrepreneurship through a national entrepreneurship awareness campaign involving the media and comprehensive integration and teaching of entrepreneurship teaching across the educational system.
- Facilitate transfers of entrepreneurial activity from the informal to the formal economy by removing undue obstacles to formal entrepreneurship in the tax and regulatory system and supporting informal entrepreneurs to upgrade their businesses and tap into new sources of demand.
- Increase SME innovation across all sectors by building the innovation and growth capacities of new and existing enterprises and their management teams.

Business environment

Changing macroeconomic conditions and resource export dependency

The Russian economy grew steadily from the mid-1990s to the mid-2000s. However, the global financial crisis of 2008-09 brought a recession, and obliged SMEs to deal with both a fall in market demand and a tightening of financial liquidity. The government stepped in with important measures to channel finance to SMEs, which helped SMEs to survive the crisis. Economic growth recommenced after the crisis but at below the previous levels. Recently, macro-economic conditions for SMEs and entrepreneurship have worsened. This is linked to the imposition of sanctions by the Russian Federation and by some of its partners, which is affecting trade involving several countries and sectors and the ability of banks to obtain financing, and lend on to SMEs. A drop in oil prices is also affecting government revenues and the scope for public investment. Inflation and interest rates have increased, the exchange rate has fallen and the prospect is of negative domestic economic growth in the short term. These trends require adjustments by SMEs, which in some cases face a difficult short-term horizon.

The Russian Federation also faces the challenge of diversifying its exports from high dependency on natural resources into other export sectors, particularly in manufacturing. Whereas the Russian Federation has been running a substantial positive balance of trade overall (USD +182 billion in 2013) its non-oil current account balance is substantially in the negative (USD -136 billion in 2013). SME and entrepreneurship activity will have an important role to play in meeting this challenge.

Gradual opening to international trade, investment and competition

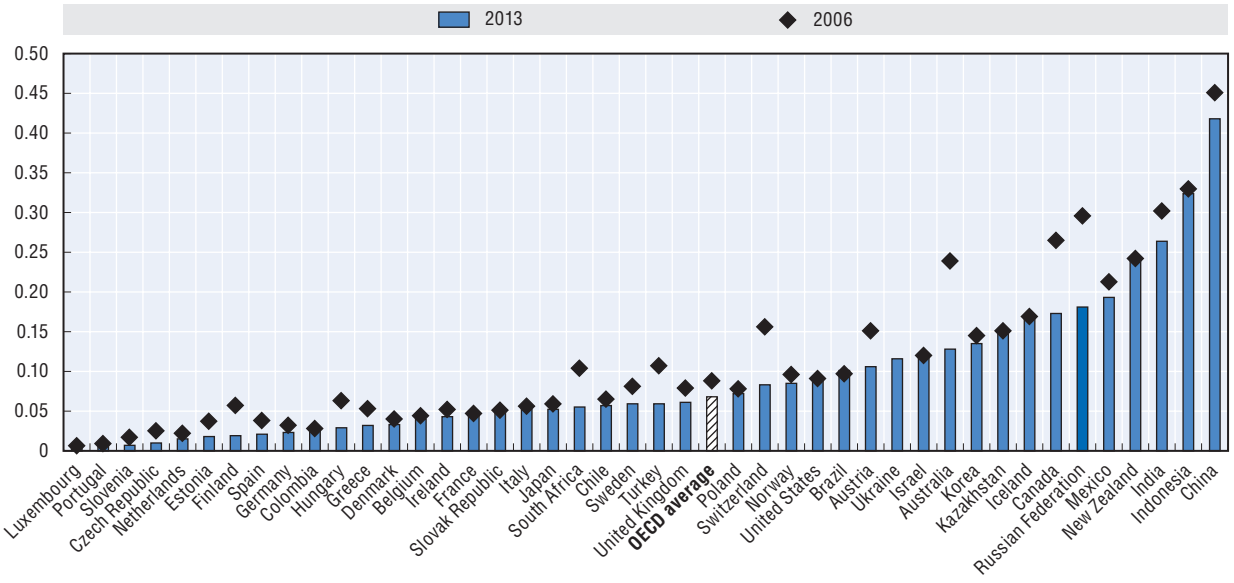
The Russian Federation is increasingly integrating into the international economy. In particular, membership of the World Trade Organisation (WTO) since 2012 has brought a programme of progressive reductions in tariff and non-tariff barriers and a Eurasia Economic Union, established in 2014, involves a customs union and increased economic integration with four neighbouring countries. Such internationalisation of markets can provide an important stimulus to SMEs and entrepreneurship by providing new export opportunities, on condition that Russian SMEs and entrepreneurs become more innovative, competitive and internationally-oriented.

The presence of inward foreign direct investment (FDI) ventures is a major vector for knowledge transfer to SMEs in many emerging and mature economies, helping to upgrade the technologies of local SME suppliers in particular. However, at 25% of GDP, the Russian Federation's stock of inward FDI is relatively low. This is connected to high regulatory barriers, which limit the accessibility of the Russian economy to foreign investors (Figure 1.6).

Barriers to product market entry

The state plays a strong direct role in the operation of the Russian Federation economy compared with OECD economies (Figure 1.7). There are large numbers of state-owned enterprises, which account for more than 80% of the sales, assets and market values of the top ten firms of the Russian Federation, for example, and occupy the dominant position in sectors such as banking, transport and energy. There is also significant use of price controls and subsidies in key sectors. This strong state involvement can limit the scope for private firms to enter the market, although there is an extensive privatisation process underway covering both large and small state operations.

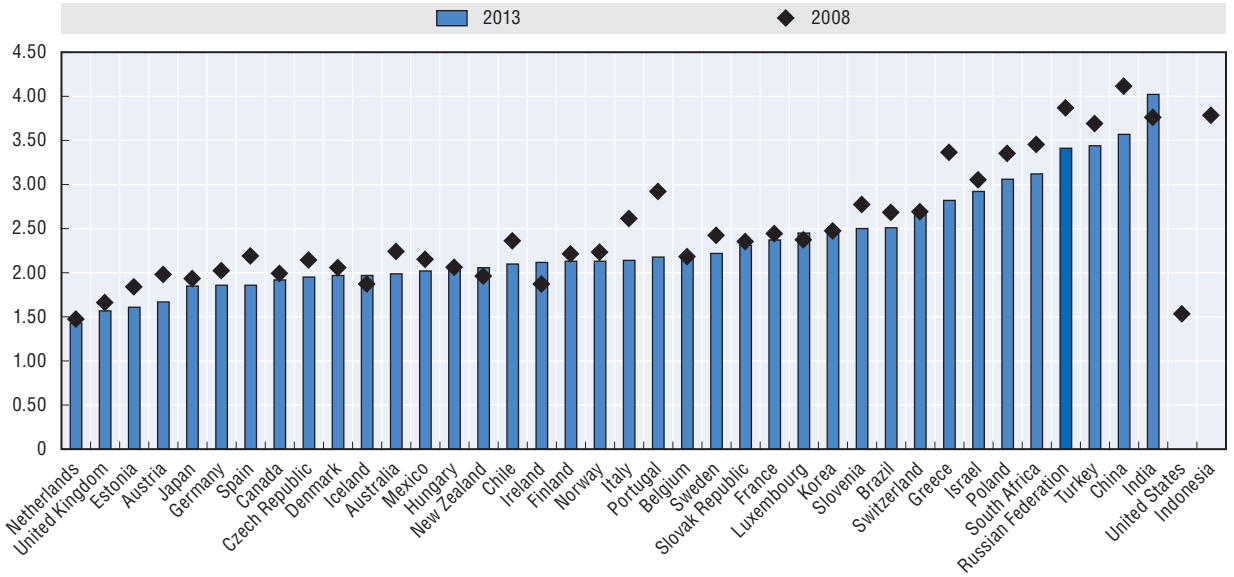
Figure 1.6. **FDI Regulatory Restrictiveness Index**
2006 and 2013, index scale 0-1 from least to most restrictive



Source: OECD, FDI Regulatory Restrictiveness database *http://stats.oecd.org/Index.aspx?datasetcode=FDIINDEX*.

StatLink *http://dx.doi.org/10.1787/888933271808*

Figure 1.7. **Product market regulation indicator: state control**
2013 and 2008, index scale from 0 to 6 from least to most restrictive



Note: The indicator covers state control in the economy in two areas: public ownership (scope of state-owned enterprises, government involvement in network sectors, direct control over enterprises, governance of state-owned enterprises) and involvement in business operations (price controls, command and control regulation).

Source: OECD Product Market Regulation database *http://dx.doi.org/10.1787/pmr-data-en*.

StatLink *http://dx.doi.org/10.1787/888933271810*

SME market entry and the growth opportunities of private firms are also negatively affected by significant levels of monopoly power and anti-competitive practices by incumbent firms. In response, the government approved a new Competition Road Map in 2013, which is expected to bring improvements in the areas of cartels, mergers, structural separation in regulated industries, market regulation, and intellectual property rights.

Targets for public procurement from SMEs

The federal government passed legislation in 2013 setting the target that at least 15% of state procurement orders by value should be placed with SMEs. A range of associated measures are planned, such as splitting contracts aimed at the SME sector so that contract sizes are below a RUB 20 million threshold, restricting the security to be required from suppliers to 2% of the initial price, and requiring procuring ministries and agencies to provide reports on their SME procurement activity. These measures may be important in stimulating SMEs if fully implemented.

Reductions in regulatory burdens

The government has made substantial progress during the last five years in reducing the burden of business regulation. This includes streamlining procedures and introducing time limits for processing property registration applications, a new electronic court case filing system, a reduction in the number of tax payments per year, simplified compliance procedures for value added tax, and accelerated liquidation procedures upon bankruptcy. As a result, the Russian Federation's ranking on the World Bank's overall Ease of Doing Business Index improved from 120th of 189 countries in 2009 to 92nd in 2014. Furthermore, the average number of days required to fulfil the administrative procedures required to start a business has dropped markedly, from 43 in 2004 to 18 in 2013, due, for example, to the introduction of one-stop shops for business registration in pilot regions and abolition of the requirement to have the bank signature card authorised before opening a company bank account.

To build on this progress, the government has announced the target of reaching a top twenty Doing Business ranking by 2018 underpinned by an "Improvement of the Business Climate" initiative, which has introduced a series of roadmaps covering different areas of administration. Improvements can also be expected from the recent introduction of a regulatory impact assessment (RIA) procedure. The success of these initiatives will depend on the extent and quality of their implementation on the ground. Furthermore, given a relatively high level of connection of Russian SMEs to the Internet, there is an important opportunity to facilitate administrative compliance for SMEs by making greater use of business-related e-services, such as online registration, on-line tax declarations and on-line reporting.

High business taxes

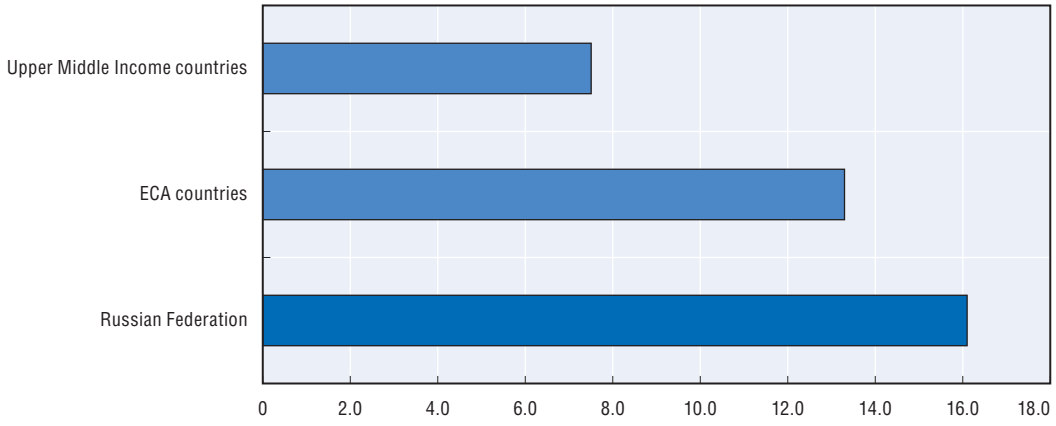
The headline corporate income tax rate was pegged back from 24% to 20% in 2010 and the total corporate tax rate as a percentage of business profits fell from 60.0% to 50.7% between 2006 and 2014. Nevertheless, the combined effect of corporate taxation and social security payments is still a significant barrier to business operation in the Russian Federation. More than one-third of SME owners and managers identified tax rates as a major obstacle to business in the World Bank's 2012 Enterprise Survey, twice as many as in Eastern European and Central Asian (ECA) countries as a whole.

Transparency and rule of law

The Russian Federation scored only 28 out of 100 on Transparency International's Perceptions of Freedom from Corruption Index in 2013; a marginal improvement on 2008, but a significantly poorer performance than OECD countries and other major emerging economies such as Brazil and China. Similarly, 16% of Russian Federation firms report needing to make payments in their interactions with public officials; a greater proportion than in ECA and Upper Middle Income countries (Figure 1.8). Corruption appears to be a significant constraint to business operation, particularly in the case of innovative enterprises, and is also likely to push firms towards the informal economy. In response the government brought in an Anti-Corruption Plan in 2012 and a new law on public procurement in 2013.

Figure 1.8. **The composite Graft Index**

Percentage of interactions between firms and public officials in which a bribe was expected



Source: World Bank/IFC Enterprise Surveys: Russian Federation Country Profile 2012.

StatLink http://dx.doi.org/10.1787/888933271870

Furthermore, the Russian Federation ranked only 80th out of 99 countries on the World Justice Project Rule of Law Index in 2014, which uses indicators such as government ability to expropriate business assets, the fundamental rights of citizens and the independence of courts (Table 1.2). Some reforms have nevertheless been introduced, including increases in the pay and training of judges and the creation of a Federal Business Ombudsman to investigate cases of injustice to business.

Table 1.2. **Rankings on the World Justice Project Rule of Law Index, 2014**

Thematic area	Russian Federation	Eastern Europe and Central Asia average
Constraints on government powers	89	75
Absence of corruption	66	63
Open government	67	60
Fundamental rights	79	62
Order and security	75	42
Regulatory enforcement	67	58
Civil justice	68	55
Criminal justice	76	61
Global ranking	80	60

Note: Countries are ranked from 1 (strongest) to 99 (weakest)

Source: World Justice Project (2014) The World Justice Project Rule of Law Index 2014, World Justice Project, Washington DC.

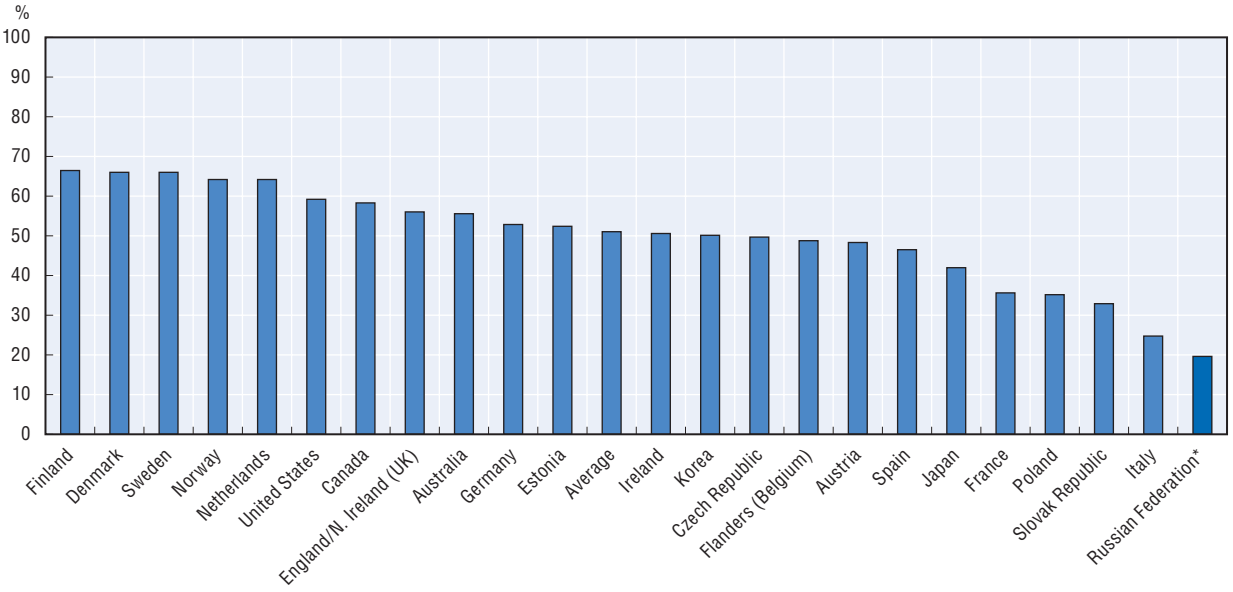
StatLink http://dx.doi.org/10.1787/888933272292

Flexible labour market, needing a boost to skills

At above 70% of the adult civilian population, the Russian Federation's employment rate is high, while its unemployment rate is low, at only 5.5%. This is largely the result of a flexible labour market in which hiring-and-firing costs are low, labour turnover rates are high, and employers can rapidly adjust working hours and make use of non-standard labour contracts. On the other hand, SMEs in the Russian Federation lack skilled labour. This is not a problem of a low entry rate into higher education, which is higher than the OECD average, but rather concerns the type of tertiary education offered, which tends to be more theoretical than practical, and a low rate of participation in vocational education and training. For example, in 2012, only 20% of Russian 25-64 year olds participated in formal or non-formal adult learning, well below typical rates for OECD countries (Figure 1.9). Furthermore, entrepreneurship education is not yet of sufficient scale to reach all young people in formal education.

Figure 1.9. **Participation in adult learning**

2012



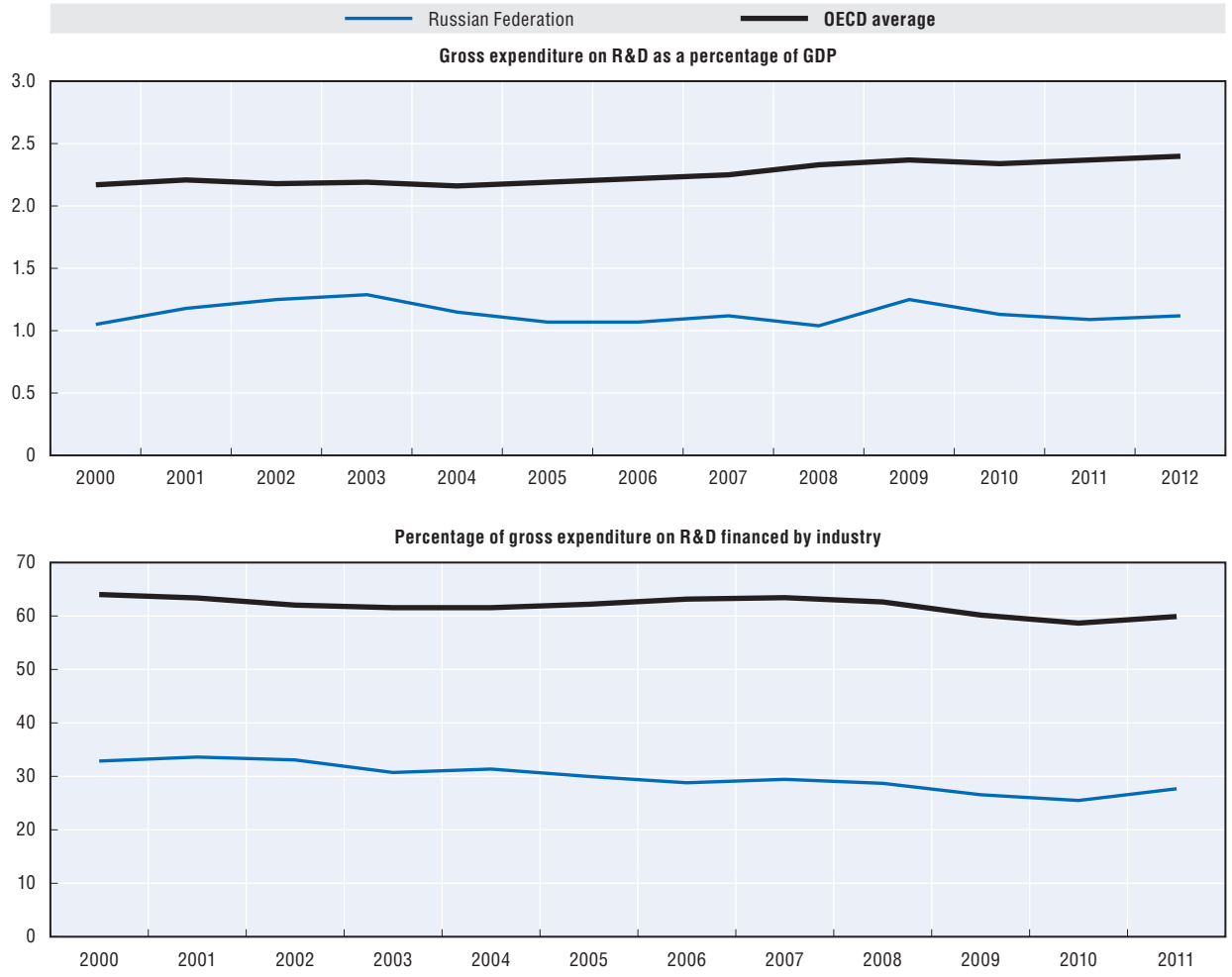
Note: The sample for the Russian Federation does not include the population of the Moscow municipal area.

Source: OECD (2014), Education at a Glance 2014, Chart C6.1, available at *http://dx.doi.org/10.1787/888933119207*.

Insufficient commercialisation in the innovation system

The Russian Federation has a long-standing tradition of excellence in a number of science and technology sectors and performs well by international standards on a few key innovation measures such as the proportion of the population with higher degrees. However, investment in innovation is quite low. As shown in Figure 1.10, gross domestic expenditure on R&D stood at 1.1% of GDP in 2012 compared to an OECD average of 2.4% and private sector expenditure represented only 27.7% of the total R&D spend, well below the OECD average of 59.9%. Furthermore, a study by OPORA Russia showed that less than 4% of Russian public sector scientists and researchers had successful experience of commercialisation.

Figure 1.10. **R&D expenditure in the Russian Federation**



Source: OECD Main Science and Technology Indicators *https://stats.oecd.org/Index.aspx?DataSetCode=MSTI_PUB.*

StatLink *http://dx.doi.org/10.1787/888933271951*

Weak aggregate financial markets

The Russian financial sector is under-developed as a source of loans and other financial products for SMEs and start-ups. Both the volume of domestic credit provided by the banking sector and the volume of domestic credit to the private sector represent a much smaller share of GDP in the Russian Federation than in OECD and Euro area countries and also lags behind ECA countries. Furthermore, despite a substantial reduction in the overall spread between bank lending interest rates in the Russian Federation since 2003, the interest rate spread is still high relative to key comparator countries. Issues hindering the growth of credit in the economy include limited legal rights of investors and lack of openness of the banking sector to new players.

Key policy recommendations for the business environment and framework conditions

- Continue to reduce the regulatory barriers and stimulate the attraction of inward FDI in order to reinforce its role in upgrading SME technologies and expanding their markets.
- Build technical capacities in competition policy assessment within the competition authority by providing analytical guidance and training for officials and establish a system for monitoring the uptake of recent product market competition reforms.
- Pursue plans to privatise SOEs and reduce state subsidies and price controls; all of which would help to create a more benign environment for SME and entrepreneurship development.
- Bolster SME procurement policy by initiating targeted information and training programmes to increase the ability of SMEs successfully to compete for public procurement contracts. Ensure that recent commitments to improving public procurement from SMEs are fully implemented and monitored.
- Further reduce regulatory burdens on SMEs and entrepreneurs by legislative reforms in lagging policy areas such as construction permits and trading across borders, training public officials in dealing with businesses, increasing the use of e-government services for businesses (e.g. on-line business registration, tax declarations and reporting), extending RIA procedures to cover existing government laws and regulations as well as new ones and creating a body to enforce RIA procedures across government and to ensure that RIA results are translated into changes in policy.
- Maintain the emphasis on rolling back corruption in the dealings of public officials with SMEs and entrepreneurs, paying attention to implementation and enforcement of existing regulation and introducing further legislation to tackle remaining gaps. Provide logistical and operational support to the Federal Business Ombudsman.
- Strengthen judicial independence through greater transparency in appointment and promotion processes, better pay and rotation of judges, and providing better protection against outside interference in court cases.
- Boost subsidies for continuous training and workforce development in SMEs, improve the quality of training in vocational education colleges and increase apprenticeships and student placements in SMEs.
- Expand and consolidate the promotion of entrepreneurial skills and competencies in formal education by introducing national incentives and support structures (such as resource banks of pedagogical materials) for entrepreneurship education and graduate business start-up support (e.g. student entrepreneur clubs and incubators) in universities, introducing entrepreneurship as a specific competence in the formal curriculum at elementary and secondary levels and developing a methodological base and training programme for school teachers in entrepreneurship education.
- Increase the emphasis of public innovation investments on the market commercialisation of research, especially in relation to individual entrepreneurs and SMEs, improve the intellectual property rights system with regard to the clarity of the law and its enforcement and take active steps to promote research, innovation and training co-operation between universities and SMEs.
- Increase legal protection for external investors in businesses and promote liberalisation and competition in the supply of finance for business.

Policy strategy and delivery arrangements

Clear basic policy framework, lacking a cohesive medium-term strategy document

The 2007 federal SME Act establishes a clear and stable legal framework for SME and entrepreneurship policy in the Russian Federation, outlining the objectives, principles, mechanisms, key actions and key actors of SME and entrepreneurship policy. Leadership is offered by the Federal Ministry of Economic Development, which uses the offer of federal funding to influence SME and entrepreneurship actions by regional and municipal

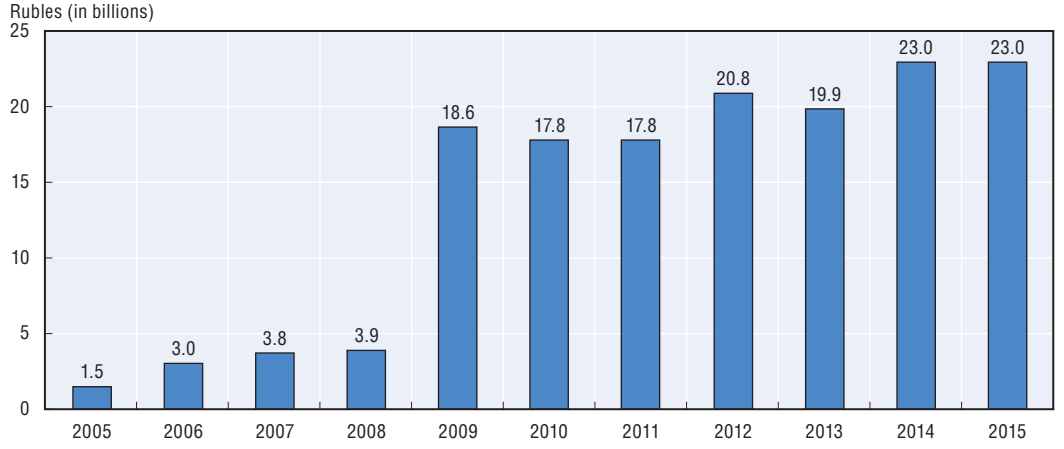
governments and co-ordinates federal ministries and agencies by chairing a cross-government working party. The State Commission for Competition and Development of SMEs and the State Duma Committee on Economic Policy, Innovation and Entrepreneurship Development provide additional policy impetus, and strong connections have been built between the government and business sector to assist in policy formulation.

However, unlike many other countries, there is no formal, comprehensive, SME and entrepreneurship strategic master plan in the Russian Federation. The role that such a document normally plays is to set out a medium-term vision for policy actions to all the relevant stakeholders, formalise collaborations, prioritise actions, set targets for activities, and set up arrangements for the monitoring and evaluation of policy impacts.

Increased federal programme spending

The federal government has substantially increased the volume of resources directed to its main SME support programme, with the funding commitment increasing from RUB 1.5 billion in 2005 to RUB 23 billion in 2015 (Figure 1.11). Other ministries and agencies also make significant spending. However, the total federal budget for SME and entrepreneurship policy in the Russian Federation still appears to be far below that of countries such as Mexico, Poland and Thailand as a share of GDP.

Figure 1.11. **Federal budget funds allocated to the SME programme, 2005-15**



Note: Expenditures for 2014 and 2015 are estimates.

Source: Russian Federation Ministry of Economic Development.

StatLink http://dx.doi.org/10.1787/888933271990

Strong focus on general subsidies

More than half of federal SME support programme expenditure is in the form of grants and loans for start-ups and SMEs in general (Table 1.3). While grants and loans are important for increasing the numbers of start-ups in the Russian Federation there is relatively little expenditure on complementary training, advice and information provision. Furthermore, general subsidies for existing SMEs, particularly the support for plant and equipment, are not likely to be the most effective tool for increasing the productivity and output of existing SMEs. These general subsidies are likely to be affected by high levels of non-additionality and include support for substantial numbers of retailing and wholesaling businesses with low economic development impacts. Important interventions that could be boosted from some reallocation of resources from general subsidies for existing SMEs are the creation of

a business development services infrastructure to provide business diagnosis, consultancy, incubation facilities, technical assistance, seed finance, and so on to potential innovative and exporting SMEs and training subsidies for SME workforce development.

Table 1.3. **Allocation of federal funds for the SME Support Programme in 2011-12**

No.	Measure	2011		2012	
		Funds allocated, RUB billions	Percentage of funding	Funds allocated, RUB billions	Percentage of funding
A.	***Subventions to regions for the state support of small and medium enterprises***	***16.0***	***89.7***	***18.57***	***92.3***
1.	Promotion of entrepreneurship and subsidies for business start-ups	2.04	11.4	1.86	9.2
2.	Assistance to the development of young people's enterprises	0.41	2.3	0.65	3.2
3.	Support of small innovative companies	2.48	13.9	1.95	9.7
4.	Support for leasing and purchase of modern production equipment and facilities	1.90	10.7	4.5	22.4
5.	Support of export-oriented SMEs	0.26	1.5	0.39	1.9
6.	Microfinance development	2.06	11.6	2.06	10.2
7.	Development of loan guarantee funds	3.42	19.2	3.31	16.4
8.	Support for municipal programmes	1.72	9.6	1.87	9.3
9.	Diversification of mono-industry cities	0.55	3.1	0.54	2.7
10.	Other	1.16	6.5	1.44	7.2
B.	***Creation and development of business support infrastructure***	***1.83***	***10.3***	***1.56***	***7.7%***
	Total	***17.83***	***100.0%***	***20.13***	***100.0%***

Note: "Other" is not specified in the information supplied but includes support for activities to promote entrepreneurship and to develop a system of personnel training, retraining and advance training for the small business sector (training vouchers, compensation for training/ retraining costs, and organisation of training events).

Source: Russian Federation Ministry of Economic Development.

StatLink http://dx.doi.org/10.1787/888933272304

Comprehensive information on public costs per job created is not available across the full portfolio of SME programme components, underlining the need for better programme evaluation. However, across the three programme components for which data are available (support of municipal programmes, support of small innovative companies and support for leasing development and production modernisation), cost effectiveness per job created was estimated to be the lowest for leasing and production modernisation support.

Key policy recommendations on the strategic framework and delivery arrangements for policy

- Develop an integrated, standalone, medium-term, strategic master plan for SME and entrepreneurship policy through an inter-government and public-private consultative mechanism. The strategy should outline the vision, goals, targets, and main policy thrusts of government policy actions that will guide and co-ordinate all the relevant federal, regional and municipal ministries and agencies.
- With the master plan as the foundation, implement a mechanism for developing annual SME and entrepreneurship promotion work plans that integrate the actions of the relevant federal ministries and agencies. These work plans should show how the different actions will support SMEs and entrepreneurs at different stages of their development (e.g. nascent, start-up, growth, restructuring) and distinguish the support that is to be specifically targeted to manufacturing, innovative, exporting and high-growth entrepreneurship.

Key policy recommendations on the strategic framework and delivery arrangements for policy *(cont.)*

- Implement a formal system of independent SME and entrepreneurship policy evaluation. The system should define the primary and secondary objectives of each action and introduce robust evaluation methodologies, including control group studies, of the outputs, outcomes and impacts of the action as compared with the objectives. Utilising standard policy cycle models, it should also include arrangements for making use of the evaluation results to design more effective programmes and institutional delivery mechanisms.
- Reduce expenditure on automatic property and equipment grants to wide categories of existing SMEs and use the resources released for subsidies that are more targeted to investment in innovating, exporting, manufacturing, and high growth potential SMEs and start-ups, for expanded business diagnosis, advice, mentoring and consultancy services and for SME workforce training activities.

Federal SME and entrepreneurship programmes

Widespread business start-up grants

Large numbers of unemployed people benefit from small grants for business start-up via the Grants for Budding Entrepreneurs Programme of the Ministry of Economic Development and the Self-Employment Support Programme of the Ministry of Labour and Social Protection. These are important tools for promoting entrepreneurship across the population, but suffer from high deadweight and high proportions of business start-ups with low turnovers and poor long term sustainability prospects. This is connected to the facts that the grants are not selective and not accompanied by advice and coaching. Furthermore, the schemes are managed separately, so that scope for synergies and removal of duplication is unexploited, while the administration procedures for the Self Employment Support Programme are relatively complex.

SME innovation programmes focused on grants and technology-based enterprises

SME innovation is the target of significant programme support in the Russian Federation, which is mainly in the form of grants for product or process development in technology-based SMEs. While these grants are very important, there are a number of weaknesses in the overall programme approach to SME innovation. First, support for non-technological innovation is very limited; it is difficult for SMEs that are not in high technology sectors to receive innovation assistance and for SMEs to obtain support for projects that are not focused on technological change (marketing, business model improvement etc.). Second, innovation grants are awarded to broad categories of firms in innovative sectors rather than targeted to firms that are diagnosed as having a need for the subsidies. Furthermore, the financial support is not packaged together with a set of consultancy and workforce training that could assist the firms to make more fundamental strategic changes to extend and exploit their innovation. Third, there is limited use of tax incentives for investors who invest in the equity of innovative SMEs directly or through equity funds, or of initiatives to stimulate knowledge transfers from universities to SMEs despite demonstrated success of these instruments in stimulating SME innovation in other countries.

Gaps in programmes for future entrepreneurs, high-growth SMEs and supplier development

A number of existing programmes seek to build awareness and skills for entrepreneurship among youth, including entrepreneurship education courses, business plan competitions, and short entrepreneurship training courses. However, the proportion of young people served is relatively low. Furthermore, there is little support to encourage adults into entrepreneurship. Despite some local campaigns, there is no national entrepreneurship awareness programme and opportunities for adults to access basic entrepreneurship training are limited.

High-growth potential start-ups and SMEs are a key target of policy in many countries because of their disproportionate impact on employment generation. Such programmes examine the key characteristics of companies and interviews with management to identify potential growers and offer them more intensive support than that offered to standard start-ups and SMEs. There is currently no federal programme of this kind in the Russian Federation. Similarly, there is no federal programme dedicated to creating supply chain linkages between domestic SMEs and inward FDI operations, despite their strong potential for improving the international market access and technologies of SMEs.

Lack of scale and quality in the business development services infrastructure

Despite recent public investments, the numbers of technology parks, business incubators, centres for entrepreneurship support, innovation centres, export centres and other key business development services facilities is limited in the Russian Federation. For example, there were only 104 state-supported business incubators in 2012, hosting 1 600 SMEs, which represents an incubator density per head of population approximately five times less than that of the USA. Similarly, there were only 34 Export Support Centres in the Russian Federation (although there are 83 regions), and only seven state-supported technology parks were developed between 2007 and 2011. The numbers of consultants, mentors, trainers and coaches are also very small compared with the needs.

The existing business development services organisations vary widely in quality and there is a general need for upgrading in their operating practices. Business support staff and consultants often lack strong competences in SME and entrepreneurship support and management often lacks an entrepreneurial attitude. In addition, the use of competitive funding awards makes it difficult for the business development organisations to achieve continuity and coherence of service provision and to build up 'learning by doing'.

The business incubator facilities in particular would benefit from upgrading. In terms of services, many of the business incubators concentrate on providing physical space for incubating enterprises together with subsidised rents and access to state loans and loan guarantees. It is rare for the incubators to include advice and consultancy and pre-incubation support to entrepreneurs and SMEs, although these are staples for incubators in other countries. On the other hand, the functions of 'standard' and 'innovative' business incubators have been clearly specified and incubators are required to conduct annual performance appraisals. This helps to maintain some basic standards of provision and quality across the business incubator system.

Key policy recommendations on federal SME and entrepreneurship programmes

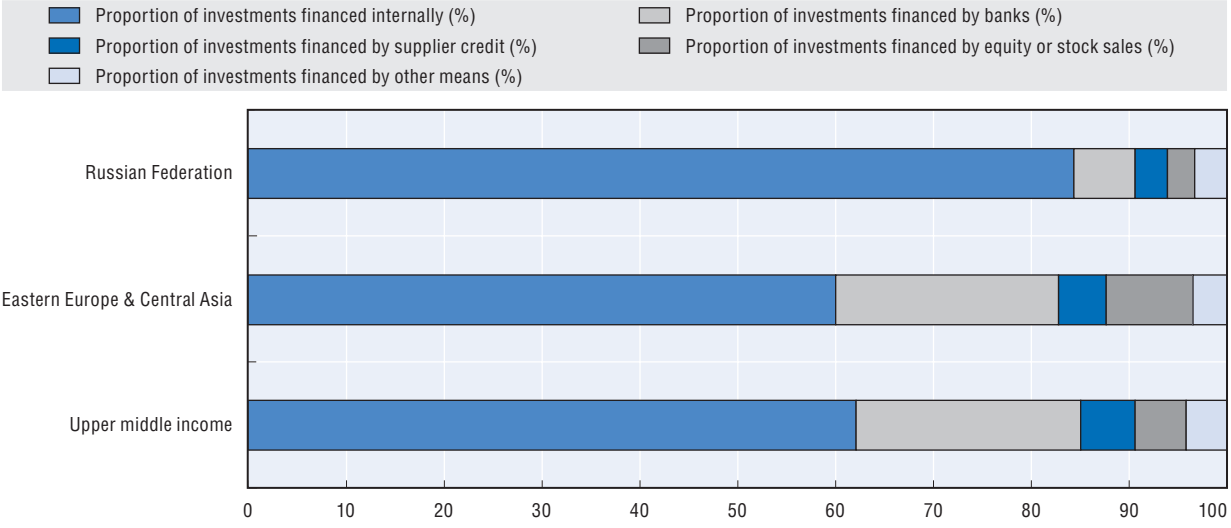
- Adjust the business start-up grant programmes for the unemployed by targeting financial awards towards sustainable business proposals, simplifying administration for accessing the programmes, offering additional business diagnosis and advice services to greater proportions of entrepreneurs supported with grants and improving co-ordination and synergies between different start-up programmes.
- Broaden SME innovation support to include non-technological companies and non-technological innovation projects, tie a proportion of the subsidy awards to a diagnosis of the enterprise development needs of potential innovator SMEs, and combine financial awards with advice, coaching, consultancy and workforce training to help deliver agreed company action plans. Consider the introduction of highly targeted tax incentives for investment in innovation in innovative SMEs.
- Build the pipeline of future entrepreneurs by launching a national entrepreneurship promotion campaign to give positive images of entrepreneurship through the media and other channels.
- Introduce a standard, subsidised basic national entrepreneurship training course for adults and youth with the intention to start a business, which could be a virtual training course delivered through the internet or could be provided through physical workshops.
- Introduce a high-growth entrepreneurship programme to identify high-potential SMEs and entrepreneurs, diagnose their business and personal development needs, and offer them tailored packages of coaching, mentoring, consultancy, technology development, management training, network building and access to seed and venture capital.
- Introduce a supplier development programme to build linkages between SMEs and inward FDI operations. The programme should identify potential FDI anchor firms and SME suppliers, diagnose how the SMEs could reduce their costs, increase their quality and reduce their delivery times in order to gain contracts with the anchor firms, and offer the necessary training, consultancy and financing support to the SMEs in order to meet their supply standards. The FDI anchor companies themselves could be engaged in providing expertise and funding to the initiative.
- Expand the numbers and quality of business development services centres (incubators, entrepreneurship centres, export support centres, etc.). This should include assessing gaps in the presence of different types support across the country to inform public investment decisions. Incentives and opportunities should also be provided for public, private and non-profit organisations to create and run facilities, with part of the public funding based on results achieved. In addition, training and certification should be provided for business development service centre managers, staff and consultants, networks created for peer learning and cross-referrals of clients and more stable core funding supplied.
- Create a national system of first-stop shop business information and advisory centres based on an integrated national platform and brand. The first-stop shop would provide basic information and advice on business start-up and development directly to entrepreneurs and make referrals to other public, private and non-profit business service providers for more detailed information and advice.
- Upgrade the business incubator network by introducing more soft services (advice, mentoring, consultancy etc.) for enterprises at incubation and pre-incubation stages, creating a national incubator co-ordination and management unit responsible for preparing standard operating guidelines and performance monitoring of incubators, promoting mutual learning networks for incubator managers, and introducing professional development programmes for incubator managers and staff, with a particular emphasis on creating an adequate supply of qualified consultants for business diagnosis and advice through recruitment and training.

Financing SMEs and entrepreneurship

Major gap in bank lending to SMEs and entrepreneurs

Limited availability of bank loans to SMEs and start-ups in the Russian Federation has led to a strong reliance of SMEs on internal sources of finance, both for investment (Figure 1.12) and for working capital. Although there has been some mitigation of the problem through the development of a relatively large private and public micro finance sector and the use of basic government financial subsidies for SMEs and entrepreneurs, such as leasing subsidies, to address financial weaknesses, these are not effective long term solutions and cannot take the place of large and better quality bank lending. The World Bank Enterprise Survey indicated that only 22% of surveyed enterprises in the Russian Federation had access to a bank loan in 2012, substantially below the averages of 43% and 46% respectively for ECA and Upper Middle Income countries. At the same time, SME loan turn down rates, real interest rates and collateral demands are high and no more than 10% of bank loans are for more than 3 years. SMEs report that the difficulties in obtaining bank finance are damaging their ability to grow and manage their operations. Lack of loans is also likely to block the creation of new growth-oriented enterprises.

Figure 1.12. **Sources of financing for investment by enterprises**



Source: World Bank/IFC (2012) Enterprise Surveys: Russian Federation Country Profile 2012. Washington DC World Bank Group.

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The supply of bank lending to SMEs is nevertheless on the increase. The stock of SME loans increased from RUB 2 500 billion to RUB 5 200 billion between 2008 and 2013, and the share of SME loans in total business loans grew from 19% to 23%. The government has been a key player in these positive developments. In particular, it offered lines of credit to 134 partner banks in 2014 to enable them to expand their SME lending balance sheets via the public development bank, Vnesheconombank (VEB) and its subsidiary, SME Bank. SME Bank is one of the few active contributors to long term SME loans of more than 3 years, which accounted for 62% of the bank loans issued using SME Bank lines of finance.

Extensive micro finance

There is a large and growing micro finance sector in the Russian Federation, with approximately 3 750 providers managing a portfolio of approximately RUB 35 billion.

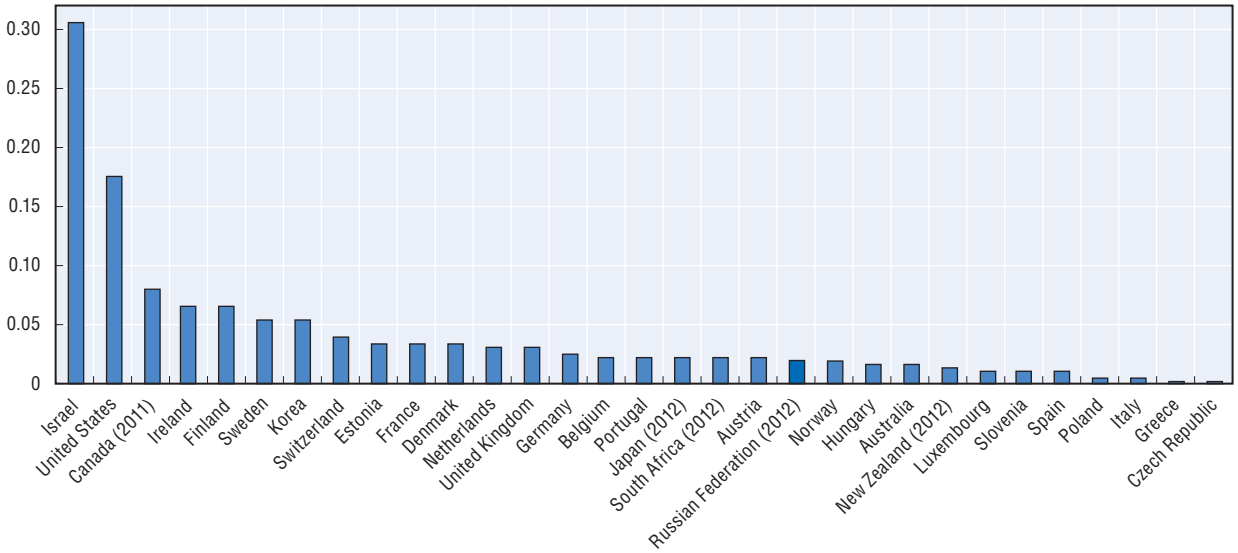
Approximately 70% of them lend to SMEs. VEB provides support to 141 non-bank organisations for a range of microfinance products, and many others are supported through federal SME support programme funding. Others are entirely private. They are predominantly small institutions, often with weak governance in terms of reporting standards and tools to assess the risk of potential borrowers, and tend to lack scale economies and portfolio spread. They tend to offer relatively small loan amounts at higher interest rates than the banking sector. In this respect, they play an important role in the financing of new and smaller SMEs, compensating to some extent for weaknesses in the banking system, but are not addressing the gap for larger scale, longer term SME lending at lower interest rates. Furthermore, borrowers often find it difficult to distinguish between very high cost pay day lenders and microfinance lenders with more reasonable interest rates.

Significant equity capital supply

The supply of venture capital is significant in the Russian Federation, and while the volume of venture capital investment is lower as a proportion of GDP than in several leading countries such as Israel, the United States and Canada (Figure 1.13), this appears to be as much a reflection of constrained demand from limited numbers of high-growth firms as it is to barriers in venture capital supply. Furthermore, the trend in supply of early stage venture capital investment in the Russian Federation is very positive, increasing from approximately USD 108 million in 2007 to USD 398 million in 2012. On the other hand, individual venture capital fund sizes are relatively small, with large investments, and investments in successfully-growing firms requiring syndication. In addition, business angel financing is still limited, reflecting a lack of a business angel tradition in the Russian Federation as well as issues about lack of legal protection for minority investors.

Figure 1.13. **Private equity and venture capital investments as a proportion of GDP**

Flows, percentage of GDP



Note: Includes later stage investments as well as seed and early stage investments.

Source: OECD (2014), Venture capital investments as a percentage of GDP: Percentage, 2013, in Entrepreneurship at a Glance 2014, OECD Publishing, Paris. DOI: *http://dx.doi.org/10.1787/entrepreneur_aag-2014-graph88-en*.

StatLink http://dx.doi.org/10.1787/888933272054

State loan guarantees are increasing substantially

The strong potential of state credit guarantees for stimulating SME lending by banks and microfinance institutions is increasingly recognised, reflecting in particular the greater leverage of public sector resources that can be achieved in this way compared with traditional subsidies, direct lending or lines of credit to partner banks. The initial stimulus came from the creation of regional and municipal credit guarantee funds in 2006, leading to the increase shown in Table 1.4 from guarantee volumes of RUB 39 billion in 2009 to RUB 249 billion in 2013.

Table 1.4. **SME loan guarantees in the Russian Federation, 2009-13**

Indicators	Units	2009	2010	2011	2012	2013
Government loan guarantees, SMEs	RUB million	18 226	32 460	58 954	87 400	116 900
Government guaranteed loans, SMEs	RUB million	38 917	66 824	122 747	185 000	249 000

Source: OECD Financing SMEs and Entrepreneurs 2015: an OECD Scoreboard.

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This system has been effective in boosting SME lending, but some of the regional operations lack scale efficiencies and the quality of practices varies widely with respect to screening of potential borrower firms to ensure the additionality of state involvement in the loans. More recently, a Federal Credit Guarantee Agency was established in 2014 with a registered capital of some RUB 37 billion, and aiming to provide RUB 170 billion of additional guarantees by 2016, as well as provide support to improving operating practices across the regional and municipal credit guarantee fund network.

Credit information

One of the underlying problems holding back lending to SMEs and entrepreneurs is a shortage of information to help banks and microfinance institutions to assess SME credit risk. The tax system does not ensure transparency in the financial statements of SMEs while there is little central collection of credit history information on SME clients or sharing of SME credit history information across financial institutions. At the same time, banks and microfinance institutions have not introduced standardised procedures for making individual SME credit adjudications, reflecting the lack of credit scoring information and limited SME lending tradition.

Key role of Vnesheconombank and SME Bank

The public development bank, Vnesheconombank (VEB), and its SME Bank subsidiary, play a critical role in improving access to finance for SMEs and entrepreneurs through the funding they provide to partner banks and micro-finance institutions. However, the range of financial and non-financial products and services they provide is more limited than public financial institutions in many other countries. In particular, VEB and SME Bank have only limited involvement in equity, hybrid debt-equity and securitisation instruments and have relatively few activities aimed at strengthening the operating practices of players in the SME and entrepreneurship finance market, such as offering financial education to entrepreneurs and lenders, exchanging information among financial institutions on best practices in SME and entrepreneurship financing, and promoting the use of credit scoring information and tools. The full scope to build on the existing infrastructures, skills, networks and services of VEB and SME Bank is not yet being fully exploited for strengthening the financial system for SMEs and entrepreneurs in the Russian Federation.

Key policy recommendations on SME and entrepreneurship financing

- Expand bank lending to SMEs and entrepreneurs and increase the scale and terms of loans made by increasing the leverage of public investments (favouring loan guarantees over direct subsidies to SMEs or lines of credit to banks for onward lending), increasing credit history information in the SME lending market and building an inter-bank SME lending market by encouraging standardisation of loan contracts and implementing legislation to provide for securitisation.
- Promote the sustainability and additionality of the loan guarantee system by using evaluation evidence and information from international experience to set the appropriate design parameters for the national, regional and municipal credit guarantee funds as well as by providing capacity-building support to local funds and encouraging consolidation of smaller funds.
- Develop a national credit information system that enables banks, microfinance institutions and finance providers to assess the riskiness of SME borrowers based on their credit histories and other parameters. Require that all state-supported credit organisations contribute credit information to an intermediate credit information organisation and share the resulting database with private banks and financial institutions on a fee-paying basis.
- Fill outstanding gaps in the regional coverage of microfinance institutions, offer capacity-building support to microfinance institutions in SME lending and introduce new reporting and supervisory measures to help borrowers distinguish between payday lenders and responsible institutions.
- Channel public investments in venture capital towards expanding existing funds rather than creating new funds.
- Boost the business angel sector through measures such as strengthening legal protection for minority shareholders, recognising business angel investment in regulations, supporting the creation of business angel networks, offering tax incentives for angel investments, providing public co-financing for projects with angel investors and offering awareness, training and mentoring support in angel investment to potential angels and high growth enterprises.
- Augment the scale of the SME lending interventions of the public development bank, VEB and its SME Bank subsidiary in the short to medium-term, particularly in encouraging longer-term and larger loans to start-ups and growth-oriented SMEs.
- Expand the remit of the activities of VEB and SME Bank to enable them to introduce new financial products in the area of equity, hybrid debt-equity and securitisation instruments, and new non-financial products, including hosting a national institute for financial education (offering distance, online, and classroom-learning programmes to financial services professionals, such as those involved in banks, credit guarantee programmes, microfinance institutions and venture capital funds), and supporting the development of a national credit information system by advancing the availability of credit rating tools, technologies and data.
- Design all measures to improve the financing system for SMEs and entrepreneurship so as to avoid the possibility of systemic corruption.

The local dimension

Spatial variations in SME and entrepreneurship activity

SME and entrepreneurship performance is geographically uneven in the Russian Federation, marked by a high level of regional economic disparity. Whereas the density of SMEs per 10 000 population is above 200 in Saint Petersburg, Kaliningrad, Novosibirsk, Yaroslavl and Moscow, it is no more than 50 in Tyva, Zabaikalsk, Chechen, Kalmykia and Dagestan (Figure 1.14). In particular, rural areas tend to have lower SME densities and

start-up rates. In order to meet targets for the growth of the SME economy and for more balanced spatial development new business activity must be generated more widely across the regions and settlements of the Russian Federation.

Figure 1.14. **Regional variation in number of SMEs per 10 000 population, Russian Federation**
2012

Note: Figures are missing for the Republic of Ingushetia.
Source: Figures are calculated from Rosstat (2013), SMEs in Russia 2013.

StatLink http://dx.doi.org/10.1787/888933272099

Business environment conditions also vary geographically

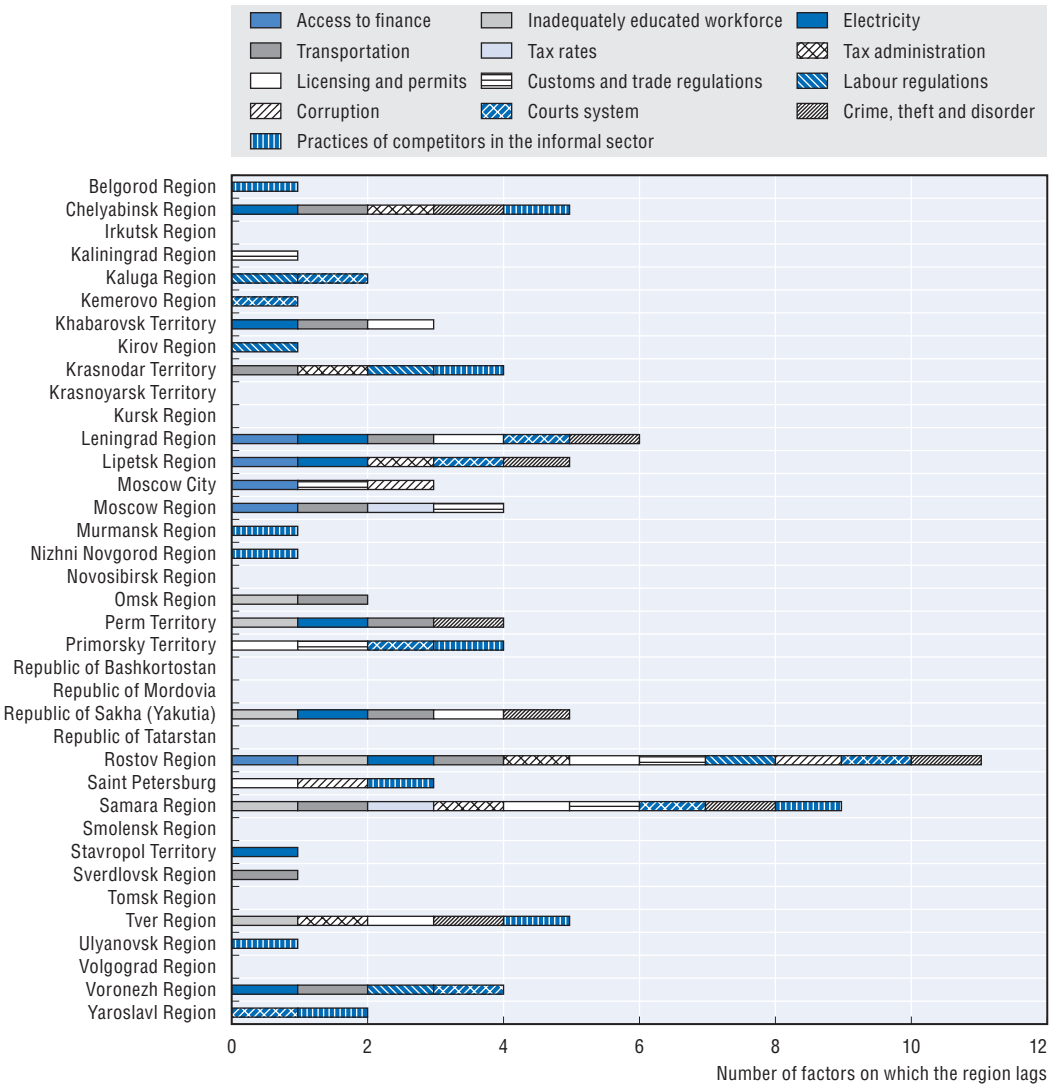
While there are some clear similarities across Russian Federation regions in what businesses perceive as the major constraints to business development – tax rates, access to a skilled workforce and access to finance – there are also some significant variations. Figure 1.15 shows, for 37 regions, the categories of business environment conditions for which the percentage of businesses reporting a major problem was at least 25% above the Russian Federation average. Certain regions lag behind on several business environment conditions, particularly Rostov, Samara, Leningrad, Chelyabinsk, Lipetz and Tver. The specific nature of the problems also varies.

Positive momentum in local regulatory improvements

Several regions and municipalities are actively engaged in improving their regulatory frameworks for business. Examples include the introduction of "single windows" for regional and local government interactions with business and help lines and appeals procedures for businesses regarding the actions of officials on regulations and inspections. Improvements are also being made in opening up local public procurement processes to SMEs and new firms and in creating a regional business ombudsman in each region. However, many of these advances are highly uneven across the Russian territory.

Figure 1.15. **Regions lagging behind in framework conditions, selected regions, Russian Federation**

2012



Note: Regions are classified as lagging behind where the percentage of firms identifying the specific framework condition as a major problem is more than 25% above the national average.

Source: Calculated from World Bank Enterprise Surveys, Russia 2012 *http://www.enterprisesurveys.org/data/exploreeconomies/2012/russia*.

StatLink http://dx.doi.org/10.1787/888933272188

Mechanisms to spread and adapt SME and entrepreneurship actions in the regions

Federal government ministries and agencies have adapted certain of their programmes to local conditions. For example, there is a federal innovative clusters programme that supports local industry clusters with strong growth potential in various regions. In addition, VEB, the public development bank, has established framework agreements with fifty regional governments in order to implement tailored actions to improve SME access

to finance in each selected region reflecting the nature of the finance gap experienced and the existing partners available to work with. However, the number of direct federal interventions that include locally differentiated actions such as these could usefully be expanded to help increase their effectiveness.

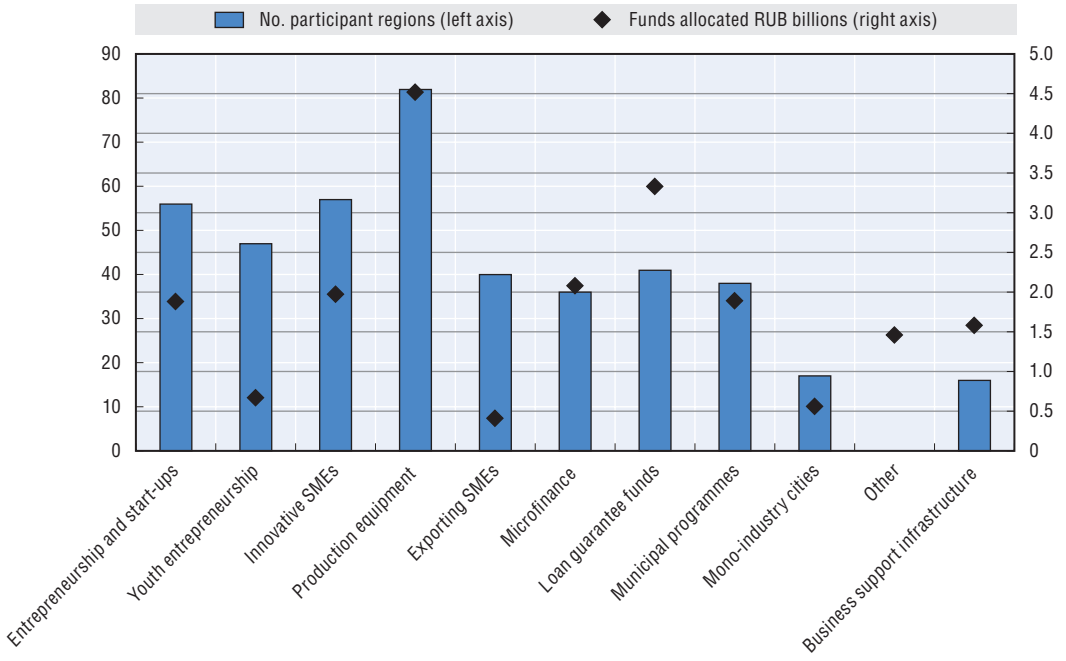
Regional and municipal governments can also get involved in SME and entrepreneurship promotion working independently or in collaboration with federal government. However, self-generated local policy actions are frequently held back by limited enthusiasm from local political leaders for small business development issues, limited professional capacities within regional and municipal governments for designing appropriate interventions and limited economic development budgets. A contributing factor is the limited level of fiscal decentralisation and the high proportion of business taxes raised locally that are transferred to the federal level. This may both reduce the motivation of sub-national governments to introduce SME and entrepreneurship actions and their capacity to plan and fund them.

The federal government plays an important part in encouraging SME and entrepreneurship programme actions in regions and municipalities through offering competitive co-funding towards the activities supported by the federal SME support programme. By varying the federal funding rate, which ranges from 50% in richer regions to 70% in poorer regions, and even as high as 95% for some support initiatives in some regions, the government helps promote particular actions in those places with the greatest needs and the weakest budgets. In practice, however, many regions do not put forward bids to participate in certain programme components, while others put forward bids that are not acceptable to federal government and are therefore not funded. As a result, only 16 regions participated in the business support infrastructure component of the federal SME support programme in 2012, and less than one-half of regions participated in the SME exporting, microfinance, loan guarantee and municipal programme components (Figure 1.16). One of the reasons for the low levels of regional participation is that the rules governing the details of the support that must be provided are often quite rigid and regional governments feel that they are not able to use the federal resources for the activities they wish to pursue.

As well as encouraging local action, the co-funding arrangements of the federal SME support programme provide a mechanism for achieving coherence between federal and local programmes. However, the co-ordination works best where there is active dialogue between federal and regional governments on proposed policy interventions. Whereas some regional authorities have been very proactive, many of those regions that have limited participation in the programme have not been very proactive in dialogue. The 2007 federal SME Act also set up a formal process for creating development strategies in each region that are cross-referenced with federal development plan priorities. In principle, such regional strategies could be very important for identifying the most appropriate SME and entrepreneurship interventions in each region and enabling co-ordination and complementarity with national interventions. However, although several economically-advanced regions, such as Kaluga and Novosibirsk, have developed solid and regionally-distinct strategies, many less advanced regions lack a genuine and tailored strategy covering SME and entrepreneurship policy actions. Furthermore, robust programme evaluation is rarely used to provide an evidence base for strategy development, even in the advanced regions.

Figure 1.16. **Regional participation in federal SME fund programme components**

2012



Note: "Other" is not specified in the information supplied but includes support for activities to promote entrepreneurship and to develop a system of personnel training, retraining and advance training for the small business sector (training vouchers, compensation for training/ retraining costs, and organisation of training events).

Source: Information provided by the Russian Federation Ministry of Economic Development.

StatLink http://dx.doi.org/10.1787/888933272196

Key policy recommendations for federal government on the local dimension of SME and entrepreneurship policy

- Encourage all regional and municipal authorities to adopt good practice approaches in regulatory improvement and the use of public procurement for SME and entrepreneurship promotion, including through the creation of a national platform for experience sharing.
- Re-examine arrangements for the distribution of business taxation revenues with a view to increasing the incentives for regional and municipal governments to implement SME and entrepreneurship actions and increase the resources they put into this task.
- Strengthen the local differentiation and tailoring of selected programmes of federal ministries and agencies, including supporting more region-specific financing services through the public development bank, *Vnesheconombank*, such as venture capital and business angel initiatives in regions where strong innovative SME sectors are emerging, and expanding the federal clusters programme to cover non-science based sectors and include activities for skills development as well as innovation.
- Increase the participation of regional and municipal governments in the federal SME support programme by increasing federal-local dialogue in the design of programme components and increasing flexibility in the rules and management of the programme to better meet local priorities.

Key policy recommendations for federal government on the local dimension of SME and entrepreneurship policy *(cont.)*

- Support regional and municipal authorities to develop their professional capacities for designing and implementing locally-distinct, evidence-based policies and programmes for SME and entrepreneurship promotion. Provide guidelines, training and forums for good practice exchange in strategy making, propose appropriate modules of policy support that can be implemented in different types of regions, and encourage the creation of new dedicated economic development ministries and offices in regional and municipal governments.

Chapter 2

SMEs and Entrepreneurship in the Russian Federation

This chapter examines the state and recent evolution of entrepreneurship and SME activity in the Russian Federation. It presents key structural indicators such as the SME share in enterprises, employment and GDP, the sector and size distribution of SME activity, business start-up rates, entrepreneurial intentions, number of growth firms and the size of the informal economy. It also analyses performance indicators including productivity, exports, investment and innovation.

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

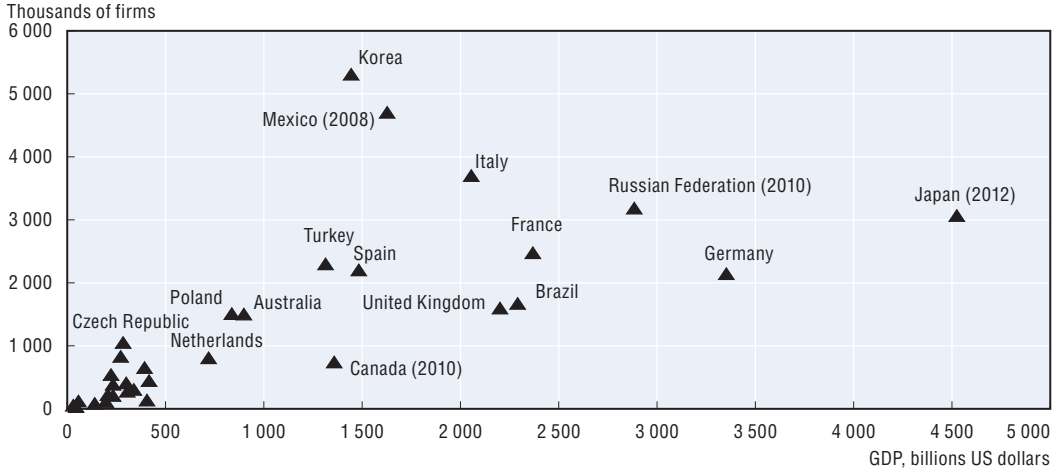
SME activity

Limited numbers of SMEs

The Russian Federation counted an estimated 3.2 million operating businesses, including the self-employed, in 2010. As shown in Figure 2.1, this is a small number relative to the size of the Russian economy. Several smaller economies such as Italy, Mexico and Korea have greater numbers of businesses than the Russian Federation. Table 2.1 shows these SME numbers in terms of a density of enterprises as a share of the working age population. The rate of 31 registered enterprises per 1 000 population in the Russian Federation is well below that of the OECD countries, and compares for example with rates of 67 in Mexico and 102 in the United States.

Figure 2.1. **Number of enterprises and GDP**

2011 or latest available year



Note: Figures refer to the number of operating enterprises in the business sector, excluding the agriculture and government sectors. They include registered enterprises ("legal entities") and the self-employed ("independent entrepreneurs"). Tax records identify some additional proprietary businesses that are considered as non-operational by the national statistical office.

Source: OECD (2014) Entrepreneurship at a Glance 2014, Paris. *http://dx.doi.org/10.1787/entrepreneur_aag-2014-en*. Figures for Russian Federation from Rosstat SMEs in Russia (2011).

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In terms of size breakdown, some 79.5% of enterprises in the Russian Federation were micro firms (1-9 employees) in 2012, 16.0% were firms sized 10-49 employees, 3.8% were of 50-249 employees and 0.7% were large firms of at least 250 employees (OECD, 2014). Compared with other countries there is a particular dearth in the numbers of micro- and small-sized enterprises.

Table 2.1. **Number of enterprises per working age population, 2011 or latest year**

	Number of enterprises (thousands)	Working age population	Enterprises per 1000 population
Switzerland	134	5 372 242	25
New Zealand (2010)	83	2 902 000	29
Russian Federation (2010)	3 180	102 846 000	31
Ireland	110	3 066 600	36
Japan (2012)	3 064	81 493 000	38
United Kingdom	1 595	41 710 800	38
Germany	2 141	54 048 604	40
Turkey	2 295	48 226 830	48
Austria	303	5 675 483	53
Greece (2009)	405	7 449 000	54
Poland	1 503	27 438 382	55
Denmark (2010)	207	3 631 155	57
France	2 471	40 766 767	61
Estonia	55	894 643	61
Belgium	446	7 267 065	61
Finland	224	3 538 000	63
Mexico (2008)	4 706	70 679 579	67
Spain	2 199	31 225 029	70
Netherlands	804	11 135 552	72
Hungary	540	6 836 546	79
Luxembourg	29	356 164	81
Slovenia	116	1 418 366	82
Israel (2012)	383	4 664 500	82
Norway	271	3 276 000	83
Slovak Republic	346	3 881 763	89
Italy	3 702	39 811 683	93
Australia	1 502	14 846 000	101
United States (2010)	21 143	207 648 030	102
Sweden	647	6 113 639	106
Portugal	826	6 981 487	118
Czech Republic	1 049	7 295 598	144
Korea	5 305	36 352 538	146

Note: Figures refer to the number of operating enterprises in the business sector, excluding the agriculture and government sectors. They include registered enterprises and the self-employed.

Source: OECD(2014) Entrepreneurship at a Glance and OECDstat Population Statistics database. Figures for Russian Federation from Rosstat SMEs in Russia report (2011).

StatLink http://dx.doi.org/10.1787/888933272218

Limited SME employment

In 2010, it is estimated that just over 18 million people were employed in SMEs in the business sector in the Russian Federation. At only 18% of the working population, employment in SMEs is relatively low in the Russian Federation (Table 2.2). Similarly, at less than 30%, the share of business sector employment accounted for by SMEs in the Russian Federation is much lower than in other countries, as shown in Figure 2.2. These figures suggest that there is great potential for job creation by establishing and growing an SME sector in the Russian Federation. Much of the SME employment gap is the result of a small micro enterprises sector. Thus, the proportion of business employment in small firms (defined as 1-15 employees in the Russian Federation) at 13% is smaller than that of employment in small firms (defined as 1-9 employees) in almost all OECD countries. Overall, these low shares of SME employment are common to both the manufacturing and services sectors (OECD, 2014).

Table 2.2. **SME employment as a share of the working age population, 2011 or latest year**

	SME employment	Working age population	Proportion of working age population employed in SMEs (percentage)
Turkey (2009)	4 560 654	48 226 830	9
Estonia	125 131	894 643	14
Greece (2009)	1 056 236	7 449 000	14
Ireland	462 096	3 066 600	15
Russian Federation (2012)	18 120 000	102 846 000	18
United States (2010)	38 121 694	207 648 030	18
Korea	7 000 104	36 352 538	19
Slovenia	277 981	1 418 366	20
Poland	5 416 765	27 438 382	20
Finland	708 623	3 538 000	20
United Kingdom	8 455 428	41 710 800	20
Luxembourg	74 343	356 164	21
Belgium	1 539 909	7 267 065	21
Slovak Republic	841 941	3 881 763	22
France	9 012 535	40 766 767	22
Denmark (2010)	812 018	3 631 155	22
Hungary	1 582 053	6 836 546	23
Spain	7 703 013	31 225 029	25
New Zealand (2010)	716 965	2 902 000	25
Sweden	1 626 221	6 113 639	27
Austria	1 541 784	5 675 483	27
Italy	11 186 215	39 811 683	28
Australia (2010)	4 245 495	14 846 000	29
Mexico (2008)	20 260 865	70 679 579	29
Germany	15 734 377	54 048 604	29
Netherlands	3 300 047	11 135 552	30
Norway	1 007 810	3 276 000	31
Portugal	2 166 851	6 981 487	31
Switzerland	1 737 030	5 372 242	32
Czech Republic	2 439 886	7 295 598	33
Japan (2009)	38 452 501	81 493 000	47
Israel (2009)	2 227 323	4 664 500	48

Note: Data refer to enterprises in the business economy, excluding the agriculture and government sectors.

Source: OECD (2014) Enterprise at a Glance 2014 and OECDstat Population Statistics database. Figures for Russian Federation from Rosstat (2013) SMEs in Russia 2013.

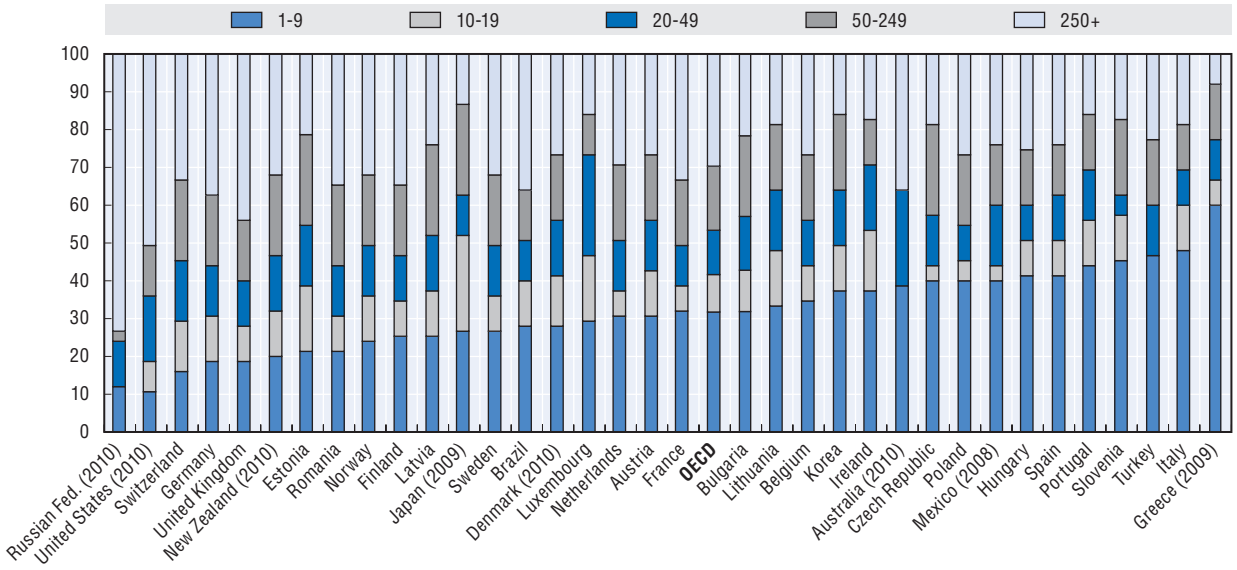
StatLink http://dx.doi.org/10.1787/888933272224

Low SME output and investment

Table 2.3 provides information on the sales, investment and assets of Russian Federation SMEs. When expressed as a share of total business activity, SMEs accounted for 32% of enterprise sales in 2012 (Rosstat, 2013). While not strictly comparable with international data, this proportion is well below the average typical figure in OECD countries of around two-thirds of business value added generated SMEs (OECD, 2014). Furthermore, SMEs accounted for only 7.6% of the total fixed capital investments of businesses and 23.5% of the fixed assets of the total enterprise sector in 2012 (Rosstat, 2013). These figures underline the need to increase the quality of existing SME activity in the Russian Federation as well as increase the numbers of businesses and their employment.

Figure 2.2. **Share of employment by enterprise size class**

Percentage of total employment in enterprises



Note: The size-class breakdown 1-9, 10-19, 20-49, 50-249, 250+ provides for the best comparability given the varying data collection practices across countries. Some countries use different conventions: the size class "1-9" refers to "1-10" for Mexico; "1-19" for ustralia and Turkey; the size class "10-19" refers to "11-50" for Mexico; the size class "20-49" refers to "20-199" for Australia and "20-99" for the United States; the size class "50-249" refers to "50-299" for Japan, "51-250" for Mexico and "100-499" for the United States; finally, the size class "250+" refers to "200+" for Australia, "300+" for Japan, "251+" for Mexico and "500+" for the United States. Figures for Russian Federation: «1-9» refers to 1-15; «20-49» refers to 16-100 «50-249» refers to 101-250.

Source: OECD (2014), Entrepreneurship at a Glance 2014, OECD Publishing. *http://dx.doi.org/10.1787/entrepreneur_aag-2014-en*. Figures for Russian Federation from Rosstat SMEs in Russia 2011 and Rosstat databases.

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Table 2.3. **SME output and investment, Russian Federation, 2012 or latest available year**

	All SMEs	Medium enterprises	Small enterprises	Micro enterpriss
Number of businesses registered	2 016 800	13 800	243 000	1 760 000
Sales, RUB billions	28 174	4 711	15 116	8 347
Fixed capital investments, RUB billions	729	208	364	157
Fixed assets (book value), RUB billions	21 285	1 657	2 465	17 163

Note: The figures for registered enterprises include non-operational enterprises, which suspended or did not start business operations. Micro enterprises are defined as having employment of less than 15 or sales less than RUB 60 million; small enterprises have 16-100 employees or sales up to RUB 400 million; medium enterprises have employment of 101-250 or sales or not more than RUB 1 billion.

Source: Rosstat (2013) SMEs in Russia report 2013.

StatLink *http://dx.doi.org/10.1787/888933272234*

Weighting to non-propulsive sectors

Table 2.4 shows that SME business numbers and employment in the Russian Federation are significantly weighted towards wholesaling and retailing. These sectors represented nearly one-half of all SMEs by number and more than one-third of SME employment. They make up particularly high shares of the numbers and employment of the smallest enterprises. A further one-third of SMEs and SME employment are in the domestic consumption oriented sectors of hotels, restaurants, transport, communications, construction, and real estate, renting and business services. On the other hand, manufacturing accounted for only 7% of

SMEs by number and only 13% by employment, including the self-employed. The proportions of manufacturing were lowest in the smallest enterprise size bands. In the "medium" size class the representation of manufacturing was nevertheless higher; manufacturing accounted for 25% of medium-sized enterprises and 29% of employment in medium-sized enterprises.

These data indicate a shortfall in the scale of the manufacturing sector within the activities of SMEs in the Russian Federation, and a bias towards consumer-oriented services. Put in other terms, less than 20% of manufacturing employment was in SMEs in the Russian Federation, compared with 38% of services employment. The SME share of employment in manufacturing tends to be much higher in comparator countries. For example, SMEs accounted for approximately 49% of manufacturing employment in the United States, 51% in Mexico, 52% in Brazil, 61% in Poland, 71% in Korea and 76% in Italy and Bulgaria (OECD, 2014).

A substantial increase should be sought in the scale of SME manufacturing activity in the Russian Federation in order to exploit its relatively good prospects to sustain long-run productivity growth, provide export income and diversify Russian exports away from natural resources exploitation, as well as to support growth in the rest of the economy through supply chain inputs. While short-term productivity improvements in the Russian Federation's transport, construction and services sectors can make significant contributions to economic growth, these sectors tend to have a relatively low capacity to generate export income and a relative small scope for long-term productivity growth compared with manufacturing. Furthermore, while the agriculture, fisheries, mining and gas sectors can have high productivity and high productivity growth and be important exporters, they are based on natural resources exploitation, whereas the long-term growth of the Russian economy requires this to be complemented with other types of exports further up the value chain. Thus support for growth in manufacturing SMEs is a particular priority for the Russian Federation, potentially complemented with an emerging knowledge-intensive business services sector supplying producers rather than consumers.

Table 2.4. **Sector composition of SMEs and individual entrepreneurs, Russian Federation, 2012**

Share of enterprises, percentage

	By number of enterprises					By employment				
	All	Medium	Small	Micro	Individual Entrepreneur	All	Medium	Small	Micro	Individual Entrepreneur
Agriculture and fisheries	5	20	5	3	5	7	19	6	3	6
Construction	7	12	13	11	3	10	12	14	13	3
Mining, electricity and gas	0	4	2	1	0	2	5	2	1	0
Manufacturing	7	25	15	9	5	13	29	17	10	7
Wholesale and retail trade	48	23	29	41	54	36	14	23	37	58
Hotels and restaurants	2	1	4	3	2	3	1	4	4	3
Transport and communication	10	4	6	7	13	7	5	6	6	9
Real estate, renting, and business activities	15	10	21	20	11	16	10	22	21	7
Other	6	2	5	6	7	5	4	5	6	5
Total	100	100	100	100	100	100	100	100	100	100

Note: Data cover all registered enterprises including some that may not be operating. The figure for All SMEs includes both legal entities (which are further divided between medium, small, and micro) and individual entrepreneurs, with or without employees. Micro enterprises are defined as having employment of less than 15 or sales less than RUB 60 million; small enterprises have 16-100 employees or sales up to RUB 400 million; medium enterprises have employment of 101-250 or sales or not more than RUB 1 billion. Figures include legal entities but exclude individual entrepreneurs, or the self-employed.

Source: Calculated from Rosstat (2013) SMEs in Russia 2013.

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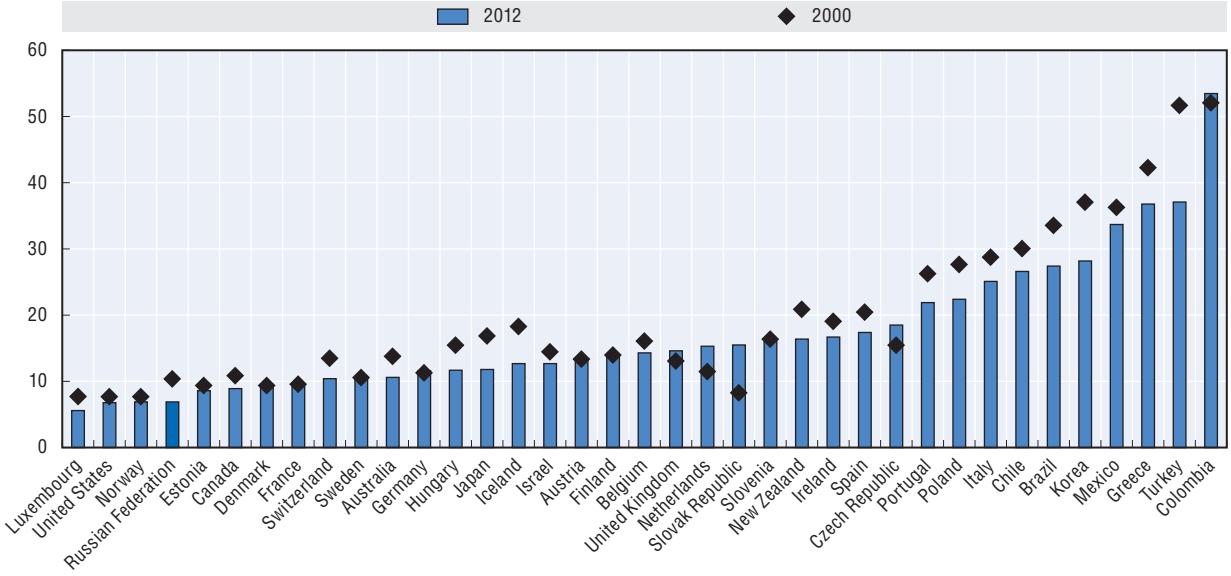
Growth in SME manufacturing could be supported by a stronger focus in SME support programmes on measures for innovation, exporting, and investment in physical and human capital. These measures are likely to see relatively greater take-up from manufacturing firms, and particularly medium-sized manufacturers, even without any specific targets for numbers or proportions of manufacturing enterprises to be covered by such programmes or eligibility restrictions to manufacturing firms. Indeed, the option should be available for firms in other sectors (particularly knowledge intensive business services) to participate on a case-by-case basis, since some non-manufacturing enterprises could also achieve significant output, export and productivity growth as a result.

Self-employment

According to the labour force survey, there were an estimated 4.9 million employers and persons working on their own account in the Russian Federation in 2012, representing some 6.9% of all civil employment. This is a relatively low share; across OECD countries the average share of self-employment was some 17% (Figure 2.3). Furthermore, the self-employment rate declined in Russia between 2000 and 2012. More than one-half of the self-employed operated in wholesaling and retailing. Other significant sectors for self-employment were transport and communications and real estate and business services, but less than 5% of the self-employed were in manufacturing (Rosstat, 2013)

Figure 2.3. **Share of self-employment in total employment**

Percentage, 2012 and 2000



Note: Figures for Brazil and Columbia are for 2001 not 2000; figures for Chile France and Luxembourg are for 2011 not 2012; figures for Australia, Canada, and United States for do not include incorporated self-employed.

Source: OECD Annual Labour Force Statistics database; Employment by Activities and Status *http://dx.doi.org/10.1787/lfs-data-en*.

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Entrepreneurial activity

Business start-up

In 2014, just 2.4% of the Russian Federation population was engaged in nascent entrepreneurship, the lowest rate of any of the large efficiency-driven economies; and, at 2.4%, the rate of new business ownership in the Russian Federation was also very

low (Table 2.5). Taking the two indicators together, the total early stage entrepreneurial activity rate in the Russian Federation was the lowest of the large efficiency-driven economies. This suggests that the forward pipeline of entrepreneurs coming into activity in the Russian Federation is currently very weak. Indeed, the percentage of the population running businesses that have been established for at least 42 months is only 4.0% in the Russian Federation compared to an average of 8.5% in efficiency-driven economies as a whole.[1]

The Table also distinguishes between "opportunity driven entrepreneurs", who claim to have started their business to exploit specific business opportunities, and "necessity driven entrepreneurs", who open businesses mainly because they have no or few other sources of income. The motives are interesting, although the distinction is generally not a good indicator of subsequent business performance. This is because an entrepreneur's motives for running a business can change over time and changes in the external environment can affect entrepreneurial opportunities. In the Russian Federation, while 42% of entrepreneurs could be attributed to necessity reasons, 59% were more opportunity driven. This balance is very similar to the overall average for the listed countries.

Table 2.5. **Entrepreneurial activity rates in efficiency-driven economies, 2014**

	Nascent	New business ownership	Total early stage entrepreneurship	Established business ownership	Opportunity driven	Necessity driven
	Percentage of population aged 18-64 years				Percentage of early stage entrepreneurs	
Argentina	9.5	5.2	14.4	9.1	68	28
Barbados	8.5	4.2	12.7	7.1	74	15
Bosnia and Herzegovina	4.5	2.9	7.4	6.7	48	51
Brazil	3.7	13.8	17.2	17.5	71	29
Chile	16.6	11.1	26.8	8.8	81	18
China	5.5	10.2	15.5	11.6	66	33
Croatia	6.0	2.0	8.0	3.6	51	47
Hungary	5.6	3.9	9.3	8.0	65	33
Latvia (2013)	8.1	5.3	13.4	8.8	53	21
Lithuania	6.1	5.3	11.3	7.8	80	20
Malaysia	1.4	4.6	5.9	8.5	82	18
Mexico	12.7	6.4	19.0	4.5	76	22
Panama	13.1	4.1	17.1	3.4	73	26
Peru	23.1	7.3	28.8	9.2	83	16
Poland	5.8	3.6	9.2	7.3	59	37
Romania	5.3	6.2	11.4	7.6	70	29
Russian Federation	2.4	2.4	4.7	4.0	59	39
Slovak Republic	6.7	4.4	10.9	7.8	64	33
South Africa	3.9	3.2	7.0	2.7	71	28
Thailand	7.6	16.7	23.3	33.1	81	18
Trinidad and Tobago	7.5	7.4	14.6	8.5	86	12
Turkey (2013)	5.5	4.7	10.2	5.7	54	30
Uruguay	10.5	5.8	16.1	6.7	82	16

Notes: Nascent entrepreneurship is defined as the percentage of the population between 18 and 64 years that is currently involved in starting a business either as owners or co-owners. New business ownership is defined as the percentage of the population between 18 and 64 years that are currently owners, owners or managers of businesses that are less than 42 months old. Total early stage entrepreneurial activity is the sum of the nascent entrepreneurship and new business ownership rates.

Source: Singer, Amorós and Arreola (2015) Global Entrepreneurship Monitor 2014 Global Report.

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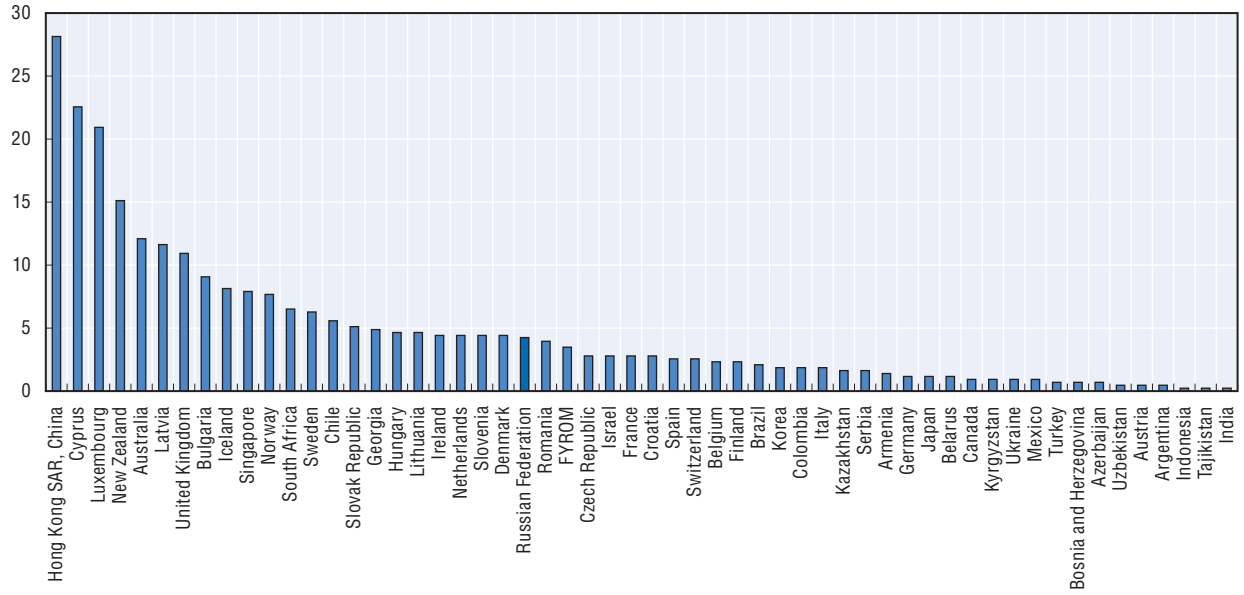
New business density

Further evidence on the performance of the Russian Federation in new venture creation is provided in Figure 2.5, based on data compiled from official business registers, which shows that although the Russian Federation falls in the centre of the distribution, it performs worse than many mature market economies as well as a number of former Socialist economies that are now part of the European Union.

Figure 2.4. **Number of newly-registered limited liability companies per thousand people of working age (15-64 years), selected OECD and emerging economies, 2012**[2 3]



Source: IFC/World Bank Entrepreneurship Database, 2012. *http://www.doingbusiness.org/data/exploretopics/entrepreneurship*.

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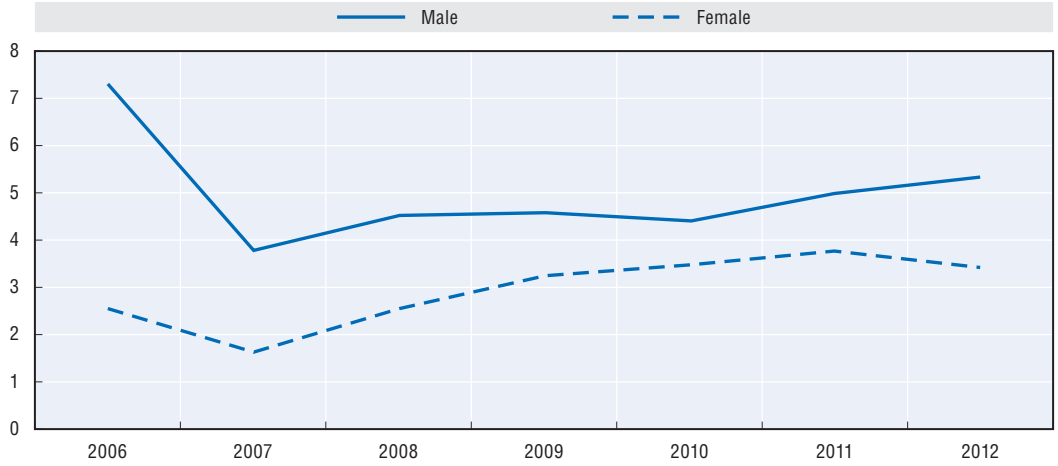
Gender differences

In many countries, the rate of participation of women in entrepreneurial activity is substantially below the corresponding rate for males. In the Russian Federation, women made up 40% of all early-stage entrepreneurs in 2012. This is one of the highest proportions of in ECA and emerging economy countries. As shown in Figure 2.6, there have been changes in the gap in early stage entrepreneurial activity between women and men since 2006. After a significant reduction in the gap between men and women from 2006-11, the gap grew again in 2012. On the one hand the generally high rate of women entrepreneurship compared with other countries is very positive, implying that SME and entrepreneurship policies in the Russian Federation are well set to increase economic activity by affecting both halves of the population. On the other hand, there is still some more to do in making up the gap with male entrepreneurs. This will require some specific initiatives to ensure that women have equal access to business support, together with some more specific training and coaching initiatives aimed at women. The latter concern relates to evidence from the GEM survey that fewer women feel that they have the necessary knowledge and skills needed to open a business (29% of

adult women compared with 38% of adult males) and that fear of failure is considerably higher among women than among men (51% of women report that fear of failure would prevent them from starting a business compared with 42% of men) (Verkhovskaia and Dorokhina, 2012).

Figure 2.5. **Percentage of adults in early stage entrepreneurial activity in the Russian Federation by gender, 2006-2012**



Source: Verkhoovskaia and Dorkhina (2013) Global Entrepreneurship Monitor Russia 2012.

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Entrepreneurial attitudes

Prevailing attitudes towards entrepreneurship in the population as a whole are less positive in the Russian Federation than in many other countries, hindering new business formation rates. As shown in Table 2.6, although 67% of non-entrepreneurs in the Russian Federation considered that entrepreneurship is a good career choice and 66% considered that successful entrepreneurs have high status within the society in 2014, much in line with the average across countries, only 27% perceived good opportunities for starting a business, only 28% believed that they have sufficient knowledge and experience to undertake entrepreneurial activity, and only 4% indicated an intention to start a business within the next 3 years. The Russian Federation is among the weakest countries on these latter measures. There appears to be significant scope to improve media coverage of entrepreneurship given that only 50% of those surveyed in the Russian Federation thought that the media gives a positive image of entrepreneurship, a rate below many other countries (Singer, Amorós and Arreola, 2015). Similarly, whereas there is little difference between Russians and European Union residents in terms of seeing entrepreneurs as job generators, 76% of Russians consider that entrepreneurs take advantage of others, compared with 57% in the European Union (European Commission, 2012).

Table 2.6. **Entrepreneurial attitudes and perceptions, selected OECD and emerging economies, 2013**

Percentage of adults who are not currently an entrepreneur

Country	Start-up intentions	Perceived opportunities	Perceived capabilities	Fear of Failure	Entrepreneurship as a desirable career choice	High status	Positive media attention
Argentina	28	32	58	24	58	52	64
Belgium	11	36	30	49	52	52	51
Brazil	25	56	50	36	0	0	0
Canada	12	56	49	37	57	70	68
Chile	50	67	65	28	69	64	65
China	19	32	33	40	66	73	69
Colombia	47	66	57	31	70	67	74
Croatia	20	18	46	30	63	47	40
Czech Republic (2013)	14	23	43	36		48	
Estonia	10	49	42	42	56	65	43
Finland	8	42	35	37	41	84	67
France	14	28	35	41	59	70	39
Germany	6	38	36	40	52	79	51
Greece	10	20	46	62	58	66	46
Hungary	14	23	41	42	47	72	33
India	8	39	37	38	58	66	57
Indonesia	27	45	60	38	73	78	85
Ireland	7	33	47	39	49	77	76
Israel (2013)	24	47	36	52	61	80	49
Italy	11	27	31	49	65	72	48
Japan	3	7	12	55	31	56	59
Korea (2013)	12	13	28	42	51	68	68
Latvia (2013)	23	35	48	42	61	59	59
Lithuania	20	32	33	45	69	58	55
Luxembourg	12	43	38	42	41	68	44
Mexico	17	49	53	30	53	51	45
Netherlands	9	46	44	35	79	68	56
Norway	5	63	31	38	58	83	0
Poland	16	31	54	51	63	56	55
Portugal	16	23	47	38	62	63	70
Romania	32	32	48	41	74	75	71
Russian Federation	4	27	28	39	67	66	50
Singapore	9	17	21	39	52	63	79
Slovak Republic	15	24	54	36	45	58	53
Slovenia	11	17	49	29	53	72	58
South Africa	10	37	38	25	70	73	73
Spain	7	23	48	38	54	49	46
Sweden	8	70	37	37	52	71	60
Switzerland	7	44	42	29	42	66	50
Thailand	22	47	50	42	74	71	80
Turkey (2013)	28	39	52	30	64	74	53
United Kingdom	7	41	46	37	60	75	58
USA	12	51	53	30	65	77	76

Source: Singer, Amorós and Arreola (2015) Global Entrepreneurship Monitor 2014 Global Report.

StatLink http://dx.doi.org/10.1787/888933272268

Informal economy

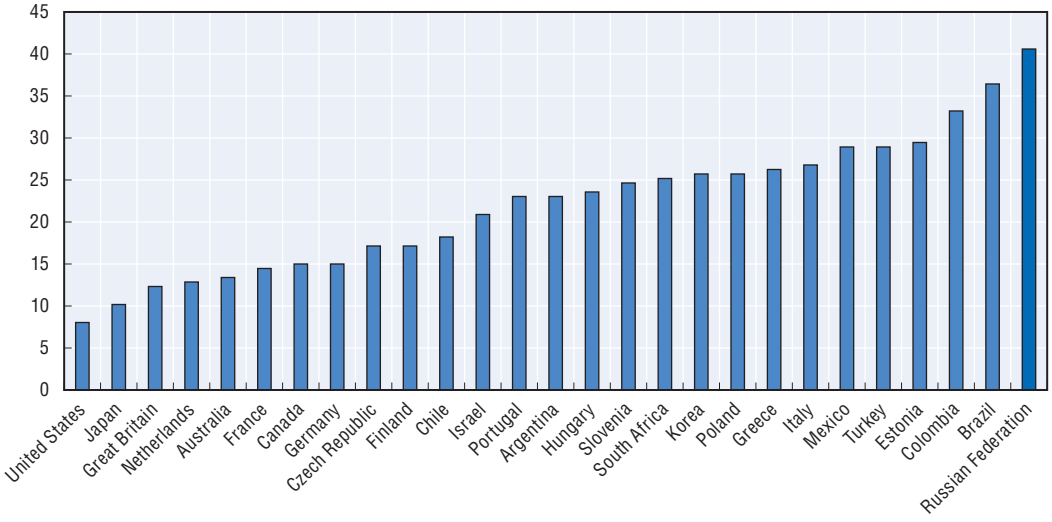
Hidden and untaxed employment and business activity is present in all countries, involving both businesses that are not registered and not compliant with business and tax laws and regulations and businesses that are registered but evade some taxes by declaring

only some of their income and workforces. In some senses this activity has a positive side, in that it provides work and income opportunities to people who might otherwise have none and offers the makings of an entrepreneurial population and entrepreneurial activity. However, a large informal sector is generally a burden to economic growth because of its low productivity and low growth ambitions (in turn reflecting lack of access to credit, training and legal protection etc.), its negative effects on formal activity (for example by undercutting prices), and its undermining of fiscal revenues and public investment.

The Russian Federation has a large informal economy relative to OECD economies but is more in line with non-OECD comparator countries in similar income groups. Figure 2.7 shows the level of informality estimated by the Schneider approach, which estimates the size of the informal sector from a number of observable factors that are correlated with informality. This measure suggests that the extent of informal economic activity is somewhat greater in the Russian Federation than in comparators such as Brazil and Mexico, and significantly higher than in other post-Socialist central and eastern European countries such as Poland and the Czech Republic.

Figure 2.6. **The estimated scale of the informal economy, Schneider definition**

Percentage of economic activity, 2007



Source: OECD (2011), OECD Economic Surveys: Mexico 2011, OECD Publishing, Paris, *http:/dx.doi.org/10.1787/eco_surveys-mex-2011*-enbased on International Labour Office (2011). Statistical Update on Employment in the Informal Economy, International Labour Office, Department of Statistics.

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Using an alternative survey-based approach, the International Labour Office (2011) estimated that there were 7.78 million informal sector jobs in the Russian Federation in 2011 (i.e. jobs which lack legal protection for employment benefits), representing 12.1% of total non-agricultural employment. While this was lower than many comparator countries (it compares for example to 32.1% of non-agricultural employment in Argentina, 24.3% in Brazil, 52.2% in Colombia, 34.1% in Mexico, and 9.4% in Ukraine), it still suggests that the Russian Federation has a substantial informal sector, and one that is much larger than in the most advanced economies. At the same time, the informal activity is not enough on its own to explain the low rates of formal activity in the SME sector in the Russian Federation. For example, even attributing all the informal jobs estimated by the International Labour Office survey to estimated SME employment would still leave the Russian Federation with an SME employment rate substantially below the OECD average.

A number of policy measures may be developed with the aim of converting informal to formal entrepreneurship activity. As well as better policing, they include simplifying business regulation and compliance costs, increasing the security of property rights to create "institutional trust" among entrepreneurs and raising awareness among entrepreneurs of the disadvantages of remaining in the informal sector. However, any measures that seek to reduce informality risk depriving households of work and income if they are not able to continue in the formal sector. The balance between deterrence as a policy to reduce informality and finding positive ways in which to incentivise formality is difficult to find and is a concern shared by many countries. Box 2.1 gives the example of a good practice initiative in Italy which provides informal entrepreneurs with incentives to formalise their businesses and employment.

Box 2.1. **Addressing the informal economy, CUORE Programme, Italy**

Description of the approach

The Urban Operational Centres for Economic Renewal (*Centri Urbani Operativi per la Riqualificazione Economica*, CUORE) project was started by Naples municipal government and the University of Naples in 1999 and has subsequently been extended to other cities across Italy. It involves the creation of a series of neighbourhood service centres in which business development advisors linked to the University make contact with entrepreneurs and potential entrepreneurs who may be operating in the informal sector. The advisors, who are familiar with local conditions, offer information on business regulation, business development advice, pathways to relevant government business support programmes and customised business regularisation procedures for undeclared businesses or workers requesting formalisation. They make door-to-door visits and telephone contacts targeting local workers, employers, and unemployed people as well as offering drop in support at the centres. They also train and support municipal staff responsible for business regulation in dealing with informal entrepreneurs. The primary objective is to develop a friendly relationship between the state and informal entrepreneurs, with the government offering help but expecting something in return.

Results

An evaluation in 2005 of the four original neighbourhood service centres established in Naples indicated the following results:

- Approximately 8 000 contacts were made by telephone, in person at the centres or during face-to-face visits. Some 3 580 people received support for setting up a business, 1 500 of whom were women.
- 1 280 businesses that were engaged in undeclared work received advice on their situation, and 326 situations were resolved through formalisation.
- 80 companies were supported to participate in regional trade fairs and received micro support to develop their businesses.

Success factors

One of the factors in the success of this initiative has been the involvement of the University, which helped to the business advisors to obtain the trust and involvement of the community, both because of their independence and their understanding of local businesses needs and cultures. It is also critical that the centres offer support to informal entrepreneurs and not simply threats. The neighbourhood service centres also have the flexibility to design and offer services that fit the needs of their local communities. Furthermore, continuous training of neighbourhood service centre staff has been important, including support in adapting to changes in the local environments in which they are operating.

Box 2.1. **Addressing the informal economy, CUORE Programme, Italy** *(cont.)*

Obstacles and responses

The project has encountered certain challenges, including:

- Mistrust and reticence among entrepreneurs, who are often reluctant to participate for fear of being exposed to organised crime. The project therefore has to be embedded within a wider strategy for reducing criminality.
- Local governments often see reducing the informal sector as a one-off action that will be quickly completed and have been reluctant to provide the sustained funding necessary to intervene with new people coming into informality.
- There have been difficulties in reconciling the obligations of agencies responsible for pursuing those breaking the law with the economic development objective of seeking to assist businesses to formalise and grow.

Addressing these issues has required continued flexibility in operation.

Relevance to the Russian Federation

The Russian Federation has significant numbers of informal entrepreneurs whose contribution to the economy is unduly limited. A deterrence approach (sanctions against those found breaking the law) has been relatively ineffective and ways need to be found to coordinate state institutions to make formality more attractive. This model shows one approach, based on outreach and flexible service support through neighbourhood service centres established in urban areas with high informality levels.

Further information

www.comune.napoli.it/flex/cm/pages/ServeBLOB.php/L/IT/IDPagina/19156

www.eurofound.europa.eu/areas/labourmarket/tackling/cases/it001.htm

Source: Based on information from Naples municipal government and Eurofound

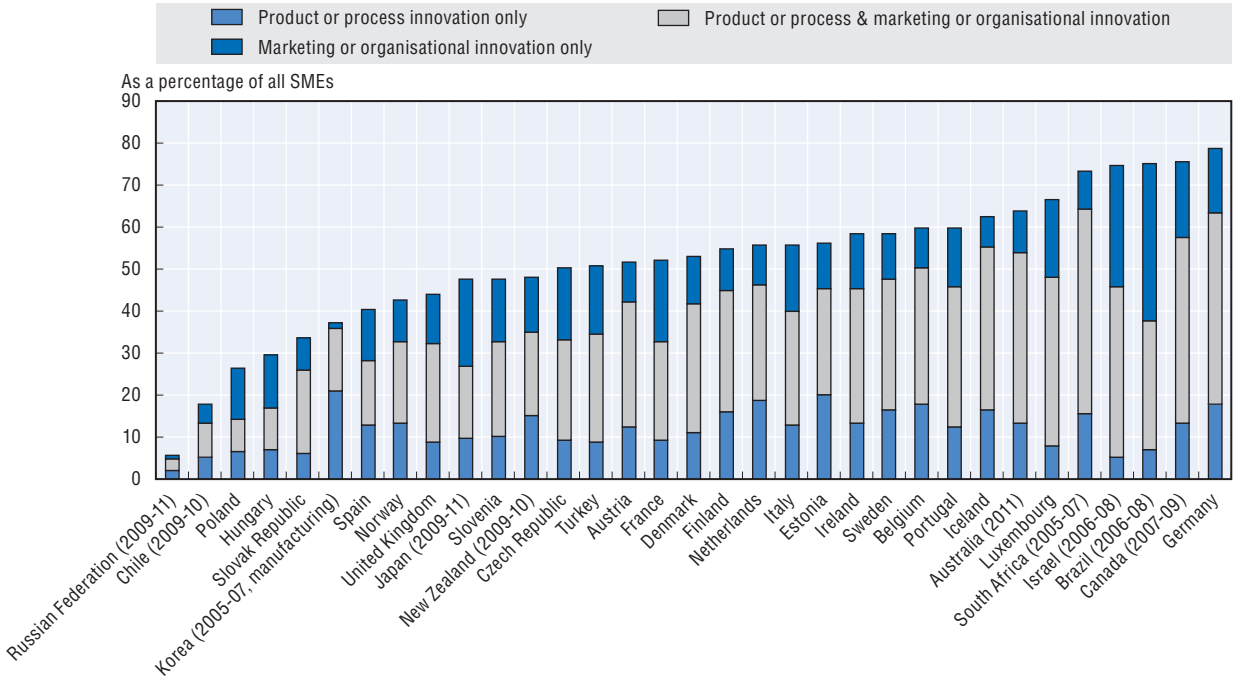
SME innovation

Innovation in the form of advances in products, processes, organisational methods and marketing techniques is a key factor in the competitiveness of territories and a vital ingredient for growth-oriented start-ups and SMEs. However, as shown in Figure 2.8, innovation activity is reported by less than 6% of SMEs in the Russian Federation, well below rates of typically around 50% in OECD countries (Figure 2.8). As shown in the chart, the proportions are low both for marketing and organisational innovation on the one hand, and product and process innovation on the other and very few Russian SMEs do both.

The finding of low innovation rates among SMEs in the Russian Federation is backed up by the 2011 SME Census in the Russian Federation, which reveals that in 2011 just 1.6% of SMEs made specific expenditures on innovation (2.8% of medium-size businesses, 1.6% of small businesses and 1.3% of micro enterprises) (Rosstat, 2011). Similarly an innovation survey by the Higher School of Economics in Moscow found that only 10% of businesses across the Russian Federation reported undertaking technological innovation activity in 2008 (a proportion that had been constant over the previous decade), and that innovative products represented only approximately 5% of total sales of Russian enterprises compared with a European Union average of approximately 10% (OECD, 2014).

Figure 2.7. **Innovating SMEs by type of innovation**

2008-10 or latest available years



Source: OECD (2013), Innovation types by firm size, 2008-10: As a percentage of all SMEs and large firms, in OECD Science, Technology and Industry Scoreboard 2013, OECD Publishing, Paris. DOI: *http://dx.doi.org/10.1787/sti_scoreboard-2013-graph165-en*.

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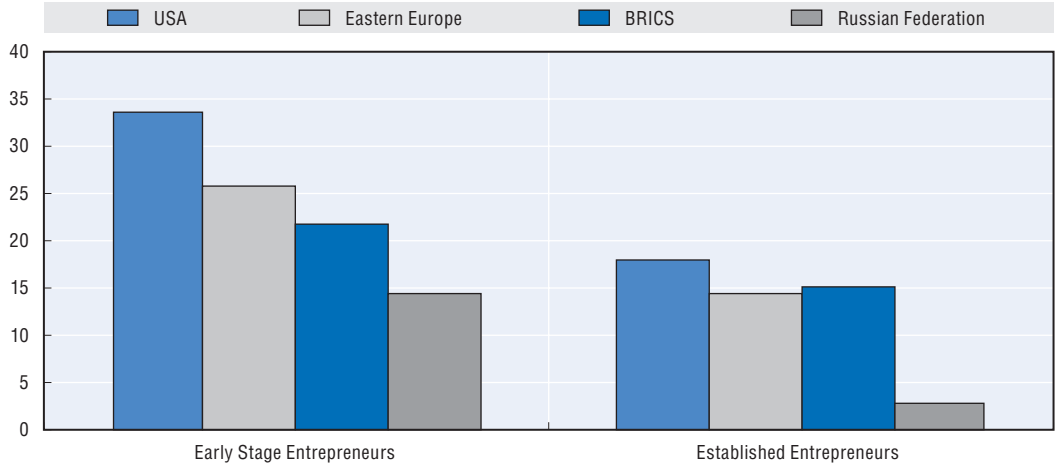
Figure 2.8. **Index of novelty of products/intensity of competition of early-stage and established entrepreneurs across countries, 2012**



Note: To measure a country's potential for innovation an index is used from a combination of indices of product novelty and intensity of competition. This reflects a quantity of entrepreneurs who consider that their product or service is new and novel for all or several consumers and at the same time has little or no competition.

Source: Verkhovskaia and Dorokhina (2013) National Report Global Entrepreneurship Monitor Russia 2012, p. 41.

StatLink *http://dx.doi.org/10.1787/888933271768*

In addition, 72.5% of early-stage and 87.9% of established entrepreneurs in the Russian Federation reported that they were offering products and services that were not that new for consumers in 2012 (a proportion that had been increasing) while 94.3%

of established entrepreneurs and 89.5% of early stage entrepreneurs did not use newer technology in their business activity (Verkhovskaia and Dorkhina, 2013). On the basis of a composite index that takes together the novelty of products and the degree to which they do not have direct competitors, Figure 2.9 indicates that both early-stage and established entrepreneurs in the Russian Federation tend to be substantially less innovative in their products and services than their counterparts in the USA, Eastern Europe and BRICS countries.

In contrast, Russian businesses appear to be very active in their use of the internet; by 2012, two-thirds of surveyed businesses were using their own websites, compared with less than one-half in ECA and Upper Middle Income countries (World Bank/IFC, 2012).

High-growth entrepreneurship

There is substantial international evidence that in any cohort of firms a minority of rapidly-growing SMEs typically generate a majority of the new jobs (OECD, 2010). In some countries, they also tend to be associated with better export performance. These two features make them an important target of policy. Unfortunately, there are no official statistics on high-growth enterprises in the Russian Federation. However, according to GEM data for 2012, entrepreneurs expecting to create more than 20 jobs in the five years after business creation represented 0.46% of the adult population in the Russian Federation in 2014, compared with 0.40% in Brazil, 0.28% in Mexico, 1.01% in China and 2.89% in the United States. Put in other terms, according to GEM data for 2011, of those involved in entrepreneurship activity, 9.8% of entrepreneurs in the Russian Federation expected to employ 20 people in 5 years' time compared to 1.5% in Mexico, 2.3% in Brazil, 6.5% in China and 21.0% in the USA. It is important that these entrepreneurs in the Russian Federation are given the opportunities to achieve their growth ambitions. In this respect, a separate study (Morris, 2011) found that the median turnover growth rate of high-growth aspiration entrepreneurs in their most recent full year of trading was 453% in China, 269% in South Africa, 311% in Brazil, and 216% in India but only 150% in the Russian Federation, suggesting that high-growth entrepreneurs in the Russian Federation have been finding it more difficult to achieve their aspirations than in other BRIC countries.

Conclusions and recommendations

There is tremendous under-exploited potential in SME and entrepreneurship activity in the Russian Federation, demonstrated by substantial shortfalls with OECD, ECA and emerging economies in numbers of SMEs per head of population, employment in small businesses, rates of new business start-ups, and levels of SME investment and innovation. Making up these shortfalls can be expected to have a dramatic impact on the Russian Federation economy, in terms of substantial job creation and income generation, increased investment, competition and productivity and a diversification of the economic base away from its current dependence on commodity exports. One of the strengths that is already there to build on is that entrepreneurship in the Russian Federation already has a relatively good gender balance, although there is still some ground to make up in the female rate of entrepreneurship relative to that for males.

One of the challenges will be to improve the attitudes to entrepreneurship in Russian society. At only 3% of the population, the proportion of adults in indicating an intention to start a business in the Russian Federation is one of lowest internationally. In addition, a majority of non-entrepreneurs doubt that they have sufficient knowledge and experience to undertake entrepreneurial activity and have a relatively strong fear of failure. Changing long-established attitudes is a challenging prospect for Russian policy makers but a necessary one if entrepreneurship is to gain the legitimacy it needs to become embedded in Russian society and economy.

Another issue to address is dependency of many Russian households on a sizable informal sector. The large scale of informality reflects a number of institutional deficiencies, and reducing the size of the informal economy will require more than a systematic approach to policing it but rather measures to tackle its causes. Efforts should also be gradual and careful, since it needs to be recognised that informal activity is currently providing jobs and contributing to reducing social and economic exclusion at least in the short term.

SME innovation rates are also relatively low in the Russian Federation, as measured by rates of product/process innovation and rates of marketing/organisational innovation and by the novelty value of the products and services of Russian enterprises for their customers. Improving the innovative performance of SMEs is one of the most important current policy priorities the Russia Federation, which is crucial to future competitiveness. In addition, there is some evidence that growth-orientated entrepreneurs in the Russian Federation find it more difficult to achieve their aspirations than in other BRICS countries. Developing a more substantial high-growth firms sector in the Russian Federation is a further key policy challenge.

In order to meet these challenges, the following key policy recommendations are offered:

Key policy recommendations on SME and entrepreneurship performance

- Increase numbers of SMEs and their employment through a combination of extensive measures aimed at increasing the level of entrepreneurship across the population and more targeted and specialised support for growth-oriented entrepreneurs and enterprises.
- Promote growth of manufacturing SMEs in particular by increasing the focus of SME programmes on innovation, exporting and investment in physical and human capital and setting targets for the participation of manufacturing SMEs in these programmes.
- Promote positive attitudes to entrepreneurship through a national entrepreneurship awareness campaign involving the media and comprehensive integration and teaching of entrepreneurship teaching across the educational system.
- Facilitate transfers of entrepreneurial activity from the informal to the formal economy by removing undue obstacles to formal entrepreneurship in the tax and regulatory system and supporting informal entrepreneurs to upgrade their businesses and tap into new sources of demand.
- Increase SME innovation across all sectors by building the innovation and growth capacities of new and existing enterprises and their management teams.

Notes

1. The notion of efficiency-driven economies is used by the World Economic Forum and others such as GEM to indicate countries in an intermediate stage of economic development (between factor-driven and innovation-driven development), where further growth is strongly connected to increases in the efficiency of production process and product quality
2. The information in this document with reference to « Cyprus » relates to the southern part of the Island. There is no single authority representing both Turkish and Greek Cypriot people on the Island. Turkey recognises the Turkish Republic of Northern Cyprus (TRNC). Until a lasting and equitable solution is found within the context of the United Nations, Turkey shall preserve its position concerning the "Cyprus issue".
3. The Republic of Cyprus is recognised by all members of the United Nations with the exception of Turkey. The information in this document relates to the area under the effective control of the Government of the Republic of Cyprus.

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Chapter 3

Business Environment For SMEs and Entrepreneurship in the Russian Federation

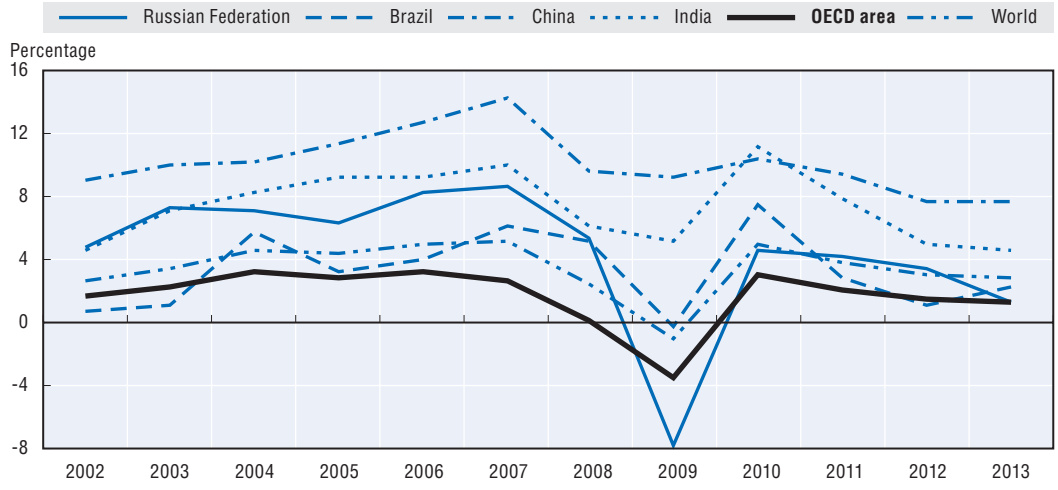
This chapter examines the quality of national framework conditions for SMEs and entrepreneurship in the Russian Federation, covering macro-economic conditions, international market integration, competition and state ownership, public procurement, the administrative burden, tax and social security, transparency and the rule of law, human resources, physical infrastructure the innovation system and access to financing. The state has made several important improvements across these areas that will ease SME and entrepreneurship development. A number of further policy reforms are recommended for example in the areas of reducing state control in the economy, strengthening transparency in public dealings with enterprises, building a skilled SME workforce and commercialising public research.

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Macroeconomic conditions

The macro-economy has an important influence on SME and entrepreneurship development through its influence on factors such as the level and stability of demand and investment. The early days of transition from Socialist planning were characterised by macro-economic instability, which encouraged entrepreneurs to focus on activities that generated quick returns rather than invest in activities, such as manufacturing, where a longer time horizon was necessary on the part of investors. However, from the mid-1990s the Russian Federation started to experience long-run stable economic growth, before the global financial and economic crisis had its impact. As Figure 3.1 shows, the 2008-09 recession affected the Russian Federation to a much greater extent than other major emerging economies, reflecting a rapid downturn in commodity demand and a severe deterioration in Russian bank liquidity, which gave rise to a need for the introduction of exceptional financing measures to support SMEs.

Figure 3.1. **Annual GDP growth rates**



Source: OECD Economic Outlook Database. *http://dx.doi.org/10.1787/na-data-en.*

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A broad-based macro-economic growth had resumed by 2010 at a rate of around 4% per annum. This was accompanied by a large trade-balance surplus, which may promote public and private investment, low inflation and increasing domestic consumption, which is likely to bring new entrepreneurial opportunities. The growth rates following the global financial crisis nonetheless did not match those achieved in the immediate pre-crisis period, in part reflecting a slow recovery of fixed investment and slow growth in major markets such as Europe. Furthermore, recent geopolitical tensions have brought import and export restrictions in certain sectors, rising inflation, a falling exchange rate and forecasted negative growth. These issues represent a significant short-term challenge for SME and entrepreneurship development in the Russian Federation but do not put into

question the need for a longer term structural adjustment programme based on SME and entrepreneurship promotion that will target job creation, productivity increases and the diversification of the economy.

Trade and international market integration

Dependency on natural resource exports

One of the most important features of the Russian Federation economy today is its heavy dependence on commodity exports in global markets for natural gas, oil, steel and primary aluminium. As Table 3.1 shows, the Russian Federation has been running a current account surplus for a number of years. Its main exported goods are petroleum and petroleum products, natural gas, metals, wood and wood products, chemicals and a variety of other manufactured goods. Its main export markets are the Netherlands, China, Italy, Germany and Poland.

The Russian Federation's strong natural resources exports, particularly from minerals and energy, present an important opportunity for revenues to be used to sow the seeds of diversification, for example by allocating a fixed part of the receivables from non-renewable resources to productive investments, including SME and entrepreneurship development projects.

The need for diversification is underlined by a negative and worsening non-oil current account balance, which reflects substantial deficits in services and investment income, and a recent drop in revenues from energy exports reflecting a fall in global oil and gas prices. Furthermore, the capital and financial account has been negative, which may reflect concerns about the quality of the investment climate for direct and portfolio investment.

Table 3.1. **Balance of Payments 2007-13**

USD billion

	2007	2008	2009	2010	2011	2012	2013
Current account balance	77.8	103.9	50.4	67.5	97.3	71.3	34.1
Trade balance	130.9	177.6	113.2	147.0	196.9	191.7	181.9
Non-oil current account balance		-206.2	-140.3	-186.6	-244.5	-275.5	-316.1
Capital and financial account	84.5	-139.8	-40.6	-21.6	-76.0	-30.9	-45.4
Errors and omissions	-13.3	-3.1	-6.4	-9.1	-8.7	-10.4	-10.8
Change in reserves (- = increase)	-148.9	38.9	-3.4	-36.8	-12.6	-30.0	22.1
Memo: average oil price (Brent, USD/barrel)	72.5	96.9	61.5	79.7	111.1	112.0	108.9

Source: World Bank (2014), Confidence crisis exposes economic weakness. Russian economic report ; no. 31. Washington, DC ; World Bank Group. *http://documents.worldbank.org/curated/en/2014/03/19357185/confidence-crisis-exposes-economic-weakness* World Bank (2013) Russian economic report : recovery and beyond. Russian economic report ; no. 29. Washington DC : World Bank. *http://documents.worldbank.org/curated/en/2013/01/17389712/russian-economic-report-recovery-beyond*.

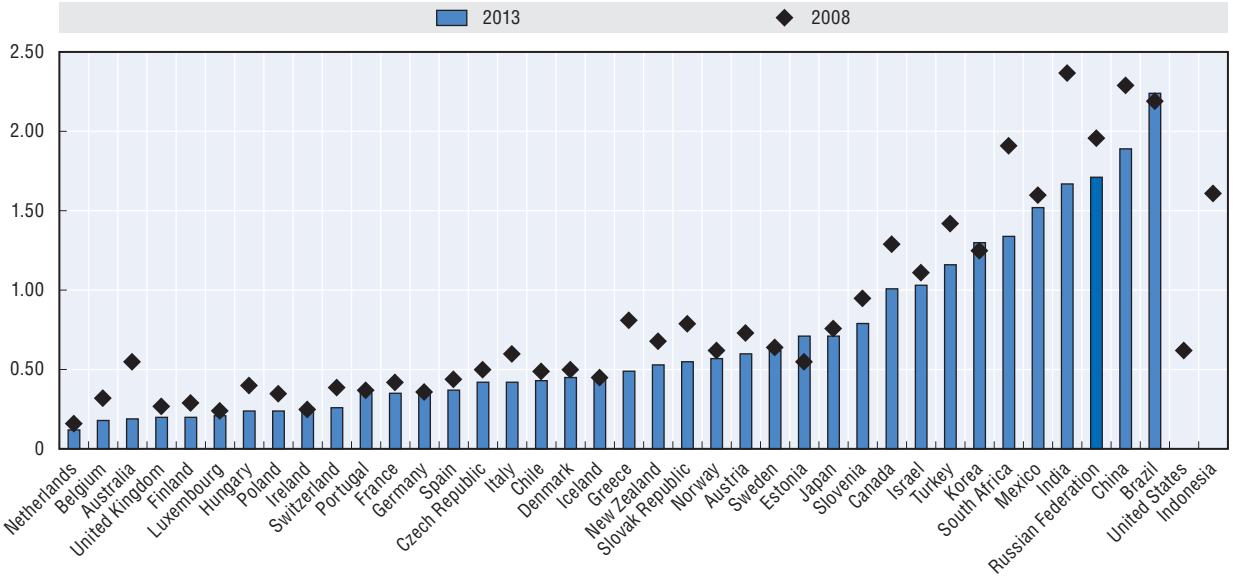
StatLink http://dx.doi.org/10.1787/888933272274

Foreign trade and investment restrictions

There are significant barriers to foreign trade and investment in the Russian Federation. These restrictions limit the competitive spur which helps drive efficiency improvements in domestic SMEs together with their ability to engage in global markets and knowledge transfers as suppliers or partners to domestically-located foreign firms. Figure 3.2 provides an overview of the scale of the barriers overall. While improvements have been made over the last 5 years, the barriers to foreign trade and investment in the Russian Federation are still greater than any OECD economy and only slightly less restrictive than China and Brazil.

Figure 3.2. **Product market regulation indicator: barriers to foreign trade and investment**

2008 and 2013, index scale from 0 to 6 from least to most restrictive



Note: The indicator covers barriers to foreign trade and investment in two areas: explicit barriers to trade and investment (barriers to FDI, tariff barriers) and other barriers to trade and investment (differential treatment of foreign suppliers, barriers to trade facilitation).

Source: OECD Product Market Regulation database *http://dx.doi.org/10.1787/pmr-data-en*.

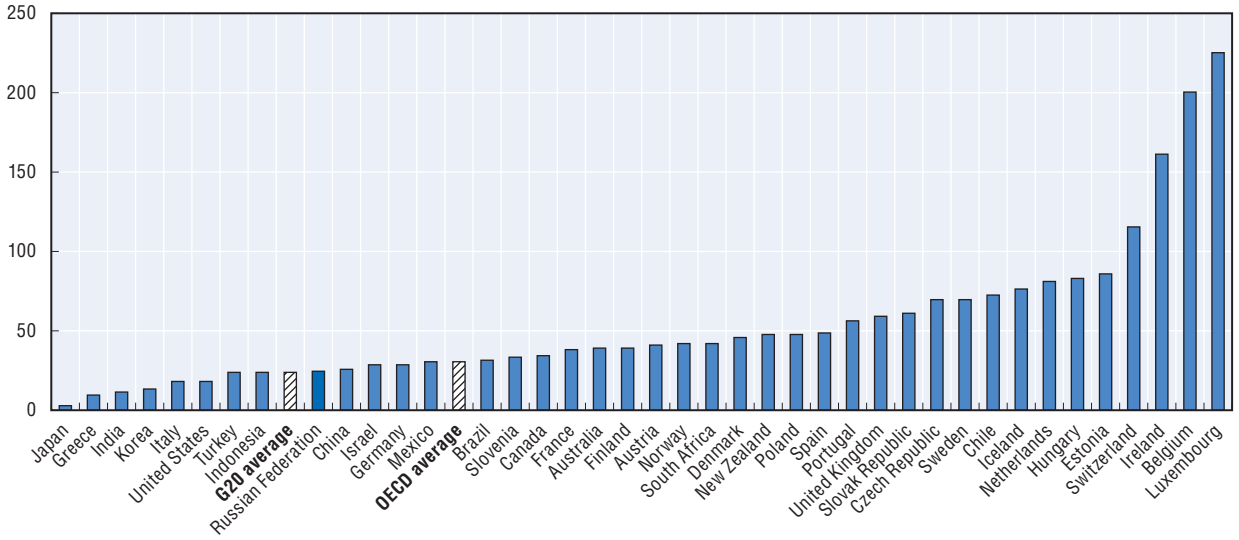
StatLink *http://dx.doi.org/10.1787/888933271785*

With respect to trade, the Russian Federation ranks only 105th of 138 economies in the World Economic Forum's 2014 Enabling Trade Index. Problem areas include the efficiency of the customs clearance process, the number of documents required to import or export and domestic market access, which reflects high, widespread and complex tariffs. On the other hand, the Russian Federation performs somewhat better with respect to foreign market access, availability and quality of transport infrastructure and transport services and the availability and use of information and communications technologies (WEF, 2014).

On the face of it, foreign direct investment (FDI) inflows to the Russian Federation appear relatively healthy. OECD international direct investment statistics show that FDI inflows to the Russian Federation amounted to some USD 54 billion in 2013 representing 2.6% of GDP. This compares with an OECD average of 1.3% and a G20 average of 1.6%. Similarly, the Russian Federation's inward FDI stock was estimated at 24.5% of GDP in 2012. Although this is somewhat below the OECD average of 31.1% it is in line with the G20 average (Figure 3.3). Caution is needed in interpreting this information however, because FDI inflows appear to have dropped in 2014 and because over 60% of reported FDI is the result of "round tripping", with Russian owners structuring firms as international conglomerates, usually as a response to institutional constraints within the Russian Federation, such as weak regulatory policies and financial markets (OECD, 2014a). Furthermore, the OECD's FDI regulatory restrictive index shows that the climate for foreign investment in the Russian Federation is relatively restrictive compared with the OECD average (Figure 3.4), although it is less restrictive than countries like China, India, Japan and Mexico, and substantial progress has been made since 2006. The barriers tend to be relatively high in certain key sectors, namely transport, media, financial services, real estate investment and mining.

Figure 3.3. **Inward FDI stock, selected countries, 2012**

Percentage of GDP

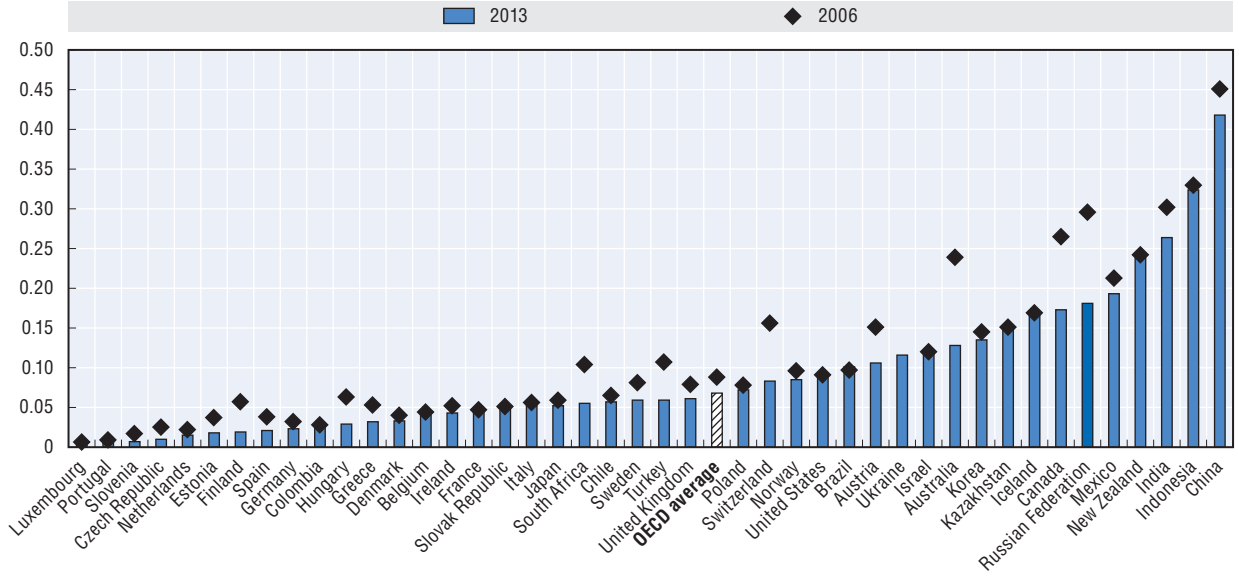


Source: OECD (2014b) International Direct Investment Statistics 2014, DOI: *http://dx.doi.org/10.1787/idis-2014-en*.

StatLink *http://dx.doi.org/10.1787/888933271795*

Figure 3.4. **FDI Regulatory Restrictiveness Index**

2006 and 2013, index scale 0-1 from least to most restrictive



Source: OECD, FDI Regulatory Restrictiveness database. *http://stats.oecd.org/Index.aspx?datasetcode=FDIINDEX*.

StatLink *http://dx.doi.org/10.1787/888933271808*

In order to increase FDI inflows and exploit its potential to support technology and market upgrading in the SME sector attention should be paid to reducing legal barriers such as the need for foreign investors to obtain operating licenses and quotas on the extent of permitted foreign ownership of the share capital of Russian businesses operating in strategic sectors (these restrictions have recently been lifted in the case of investments in SMEs but remain on larger firms). At the same time, improved information should be made

available to foreign investors on rules and procedures, including on the internet and in national and local investment promotion offices.

Increasing competition through WTO engagement

The Russian Federation joined the World Trade Organisation (WTO) in August 2012, following 18 years of negotiation. Under the terms of accession, the Russian Federation will gradually lower a number of import duties on agriculture and manufacturing goods by around 2 to 3 % on average over a phase-in period that will run until 2020. After the phase-in period, the Russian Federation's average bound tariff will be reduced from 11.9% to 7.1% (OECD, 2014a). Restrictions on foreign entry in the service sectors will also be relaxed, including insurance and telecommunications, future agriculture subsidies will be reduced and non-discriminatory tariffs will be introduced on trans-shipment of goods through the Russian Federation. At the same time, a Eurasian customs union including the Russian Federation, Belarus and Kazakhstan came into existence in 2010, leading towards a Eurasian Economic Union in 2015 providing for the free movement of goods, services, capital and labour between these three countries and the Republic of Armenia.

The anticipated increases in international market integration will have two major implications for the Russian SME and entrepreneurship sector; increased access to external markets and increased international competition in domestic markets. In this context, it is important to implement policies and programmes that will support domestic SMEs to increase their productivity and international outlook. There are also some implications for the scope and resourcing of Russian SME and entrepreneurship policy since WTO membership places some restrictions on how far governments can subsidise businesses that are competing internationally. In addition, businesses within the territories that are part of the Eurasian Economic Union should also be treated in the same manner. This means, for example, that the current attempts to open up public procurement to SMEs must apply to all SMEs within the union and not just to Russian SMEs.

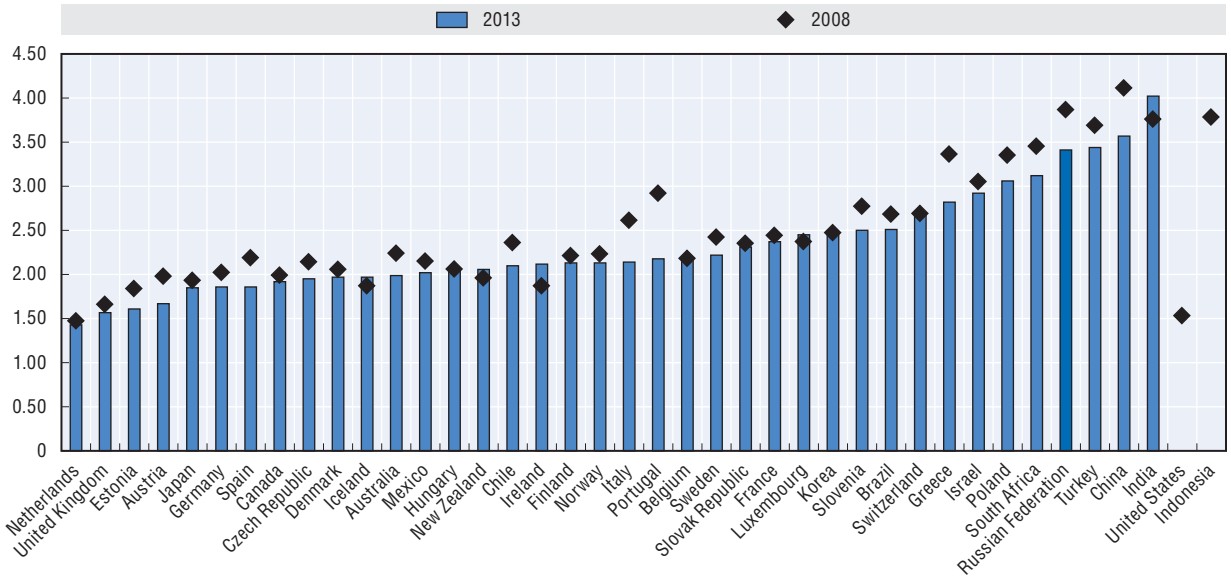
State ownership and product market competition

A long-standing challenge facing policy makers in the Russian Federation is to manage the continued transformation of a centrally-planned economy into a market-based system by promoting competition where previously there was state monopoly. A market reform process has been underway since the beginning of the 1990s, which has led to substantial privatisations of state activity in many sectors of industry and agriculture. However, high levels of state control and barriers to product market competition remain, which contributes to the slow pace of SME and entrepreneurship development.

Substantial state control

Figure 3.5 illustrates the major role that the state continues to play in the Russian Federation economy through public ownership and command and control regulation affecting non-state enterprises. The level of state control in the Russian Federation is estimated to exceed that of any OECD economy except Turkey as well as certain other key emerging economies such as South Africa and Brazil, although the state influence is not as large as in China, India and Indonesia. For example, state-owned enterprises account for more than 80% of sales, assets and market values of the top ten firms of the Russian Federation and occupy the dominant position in sectors such as banking, transport and energy.

Figure 3.5. **Product market regulation indicator: state control**
2008, index scale from 0 to 6 from least to most restrictive



Note: The indicator covers state control in the economy in two areas: public ownership (scope of state-owned enterprises, government involvement in network sectors, direct control over enterprises, governance of state-owned enterprises) and involvement in business operations (price controls, command and control regulation).

Source: OECD Product Market Regulation database. *http://dx.doi.org/10.1787/pmr-data-en.*

StatLink *http://dx.doi.org/10.1787/888933271810*

The level of state control is gradually reducing, and a presidential decree in May 2012 set the objective of a full withdrawal of the state from all companies except natural monopolies and the energy and defence sectors by 2016 (OECD, 2014a). Thus the privatisation plan for 2011-13 foresaw the sale of 1 500 state-owned enterprises (SOEs), including several large companies in key sectors, such as banking, telecommunications and transport. Furthermore, the number of state stakes in unitary and joint stock enterprises fell from approximately 6 500 to approximately 4 100 between 2010 and 2013 (OECD, 2014a). This has provided important opportunities for the privatisation of smaller SOEs. In addition, legislation is currently being considered to restrict the establishment of new state-owned enterprises, especially at regional and local levels.

More physical spaces are also being made available to private firms as business premises. These have traditionally been owned by the state as a legacy of the Soviet regime. To this effect, the federal Small Privatisation Law of 2008 allows SMEs to benefit from the privatisation of State and municipal property. Within this framework, more than 33 000 SMEs became owners of premises during 2008-13, with a total area of about 5 million square meters. In addition, over 80 000 municipally registered state-owned properties are available for lease by SMEs, with government subsidies offered to partially cover the costs of the initial lease payments (SMEs pay only 40% of the lease rate in year one, 60% in year two, and 80% in year three, to a maximum of RUB 1 million per beneficiary firm). It is important to continue to implement this programme of privatisation of state enterprises and reductions of state control in order to provide opportunities for SMEs and entrepreneurship development.

Need to pursue promotion of competition

The market entry and growth of new and small firms in the Russian Federation is also hindered by significant levels of monopoly power and the presence of anti-competitive practices by incumbent firms such as non-compliance with established contract deadlines or agreements with other established businesses to restrict competition. In addition to national monopolies, the large geographical size of the Russian Federation lends itself to the emergence of important local monopolies.

Again, the Russian Federation government has an active programme to promote product market competition. This process was accelerated in 2009 by the introduction of a "competition road map" focused on a series of actions to improve antimonopoly legislation and the technical mechanisms for implementing it. Further road maps have been introduced, the most recent, in 2013, introducing principles of reform covering cartels, mergers, structural separation in regulated industries, market regulation, and intellectual property rights.

The state agency responsible for the implementation of competition policy is the Federal Anti-monopoly Service (FAS), with central administration in Moscow and territorial offices throughout the regions. However, it experiences a number of difficulties in enforcing competition regulations. One of the issues is the need to investigate and judge a very large case load. The 2013 road map responded in part to this problem by removing some of the smaller cases through an automatic instrument to sanction repetitions of competition abuse but further intervention is needed to boost the scale of the FAS. Another issue concerns a lack of depth and spread of technical expertise within FAS in making economic assessments of the degree and impacts of competition abuse and an overly theoretical approach, which can lead to onerous applications of competition policy. This could be addressed by the introduction of further analytical guidelines together with capacity-building efforts to train professionals and create an infrastructure for the effective implementation of competition policy. In addition, there has been patchy implementation of competition law across the country and attention should be paid to encouraging a level application of competition policies in all regions. Another issue concerns the need to reform attitudes and traditions of behaviour of public institutions and their officials. For example, the practice of giving informal preferences to certain companies, in particular at the regional and municipal levels, is a distortion of free competition.

Access to public procurement

The public procurement market, including federal, regional and municipal governments and state-owned enterprises and their subsidiaries is worth about RUB 13 trillion per year in the Russian Federation, and hence represents an important potential tool for SME and entrepreneurship promotion. This potential was first explicitly recognised by a federal law of 2005 specifying that between 10% and 20% of state and municipal public procurement contracts should be awarded to small businesses, defined as enterprises with fewer than 100 employees and annual turnover of less than RUB 400 million. In addition, the legislation specified that the security to be required for participation in procurement exercises to be carried out among small businesses should not exceed 2% of the initial price.

More recently, further legislation has been introduced to support SME access to public procurement. In 2009, a government regulation fixed the value of individual contracts offered to small businesses at less than RUB 15 million in order to make it more feasible for small firms to submit bids and to ensure that they were competing against each other and not with large businesses.[1] In 2011, a new federal law extended the provisions of the 2005 law to the procurement policies of state-owned enterprises and their subsidiaries.

A further major step forward came in 2013, when a separate section of a new law on procuring goods, works and services for state and municipal needs (Section 29) was introduced on the participation of small businesses. While the 2005 law had already contained a provision for SMEs, the new legislation includes a number of innovations:

1. The new law states that the quota for procurement from small business must be not less than 15% of the aggregate annual procurement volume provided for by the procurement schedule, whereas the previous quota was not less than 10% and not more than 20%. According to the national statistical office, the share of procurement orders placed solely with small enterprises was 11% at state level and 12% at municipal in 2012. The new threshold will therefore lift the proportion of orders going to small enterprises.
2. While the small business quota was formerly computed on the basis of a prescribed list of goods, works, and services to be procured from small businesses, this list was abolished. This will reduce complexities in interpreting precisely which goods, works and services can be procured from small businesses.
3. The maximum value of individual contracts offered to small businesses will be increased from the previous ceiling of not more than RUB 15 million to an amount not to exceed RUB 20 million.
4. Procurement departments will be obliged to make a report on the volume of procurement of goods, works and services from small businesses, including information on concluded contracts and failed purchases.
5. A so-called "second-hand" rule was introduced, which entitles the procuring department to require that larger contractors engage small businesses as subcontractors and/or joint contractors for the performance of the contract.

At the same time, the federal government approved a road map for measures to expand the access of SMEs to procurement by state-owned enterprises to be carried out during the period 2013-18. The road map sets out measures to remove administrative, financial and information barriers for SMEs in accessing SOE contracts with the aim of increasing their share from 10% to 25% of direct procurement and from 2% to 5% of the share of procurement of innovative products, research and development, and technological work.

The government's new SME procurement quotas and procedural simplifications are very promising developments. In order to translate the targets into reality on the ground, complementary information and training should be offered to SMEs on how to successfully access public procurement contracts.

Administrative burden and regulation

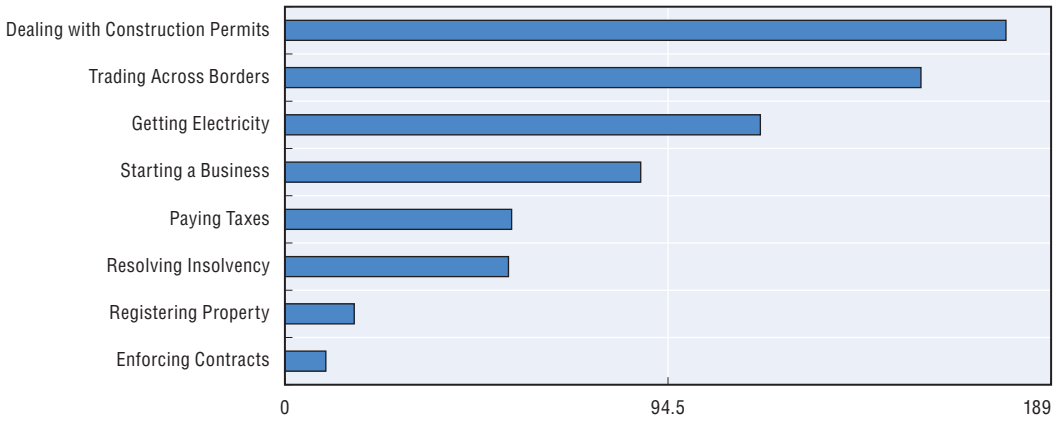
Reducing administrative burdens

The Russian Federation ranked very well on the World Bank's 2014 Ease of Doing Business index with respect to the indicators concerned with the ease of contract enforcement and registering property and also ranked within the top one-half of countries for the administrative simplicity of paying taxes, resolving insolvency, and starting a business. On the other hand its performance was relatively poor with respect to measures of getting electricity, trading across borders and dealing with construction permits (Figure 3.6).

The Russian Federation's current frequently very good rankings are the result of some significant improvements in recent years. Thus its overall ranking (taking all the Doing Business indicators together) improved from 120 in 2009 to 92 in 2014. Considerable progress

has also been made in reducing the number of days taken to start a business, which fell from 43 in 2004 to 15 in 2014 (Figure 3.7). Although the Russian Federation is still slightly behind the OECD and ECA averages on this measure (11 and 13 days respectively), it is now considerably ahead of some other emerging economies such as Brazil and Indonesia. Furthermore, the administrative cost of starting a new business is very low in the Russian Federation, at 1.3% of average income per capita compared with an average of 6.7 in ECA countries as a whole and 3.6% in OECD countries (World Bank/IFC, 2014).

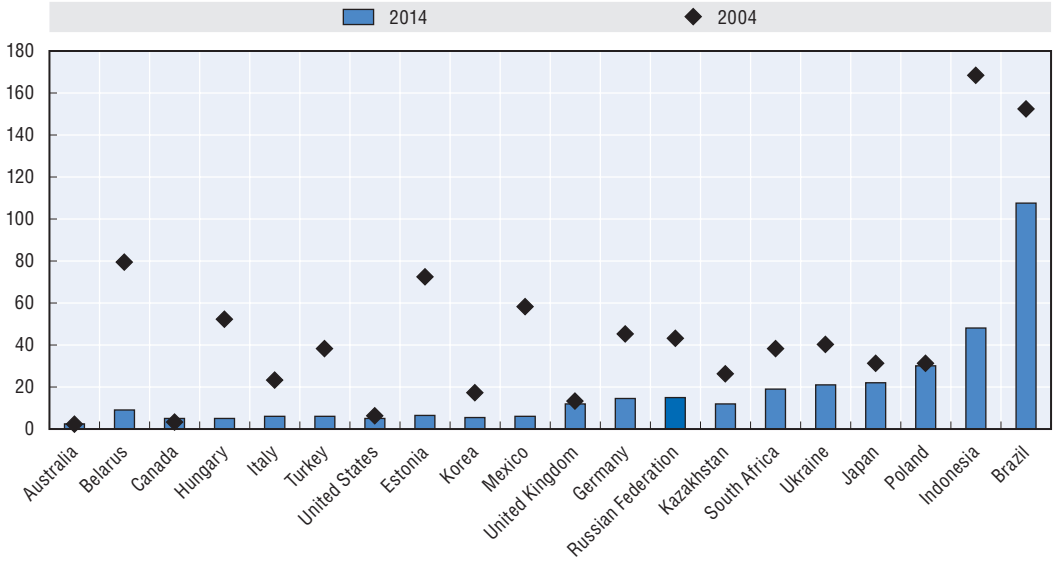
Figure 3.6. **Russian Federation ranking on selected administrative burden indicators, 2014**



Source: World Bank/IFC (2014), Doing Business 2014: Understanding Regulations for Small and Medium-Size Enterprises. Washington, DC: World Bank Group. DOI: *http://10.1596/978-0-8213-9984-2.*

StatLink *http://dx.doi.org/10.1787/888933271825*

Figure 3.7. **Average number of days required to deal with administrative procedures to start a business**



Source: World Bank/IFC (2014) Doing Business 2014: Understanding Regulations for Small and Medium-Size Enterprises. Washington, DC: World Bank Group. DOI: http://10.1596/978-0-8213-9984-2.

StatLink *http://dx.doi.org/10.1787/888933271831*

The Russian Federation's strong performance in certain key areas of government administration of businesses and its recent improvements have been driven by the implementation of several administrative simplification reforms between 2006 and 2014 (Table 3.2).

Table 3.2. **Number of administrative reforms in the Russian Federation, 2006-14**

Indicator	2014	2013	2012	2011	2010	2009	2008	2007	2006	TOTAL
Starting a business	1							1	1	3
Construction permits	1	1		1						3
Registering property	1		1		1					3
Paying taxes		1			1			1		3
Trading across borders	1		1						1	3
Enforcing contracts			1							1
Resolving insolvency				1	1					2
Total	4	2	3	2	3	0	0	2	2	18

Source: World Bank/IFC (2014) Doing Business 2014: Understanding Regulations for Small and Medium-Size Enterprises. Washington, DC: World Bank Group. DOI: 10.1596/978-0-8213-9984-2.

StatLink http://dx.doi.org/10.1787/888933272281

Since 2011, the reform effort has been spearheaded by the Agency for Special Initiatives to Promote New Projects (ASI); a non-government body chaired by the President of the Russian Federation, set up in response to a presidential commitment to improve the Russian Federation's rank on the World Bank Doing Business indicators to number 20 by 2020. The ASI has introduced a "100 steps" platform linked to reform roadmaps in the following areas:

1. Accessibility to energy infrastructure.
2. Business climate in the construction sector.
3. Customs administration.
4. Quality of public services regarding state cadastral registration of immovable property and state registration of immovable property rights and transactions.
5. Procedures for the registration of businesses and the self-employed.
6. Competition and antitrust policy.
7. Access to foreign markets and export promotion.
8. SME access to the procurement of SOEs.
9. The regulatory environment for business.

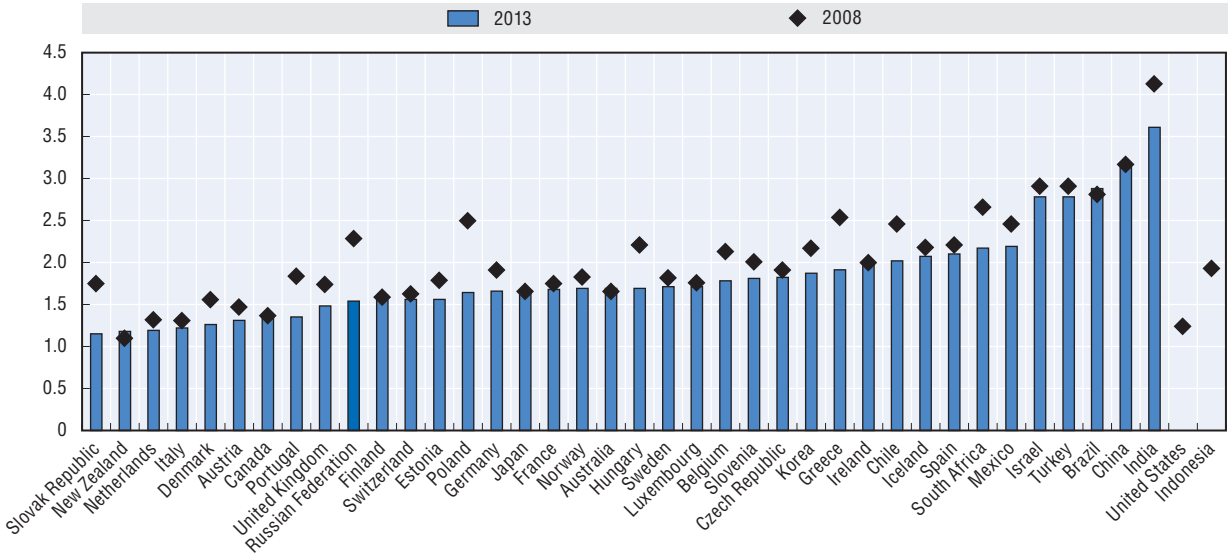
The improvements that have been made as a result of all these efforts include establishment of one-stop shops for firm registration in several pilot regions, abolition of the requirement to have a bank signature card authorised before opening a company bank account, a new licensing law that has reduced the number of licensed activities and made licence duration indefinite, an electronic court case filing system to accelerate legal proceedings for enforcing contracts, accelerated liquidation procedures upon bankruptcy, an electronic system for submitting export and import documents and a reduction in the number of physical inspections, reduction of the number of tax payments to be made per year, simplified compliance procedures and claims for exemption from value added tax and promotion of the use of tax accounting software and electronic services for business taxation, and streamlined procedures and effective time limits for processing property transfer applications. The latter included a law in 2008 that unified the management of ownership registration and land cadastre in a new Federal Service of Registration and Cartography.

As shown in Figure 3.8, the OECD's Product Market Regulation index confirms the substantial progress made in reducing administrative and regulatory barriers to entrepreneurship over the last 5 years, and the relatively good performance

already achieved in the Russian Federation compared with many OECD and emerging economies.

Figure 3.8. **Product Market Regulation Indicator: Barriers to Entrepreneurship**

2008, index scale of 0-6 from least to most restrictive



Note: The indicator covers barriers to entrepreneurship in three areas: complexity of regulatory procedures; administrative burdens on start-ups and regulatory protection of incumbents.

Source: OECD Product Market Regulation Database. *http://dx.doi.org/10.1787/pmr-data-en.*

StatLink *http://dx.doi.org/10.1787/888933271847*

However, there is still a long way to go to achieving the government's target of becoming one of the countries in the world with the least administrative burdens on business and this will require continued work to put into action the steps set out in the ASI road maps.

Particular emphasis will need to be paid to improving the areas of administration on which the Russian Federation has continued to rank poorly; namely dealing with construction permits, trading across borders and getting electricity. The administrative burden estimated by the World Bank in terms of construction permits in 2014 was estimated to involve some 36 procedures, take some 297 days on average and cost some 89% of average income per capita. Similarly, it is estimated that SME managers needed to complete 9 administrative procedures to export, taking an average of 22 days, while importing required 10 administrative procedures and 21 days. Although, the Russian Federation's ranking on getting electricity improved substantially (from 188 to 117) between 2013 and 2014 by setting standard connection tariffs and eliminating many procedures previously required, it still involved 5 procedures, an average of 162 days and cost approximately three times average per capita income to get a connection to electricity in 2014. Regulatory reform efforts should focus in particular on making further improvements in these problem areas.

In addition, given the relatively widespread use of the Internet by Russian businesses, there is an important opportunity to facilitate administrative compliance for SMEs by making greater use of business-related e-services, such as online registration, on-line tax declarations and on-line reporting.

New regulatory impact assessment procedures

The federal Ministry of Economic Development set up a regulatory impact assessment (RIA) department in 2010 in order to review draft federal legislation that affects business regulation. This department has since performed more than 1 800 assessments, with around 35% of them identifying problems that required changes in the law (OECD, 2014a). A preliminary assessment takes 5 days. If it finds that a given regulation could potentially have a negative influence on the business environment, a more detailed cost and benefit study is carried out within one month, which includes public hearings. The government is then asked to modify the draft legislation, although it cannot be required to do so as a result of the RIA findings. A further improvement would be to extend the regulatory review procedures to cover existing government laws and regulations that may affect SMEs and entrepreneurship, in addition to proposed new legislation. Another would be to set up a system to enforce the RIA; since experience in other countries shows that implementation can be difficult because of the number of government departments involved in passing regulations which impact on business. Ideally such a body would report direct to the President of the Russian Federation.

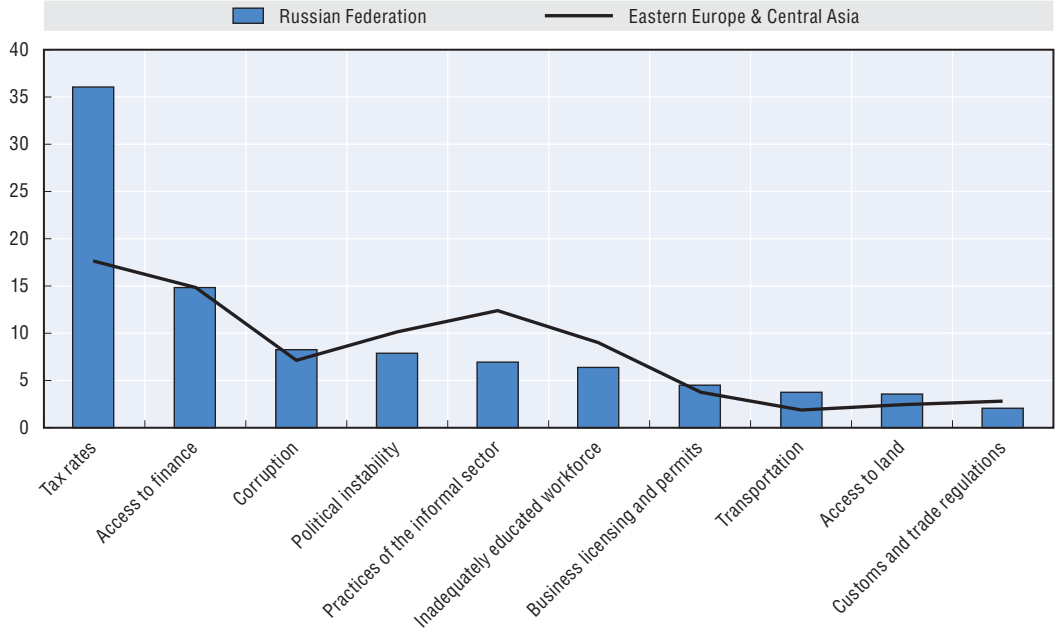
Taxation and social security system

High tax burden on SMEs

Many businesses report tax rates to be the most important barrier to their operation in the Russian Federation. As shown in Figure 3.9, more than one-third of SME owners and managers identified tax rates as a major obstacle in the World Bank's 2012 Enterprise Survey, twice as many as the next most commonly identified barrier (access to finance)

Figure 3.9. **Business environment problems reported by Russian Federation enterprises, 2012**

Percentage of firms identifying the problem as the main obstacle to their business operations



Source: World Bank/IFC (2012) Enterprise Surveys: Russian Federation Country Profile 2012. Washington DC World Bank Group.

StatLink http://dx.doi.org/10.1787/888933271859

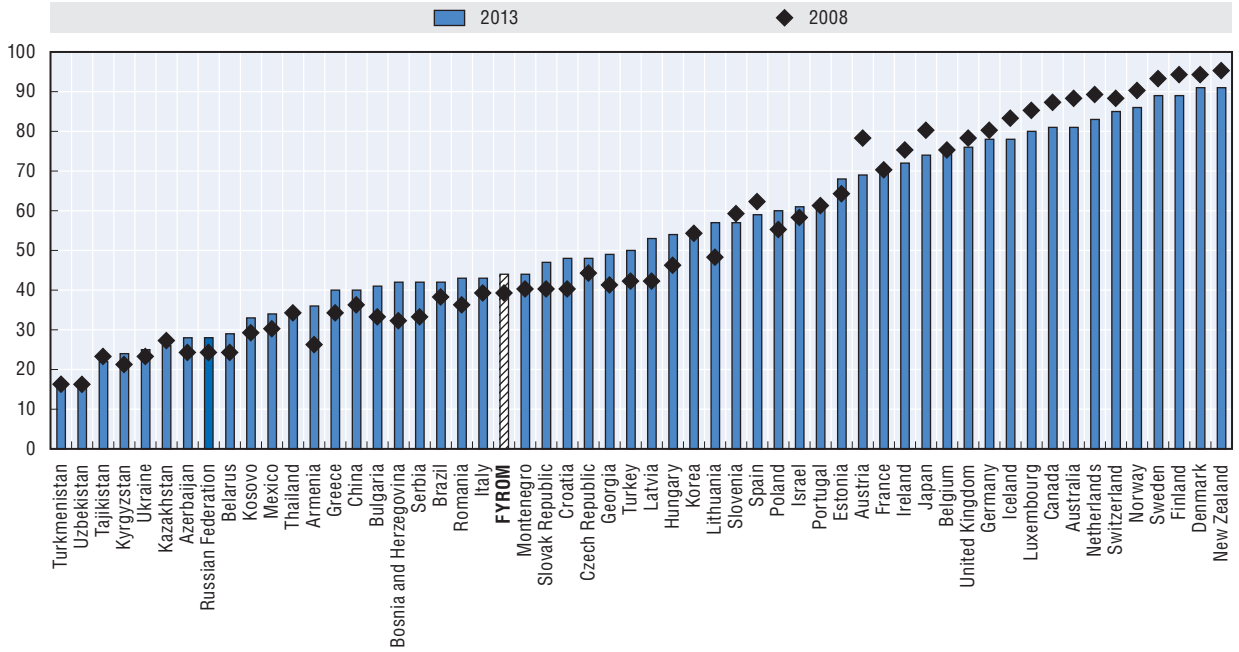
and twice as many as in ECA countries as a whole. The problem appears to reflect the combined effects of corporate taxation and social security payments. Improvements have nevertheless been made. According to World Bank data, the total tax rate as a percentage of profit fell from 60.0% to 50.7% between 2006 and 2014 in the Russian Federation. In particular, the headline corporate income tax rate was reduced from 24% to 20% in 2010, although in 2012 the social security contribution rate from employers was increased.

Transparency and the rule of law

Creating a corruption-free business environment

As countries transform from central planning to market-based systems, one of the biggest challenges has proven to be institutional change to secure transparent and corruption-free business regulation. Figure 3.10 shows the Russian Federation's position on Transparency International's Freedom from Corruption Index compared with selected OECD, ECA and emerging economy countries. The Russian Federation's score is poorer than any OECD country and worse than the key emerging economies of Brazil and China, even though the Russian Federation achieved a small decline in corruption perceptions since 2008. Similarly, as shown earlier in Figure 3.9 above, the European Bank for Reconstruction and Development's (EBRD) Business Environment and Enterprise Performance Survey also points to corruption as an important barrier to entrepreneurship and SME development in the Russian Federation.

Figure 3.10. **Perceptions of Freedom from Corruption**



Note: Transparency International's Corruption Perceptions Index ranks countries on how corrupt their public sector is perceived to be on a score of 0-100, where 0 means that a country is perceived as highly corrupt and 100 means it is perceived as very clean.

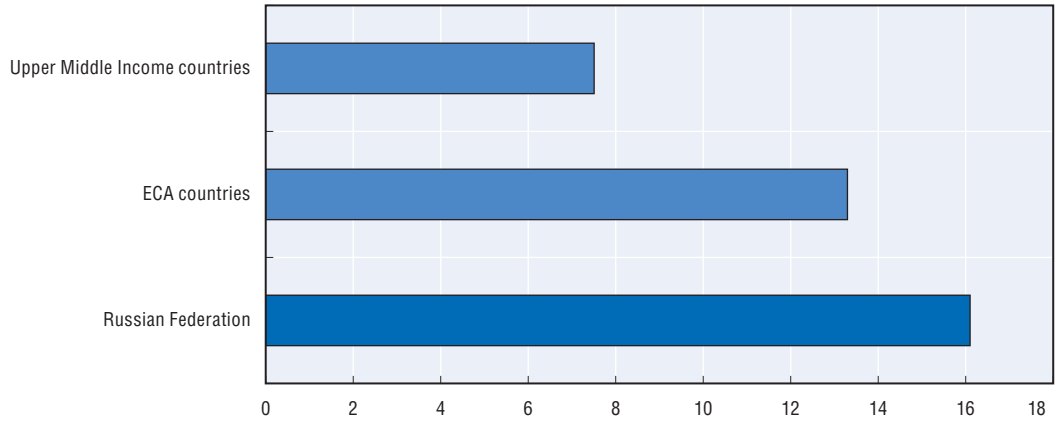
Source: Transparency International Corruption Perceptions Index, 2013 *http://www.transparency.org/cpi2013/results/*.

StatLink *http://dx.doi.org/10.1787/888933271868*

An alternative source of cross-country information on these issues is the IFC/World Bank Enterprise Survey, which seeks to measure corruption by asking businesses the number of times they are expected to pay a bribe when seeking to obtain various public services. The Russian Federation performs poorly on the summary Graft Index measure relative to the averages for ECA and Upper Middle Income countries (Figure 3.11). As shown in Figure 3.12, the percentage of firms reporting that they are expected to give gifts in meetings with tax inspectors was below the ECA average and in line with the Upper Middle Income country average, but in other areas of public service the performance of the Russian Federation tends to be worse than these comparator countries. The problems are also often quite widespread. For example, more than one-quarter of Russian Federation firms report needing to make payments to obtain a construction permit or import license.

Figure 3.11. **The composite Graft Index**

Percentage of all interactions between firms and public officials in which a bribe was expected



Source: World Bank/IFC (2012) Enterprise Surveys: Russian Federation Country Profile 2012. Washington DC World Bank Group.

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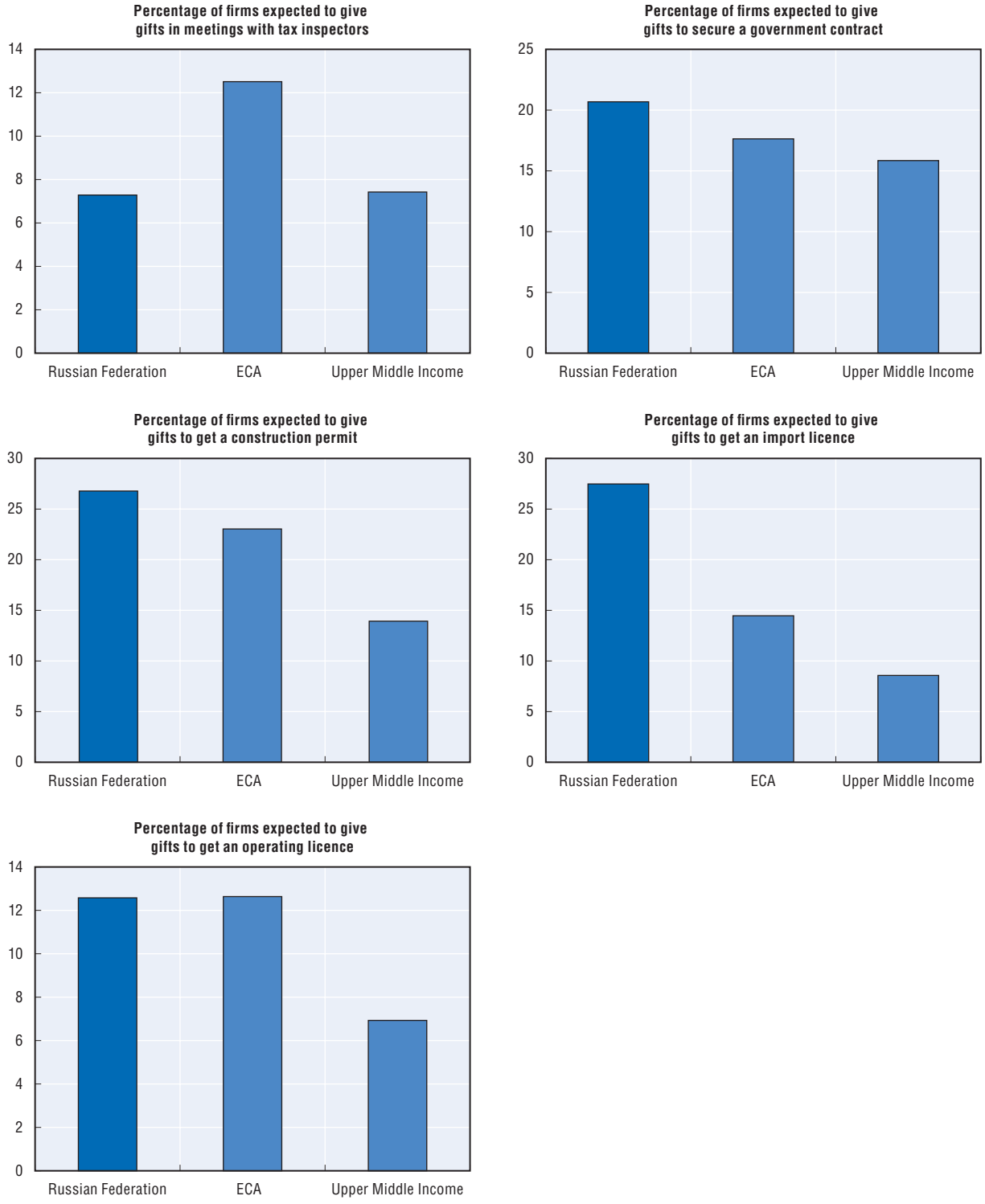
In an attempt to accelerate the rolling back of corruption in public relationships with businesses, the Russian government introduced an Anti-Corruption Plan in 2012. This involves a number of measures with significant potential to change cultures and behaviours in the public sector towards SMEs and entrepreneurs. For example, public bodies must appoint an ethics commission to review possible cases of corruption, public officials must declare any major expenditures they make on real estate, vehicles and financial securities, and public officials with responsibilities that are associated with high corruption risk must rotate functions regularly. In addition, a new law on public procurement was introduced in 2013 that reduces the opportunities for corruption in awarding public contracts by increasing transparency in the public procurement process. There are signs that this new energy in fighting corruption is making a difference. Thus, OECD (2014a) notes that the Russian Federation has implemented as many as 15 of the 26 recommendations of the Council of Europe's Group of States Against Corruption and partially implemented the remaining eleven (GRECO, 2013). It is important that the government maintains this emphasis on rolling back corruption in the dealings of public officials with SMEs and entrepreneurs, paying attention to implementation and enforcement of existing anti-corruption rules as well as to introducing new areas of legislation to tackle remaining gaps and weaknesses.

Figure 3.12. **Incidence of graft by public service area**



Source: World Bank/IFC (2012) Enterprise Surveys: Russian Federation Country Profile 2012. Washington DC World Bank Group.

StatLink http://dx.doi.org/10.1787/888933271889

Strengthening the rule of law

Ensuring the rule of law is also essential to providing favourable conditions for business investment and operation. However, the World Justice Project's Rule of Law Index ranks the Russian Federation only 80th out of 99 countries across a set of 47 indicators derived from household and expert surveys (World Justice Project, 2014), and significantly worse than the ECA average. In particular, the protection of property rights and the fairness of the judicial system are perceived to be affected important problems. Similarly, the IFC/World Bank Enterprise Survey suggested that only 30% of firms perceived the courts as being fair and impartial in 2012.

Table 3.3. **Rankings on the World Justice Project Rule of Law Index, 2014**

Thematic area	Russian Federation	Eastern Europe and Central Asia average
Constraints on government powers	89	75
Absence of corruption	66	63
Open government	67	60
Fundamental rights	79	62
Order and security	75	42
Regulatory enforcement	67	58
Civil justice	68	55
Criminal justice	76	61
Global ranking	80	60

Note: Countries are ranked from 1 (strongest) to 99 (weakest)

Source: World Justice Project (2014) The World Justice Project Rule of Law Index 2014, World Justice Project, Washington DC.

StatLink http://dx.doi.org/10.1787/888933272292

In response, certain measures recently been introduced to increase the independence and transparency of the judicial system and increase the protection of business property including increased pay and training of judges and investment in information technologies to increase the efficiency of operation of court administration. On the other hand, rotation of judges, randomised case assignments, increased transparency in the appointment and promotion of judges, and limitations on the discretion available to tribunal presidents to influence the rewards of judges have not yet been introduced (OECD, 2014a).

A new business ombudsman

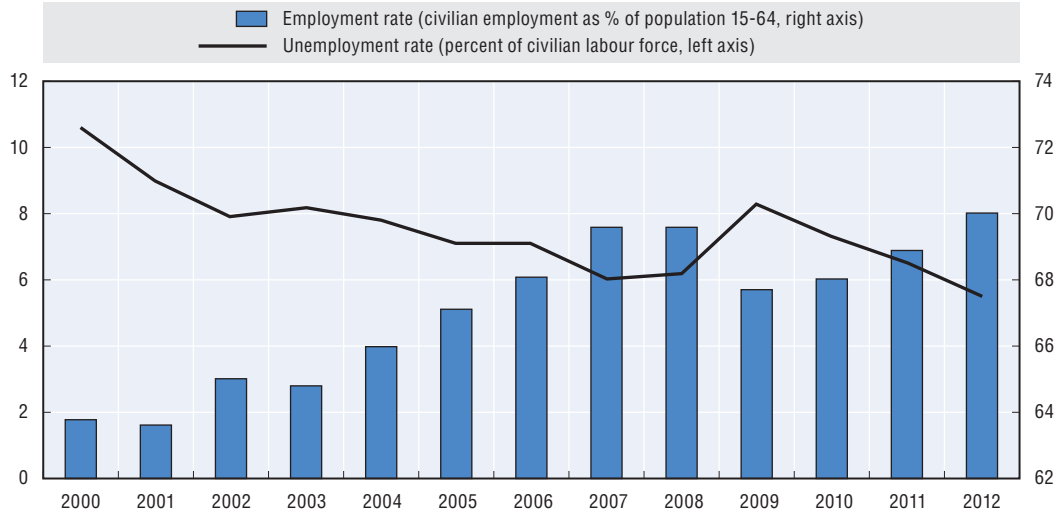
An important step was taken to create the position of Federal Business Ombudsman in the Russian Federation in 2012 in order to protect businesses from administrative and legal abuse by the government. The federal ombudsman is supported by a network of regional representatives. The role of the ombudsman is to monitor government behaviour and act as an advocate for businesses in government. It can investigate individual cases of injustice caused by poor administration of businesses by the government and seek improvements in the initial decision-making processes or in the way complaints are handled. As discussed in OECD (2014f) to be effective as a champion for SMEs and entrepreneurship in government, the ombudsman should have independence and strong operational capabilities, including the ability to make an independent evaluation of any grievance or complaint.

Labour market and human resources

Flexible labour market

The Russian labour market is characterised by high numerical and wage flexibility. As shown in Figure 3.13, employment recovered well from the shock of the global economic crisis and the economy now has both a high employment rate, which stood above the OECD average of 70% in 2012, and a low unemployment rate, which, at 5.5%, was below the OECD average of approximately 7.9%. The Russian economy has relatively high labour turnover rates, with approximately 30% of workers leaving their jobs every year, and the ability to rapidly adjust working hours and make use of non-standard labour contracts. In addition, there is substantial use of performance-related pay and informal payments. All this is indicative of a flexible labour market in which SMEs and entrepreneurs have relatively easy access to the volumes of labour they require.

Figure 3.13. **Employment and unemployment in the Russian Federation**



Source: OECD Annual Labour Force Statistics Database *http://dx.doi.org/10.1787/lfs-data-en.*

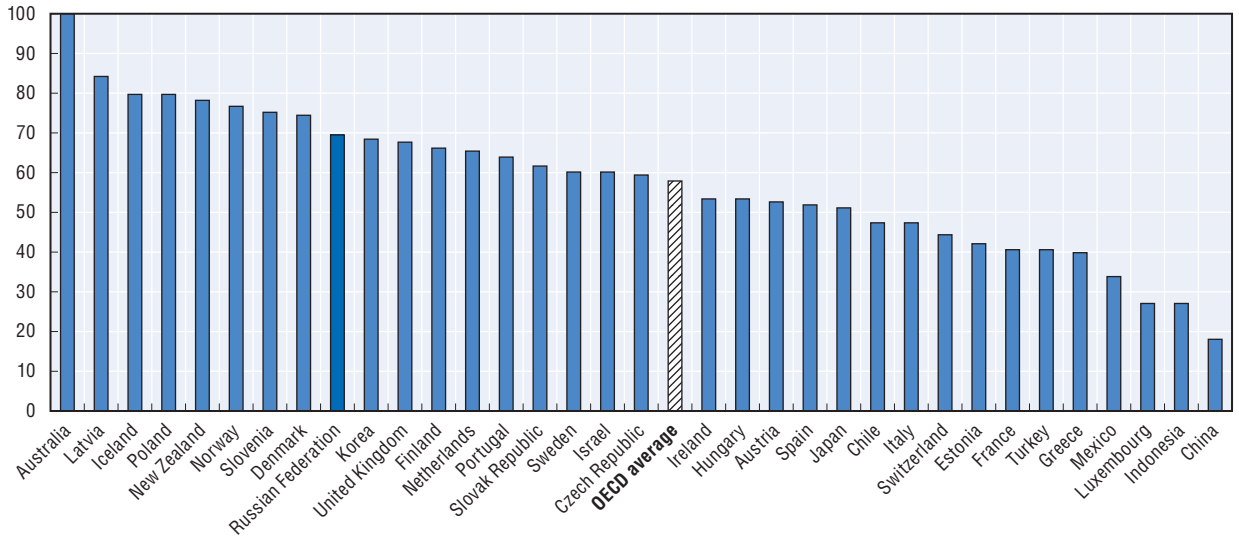
StatLink *http://dx.doi.org/10.1787/888933271896*

Skills shortages

Entry rates into tertiary education in the Russian Federation are above the OECD average (Figure 3.14). Furthermore, at approximately 34%, the proportion of young people entering vocationally-oriented tertiary education is relatively high, and the employment rate of adults with higher education is over 80%, in line with the OECD average (OECD, 2014a). These indicators imply that SMEs and entrepreneurs should have good access to university-educated labour, although not necessarily with ready-made skills for business.

However, there is a shortfall in secondary-level vocational skills and continuing workforce training. For example, only 20% of 25-64 year olds in the Russian Federation participated in formal or non-formal adult learning in 2012, well below levels typical of OECD countries (Figure 3.15). This deprives firms of important employee skills for innovation and entrepreneurship. Incentives to SMEs to engage in continuous training could be considered to mitigate this problem, for example through a training levy on employees to be reimbursed in the form of grants or vouchers to SMEs that offer training within or outside of the firm. The system of apprenticeships should also be strengthened with a particular view to increasing student placements in SMEs

Figure 3.14. **Entry rates into tertiary education, 2012**

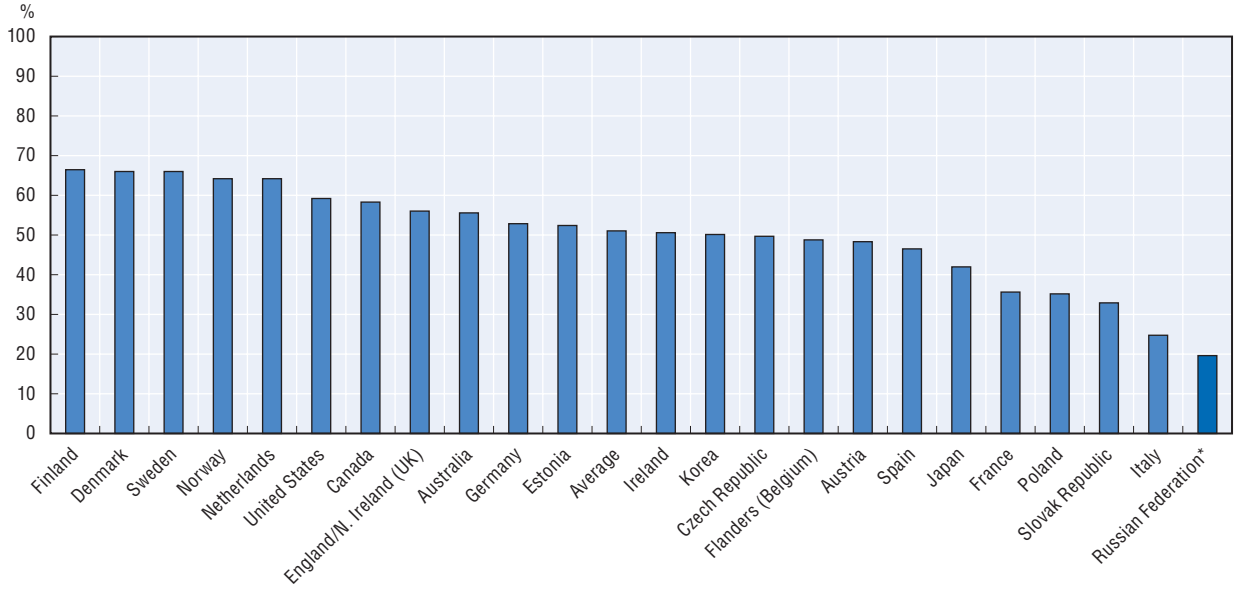


Source: OECD (2014), Education at a Glance 2014, Chart C3.2, available at *http://dx.doi.org/10.1787/888933118599*.

StatLink *http://dx.doi.org/10.1787/888933271905*

Figure 3.15. **Participation in adult learning**

2012



Note: The sample for the Russian Federation does not include the population of the Moscow municipal area.

Source: OECD (2014), Education at a Glance 2014, Chart C6.1, available at *http://dx.doi.org/10.1787/888933119207*.

There are also some weaknesses in the quality of school education. Notably, the performance of Russian 15 year olds was below the OECD average in mathematics, reading and science, although in line with other emerging countries such as Brazil, India and China (Figure 3.16). Similarly, the Russian Federation performs relatively poorly compared with OECD countries on the ability of students to apply the knowledge they learned in school to various problem solving tasks, although it is the best of the emerging economy countries investigated (Figure 3.17). These findings suggest the need for measures to increase investment in school education and orient it more towards problem-solving.

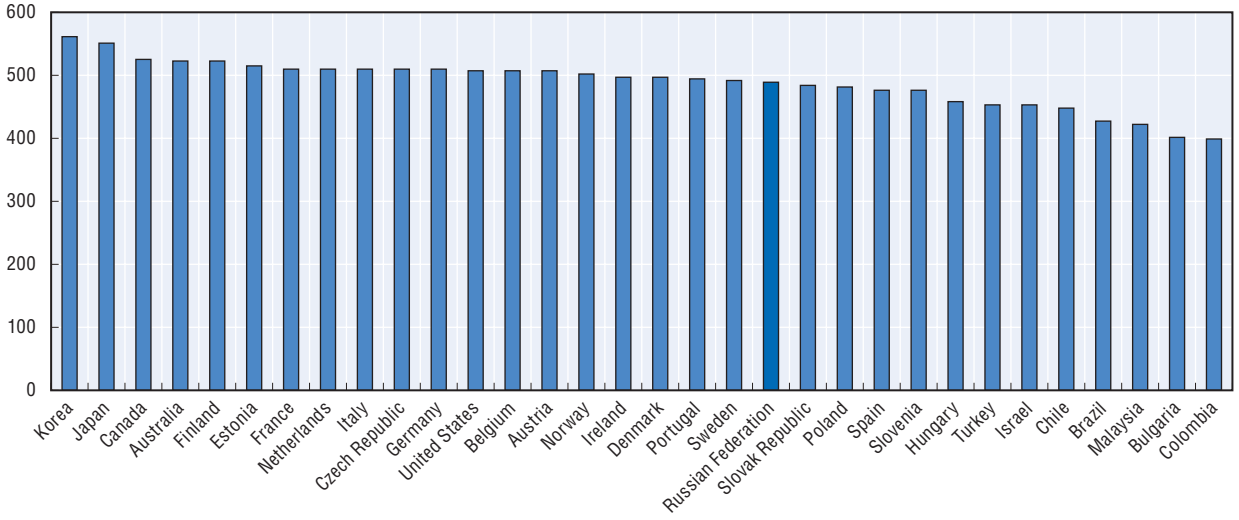
Figure 3.16. **Student proficiency in mathematics, reading and science, 2012**

Average scores of 15 year old students in PISA tests

Source: OECD (2014d) PISA 2012 Results: What Students Know and Can Do, Student Performance in Mathematics, Reading and Science (Volume I).

StatLink http://dx.doi.org/10.1787/888933271919

Figure 3.17. **Student proficiency in problem solving, 2012**
Average scores of 15 year old students in the PISA test on problem solving



Source: OECD (2014e) PISA 2012 Results: Skills for Life (Volume V) Student Performance in Problem Solving.

StatLink *http://dx.doi.org/10.1787/888933271928*

Developing entrepreneurial skills and mind sets

In order to create the substantial volume of new small businesses needed to fill the SME shortfall in the Russian Federation, it will be important to invest in preparing an incoming generation of motivated and skilled entrepreneurs. The formal education system has a critical role to play in this respect. However, whilst there are a number of individual entrepreneurship education actions in particular institutions and certain non-governmental organisations are making important contributions to the spread of entrepreneurship education and supporting educational materials and networks, the scale of entrepreneurship education activities is nowhere near what would be required to offer it to all young people in the Russian Federation. A wide-reaching activity for entrepreneurship education should therefore be considered, involving adopting entrepreneurial skills and mind sets as a key competency in school and university curriculums. As experience in other countries demonstrates, to achieve this will require substantial investment in training teachers to implement such a programme.

Steps to expand entrepreneurship education across the Russian formal education system might usefully start at the higher education level, which could act as a test bed and pioneer for the roll out of entrepreneurship education initiatives to the larger school and vocational education sectors. This partly reflects the fact that university students in many countries tend to have relatively high venture creation rates and be associated with better quality businesses. Thus, within the Russian Federation, nearly one-half (47.1%) of university students report the aspiration of founding their own business within five years of graduation (Shirokova and Kulikova, 2011). A number of ad hoc entrepreneurship education activities already exist at the tertiary level that can be scaled up and replicated across the country. Thus many university students, particularly in business studies, already take entrepreneurship courses. In addition, organisations including the Russian Centre for Entrepreneurship and the Russian Association for Entrepreneurship Education are helping to develop quality standards in entrepreneurship education and disseminate best practice teaching methodologies to the tertiary education sector. At the same time, there is great scope for more comprehensive entrepreneurship education. Thus no more than 10 Russian universities appear to be offering

a full learning cycle, including business support, coaching and mentoring, to nurture the launch of new companies, and university-level entrepreneurship education overall appears to be relatively weak in terms of the quality of courses offered, the institutional support offered to those delivering courses, and the infrastructure available for students who want to start a business (such as practical training, coaching and advisory support, and linkages to university-based business incubation facilities) (Shirokova and Kulikova, 2011).

Federal government can support the development of university entrepreneurship education and start-up support in a number of ways. One key component involves creating a national entrepreneurship education strategy in universities with clear objectives, indicators and incentives for universities to participate. This should emphasise both supporting people to act more entrepreneurially and supporting people to create new ventures, whilst recognising the distinctions between the two objectives. A second key component involves creating a shared learning platform for stakeholders involved in delivering entrepreneurship education. This could involve creation of a national observatory of pedagogical practices in entrepreneurship, which gathers together a repository of teaching materials and methods that can be used, and creating a training programme for entrepreneurship teachers in universities. Higher education institutions themselves should be encouraged to experiment and innovate in the provision of entrepreneurship teaching and start up support such as coaching and incubation for the those students who are most motivated to start a business.

A guiding framework for good practice and a number of international good practice models for supporting entrepreneurial competences in higher education have been developed by the OECD and the European Commission and can be examined at *www.heinnovate.eu/*. The framework stresses the importance of university leadership, organisational capacity, entrepreneurship teaching, pathways for entrepreneurs, linkages with business for knowledge exchange, acting as an internationalised institution and measuring the impact of entrepreneurship activities. It provides examples of how higher education institutions are achieving this.

Consideration should also be given to methods of rolling out entrepreneurship education activities to schools and vocational education and training institutions in the Russian Federation. Many countries have attained considerable success in implementing entrepreneurship education programmes, which are often the result of partnerships between the ministries responsible for economic development and education ministries (Box 3.1).

Box 3.1. **Co-operative development of an entrepreneurship education programme, The Netherlands**

Description of the approach

In the late 1990s, the Dutch government adopted the vision of becoming a more entrepreneurial society in response to analysis indicating that the Netherlands was lagging behind the European Union and United States in numbers of new entrepreneurs, innovators and high-growth companies, and that its population had relatively low aspirations and skills for entrepreneurship. The government adopted a multi-faceted strategy, including an initiative to foster entrepreneurship at all levels of the education system from primary school to university.

The goal was to make students aware of the opportunities of entrepreneurship as an alternative to paid employment, helping them to develop traits that contribute to successful entrepreneurship, and introducing them to elements of knowledge necessary for entrepreneurial activity. Although there were already a few

Box 3.1. **Co-operative development of an entrepreneurship education programme, The Netherlands** *(cont.)*

good practices in entrepreneurship education at the university and vocational training levels, there was no comprehensive coverage and there was very little understanding of entrepreneurship teaching in primary and secondary schools. Recognising that the starting point for preparing for entrepreneurship varies according to education level and while the educational institutions themselves are responsible for the content of their entrepreneurship education programmes, the government decided to take a "bottom-up" approach to charting and implementing the possible improvements to the education system.

To begin the process, the Ministry of Economic Affairs, Ministry of Education, Culture and Science and Ministry of Agriculture, Nature and Food Quality launched the National Entrepreneurship and Education Programme in 2000. They immediately formed a consultative commission on entrepreneurship education consisting of people from different fields of education, employer associations, entrepreneurs, and the Dutch Association of SMEs to draft proposals for the development, piloting and implementation of promising activities. As a result, the government, with education experts, developed a learning path for the introduction of age-appropriate entrepreneurship concepts at different levels of education. It also completed an inventory of existing good practice initiatives that corresponded to the proposed learning path and could serve as models for other educational institutions. It also identified barriers that might be faced by schools and universities to supporting the learning path and adopting good practices and organised regional meetings with education officials, enterprises and business support organisations to promote the scheme.

To accelerate the process, the government approved a Subsidy Scheme on Entrepreneurship and Education, setting aside EUR 5 million for the 2000-2002 period to support pilot projects in education institutions (e.g. seminars, training for teachers) and horizontal projects to develop learning instruments for entrepreneurship awareness, knowledge and skills. The Scheme was operationalised through a call for proposals from schools, vocational and higher education institutions wishing to start teaching entrepreneurship. Since then, significant budgets have been allocated and the budget had increased to EUR 30 million for 2008-11. At the primary and secondary levels, the call for proposals solicited projects focused on creating and encouraging a modern-day learning environment, teaching methods for entrepreneurship, the further professionalisation of teachers in the field of entrepreneurship, and collaboration between students, teachers, entrepreneurs and the business community. At the university level, the recent emphasis has been on funding the creation of regional Centres of Entrepreneurship that will encourage entrepreneurship activities in all regional HEIs on a multidisciplinary, institution-wide basis.

In addition, all teachers and education institution leaders have the opportunity to follow courses in entrepreneurship education and subsidies are offered to set up entrepreneurship education networks in association with the regional business community, chambers of commerce, knowledge centres, teacher training institutes and other authorities. Part of the mission of these networks is to stimulate other educational institutions and regional actors to be active in entrepreneurship education. Annual competitions are also organised where prizes are awarded for the most enterprising entrepreneurship education projects.

Results

The numbers of educational institutions that have started to offer regular study programmes in entrepreneurship education has increased. In addition, several HEIs have introduced a certificate in entrepreneurship, an initiative that is being expanded as a national programme offer from middle vocational education up to and including university. Thousands of teachers have received training and thousands of students have been exposed to entrepreneurship education activities. Impact studies, carried out every two years, indicate that this has resulted in an increased number of Dutch students showing entrepreneurial behaviour and starting businesses within five years of completing their studies.[2]

Box 3.1. **Co-operative development of an entrepreneurship education programme, The Netherlands** *(cont.)*

Obstacles and responses

Some of the challenges have been convincing educational institutions that entrepreneurial learning methods fit within the objectives and terms of inspections; overcoming a non-entrepreneurial culture among school administrations and teachers; building the skills and knowledge of teachers on entrepreneurship education; and increasing the participation of businesses and educational institutions in lagging localities. Progressive versions of the Action Programme Education and Entrepreneurship have focused on addressing these constraints.

Relevance to the Russian Federation

This example offers a possible model for generating and supporting bottom-up entrepreneurship education initiatives using a competitive call for proposals together with a national mechanism for building networks to share knowledge on good practices.

Further information

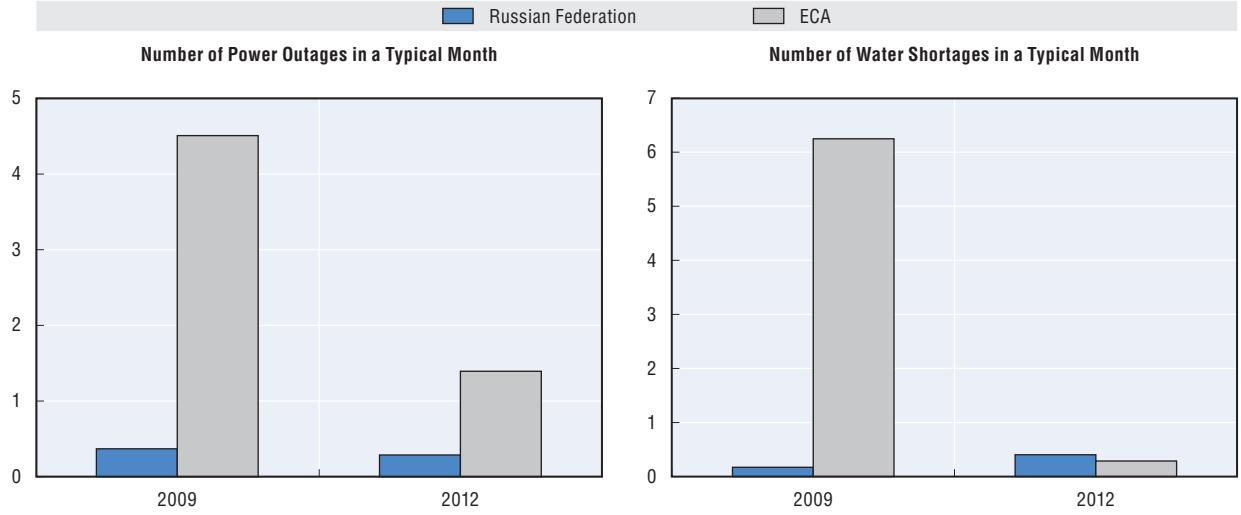
Information on funded projects and their outcomes (including materials and tools) are available on the entrepreneurship education website *www.onderwijsonderneemt.nl/*.

Source: Based on information from the Ministry of Economic Affairs, Netherlands

Physical infrastructure

Figure 3.18 shows that the number of electricity outages and water shortages is low for the typical SME in the Russian Federation, and is significantly less of a problem than in other ECA countries. On the other hand, there are significant delays in the Russian Federation in securing electricity and water supply, which is an important issue for start-up firms (Figure 3.19). Completion of the necessary procedures is estimated to take an average of 120 days with respect to electricity supply and 54 days with respect to water. These are substantially greater than the ECA and Upper Middle Income Country averages. A priority for entrepreneurship policy is to ensure that these delays are substantially reduced.

Figure 3.18. **Quality of water and electricity infrastructure for businesses**



Source: World Bank/IFC (2012) Enterprise Surveys: Russian Federation Country Profile 2012. Washington DC World Bank Group.

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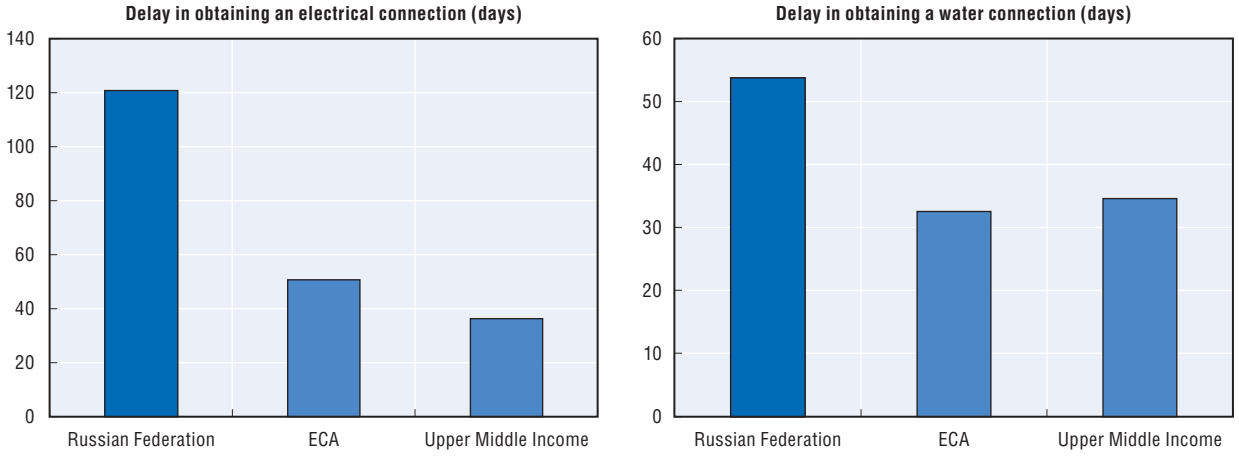
Figure 3.19. **Infrastructure service delays**



Source: World Bank/IFC (2012) Enterprise Surveys: Russian Federation Country Profile 2012. Washington DC World Bank Group.

StatLink http://dx.doi.org/10.1787/888933271946

There are also certain weaknesses affecting Russian businesses with respect to transport infrastructure in terms of intensifying urban transport problems, poor inter-modal connections around seaports, slow and costly rail freight delivery and an under-developed road network (OECD, 2014a). Measures to increase investment in transport infrastructure, to ensure competition in the transport sector and to improve the financing and management of urban public transport would be beneficial for SME development as well as for businesses and consumers in general.

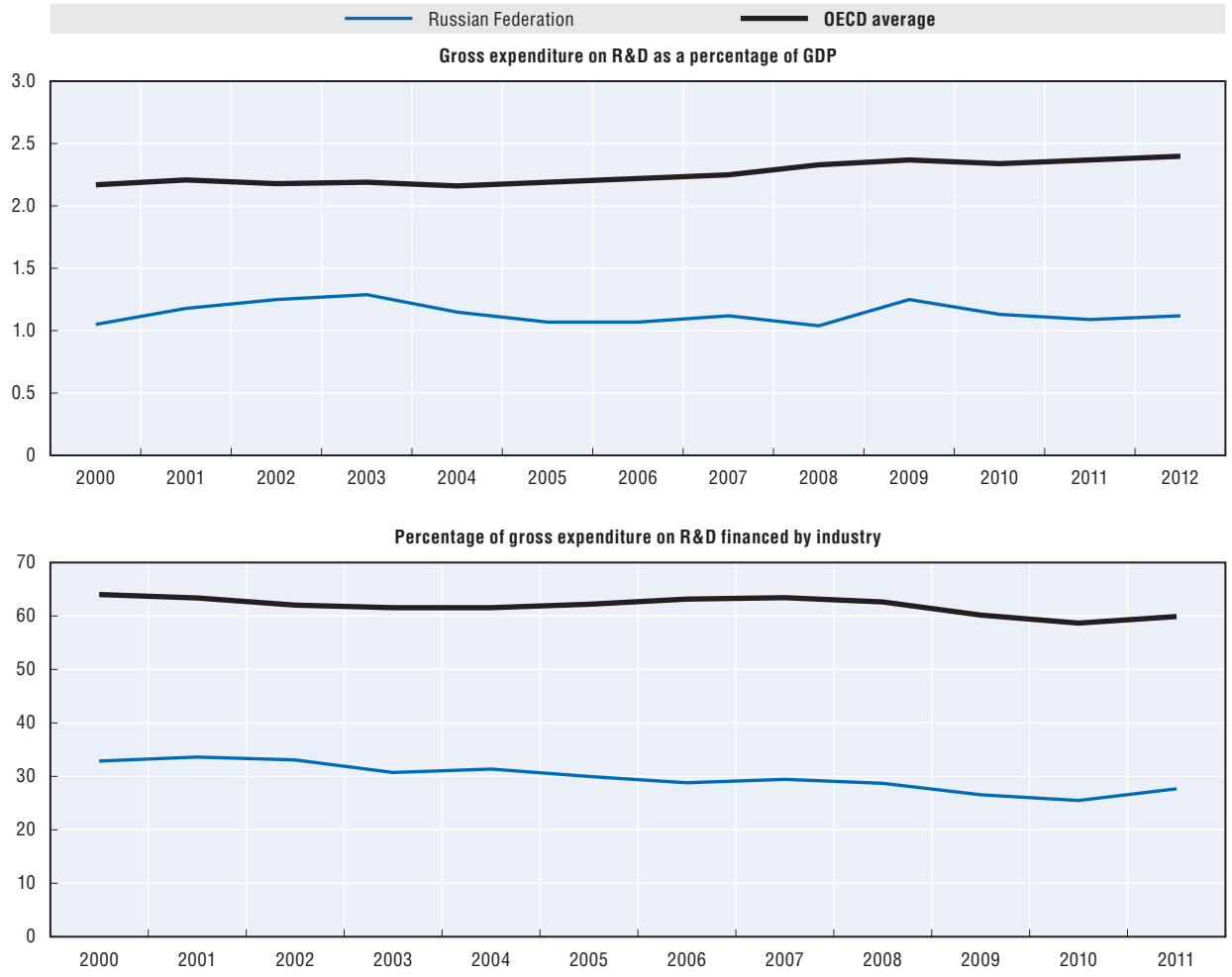
The innovation system

The innovation system in the Russian Federation has produced long-standing excellence in a number of branches of science and technology, reflecting high levels of education and a research tradition in these fields. Moreover, the government has clearly recognised the need to build on these assets through the launch of the "Innovative Russia 2020 Strategy" in 2012 containing a range of policy initiatives aimed at increasing R&D activities in the business sector.

Low R&D expenditure

One of the key challenges will be to increase R&D expenditures in the Russian Federation. As indicated in Figure 3.20, the Russian Federation's R&D intensity is low relative to OECD countries. Gross domestic expenditure on R&D stood at approximately 1.1% of GDP in the Russian Federation in 2012, well below the OECD average of approximately 2.4%. This reflects the Russian Federation's emerging economy status and an industrial structure that is dominated by extraction industries with traditionally low R&D intensities. Another contributing factor is a low level of R&D expenditure financed by industry as opposed to government. The industry share of R&D was only 27.7% in the Russian Federation in 2011, well below the OECD average of 59.9%; moreover it had declined from approximately 32.9% in 2000. On the other hand, at 6.4 researchers per thousand employees in 2008, the number of researchers in the Russian Federation was much closer to the OECD average of 7.6, and it is possible that many R&D personnel in the Russian Federation are under-utilised (OECD, 2011).

Figure 3.20. **R&D expenditure in the Russian Federation**



Source: OECD Main Science and Technology Indicators Database. *https://stats.oecd.org/Index.aspx?DataSetCode=MSTI_PUB.*

StatLink *http://dx.doi.org/10.1787/888933271951*

In addition to increasing R&D expenditure, particularly in industry, there are some issues to address in the methods of financing public science, including a shortage of suitably qualified scientists in some specialist areas, inadequate laboratory equipment and materials, insufficient grant sizes compared to the intended task, and overregulation of grant spending (OPORA Russia, 2011).

Insufficient research commercialisation

A recent innovation survey (OPORA Russia, 2011) found that Russian public sector scientists significantly lag behind the global average rate of international scientific publication and have performed poorly in terms of converting research expenditure into scientific publications. The survey also showed that almost three-quarters of public scientists and researchers had no experience of commercialisation and less than 4% had successful experience. It is therefore important to take measures to increase the commercialisation of public research, which should be a vital part of a strategy designed to increase the competitiveness of Russian businesses.

A significant step forward was taken in this respect in 2009 with the adoption of a law authorising universities and public research organisations to create innovative small enterprises. In addition, financial incentives could be offered in the form of incentives for investors in early-stage innovating companies. On the other hand, there has not been a sufficient set of complementary actions aimed at facilitating linkages between public researchers and existing SMEs (OECD, 2011). The United Kingdom's Knowledge Transfer Partnerships programme offers a potential model for this type of action, as described in Box 3.2.

Box 3.2. **Knowledge Transfer Partnerships, United Kingdom**

The approach

This programme aims to create a series of partnerships between a business and an academic institution in order to:

1. Facilitate the transfer of knowledge through projects undertaken by high-calibre recently-qualified graduates working under the joint supervision of a company and an academic institution.
2. Provide company-based training for recently-qualified graduates, to enhance their business and specialist skills.
3. Stimulate and enhance business-relevant training and research undertaken by academic institutions.
4. Increase the interaction between businesses and academic institutions as well as awareness of the contribution that academia can make to business development and growth.

Each Knowledge Transfer Partnership (KTP) employs at least one recently qualified graduate known as an Associate who works in the company on a project of strategic importance to the business whilst being supervised by an academic within the partner HEI. The project can vary in length between 12 months and 36 months. The Associates are either postgraduates, researchers, university graduates or individuals qualified to at least NVQ level 4 or the equivalent

KTPs were first launched in 1975 under the heading of the Teaching Company Scheme and are now supported by 15 government organisations led by the Technology Strategy Board. There are currently 800 KTPs operating across the UK. Up to GBP 60 000 available in government grants per KTP, with the balance of the project cost coming from the company partner. The latter contribution varies according to the size of business. For example in the case of an SME employing less than 250 people, the contribution would normally be limited to one-third of total project costs. The grant from government plus the contribution of the company more than covers the employee's salary and is expected to make a contribution to the HEI's overhead costs.

Results

Each of the various parties involved in the KTPs gain benefits. Academic institutions can apply knowledge and expertise to business problems, develop business-relevant teaching and research materials, identify new research themes, publish high-quality research papers on the basis of results, and improve their understanding of the business environment. Companies benefit from the opportunity to develop non-price competitive advantages by linking up with academics and accessing high-quality postgraduates. Approximately three-quarters of the graduates are offered a position by the company at the end of the KTP, and all participants gain a competitive salary, a management qualification and valuable experience during project implementation.

Each partnership created 3 additional jobs on average (excluding the Associate) between 2001/2 and 2007/8, at a cost per job of approximately GBP 60 000. The value added generated by the projects was approximately five times the public money invested. There are also wider benefits in the form of increased innovation capacities in the participating businesses.

Box 3.2. Knowledge Transfer Partnerships, United Kingdom *(cont.)*

Success factors

The 2010 evaluation report on the KTPs indicates that there is a high level of client satisfaction among the businesses, academics and Associates that are involved. Stakeholders have a clear picture of its role in value creation. In addition, the long standing nature of the programme means that its delivery infrastructure is well established.

Problems and responses

The 2010 evaluation review identified a number of problems which are now being addressed. These included a cumbersome application process, lack of user-friendliness of the web portal, inflexible training provided to Associates (which often repeated prior learning and did not always add value to the project), and promotion of the KTP programme in isolation from other government knowledge transfer programmes.

In addition, decisions have been made to increase the targeting of support onto those KTPs that generate the greatest impacts, increase the flow of new businesses into the programme, increase the number of knowledge based institutions involved and increase the number of KTPs supported by each participating institution.

Relevance to the Russian Federation

A programme of this kind would help to raise innovation investments and capabilities among SMEs in the Russian Federation. To be successful, such an initiative would need to be strongly promoted to companies and research organisations, which should include training for academic supervisors and some hands-on workshops for participating companies in order to help them to fully understand the nature of the partnerships being supported.

Further information

Regeneris Consulting (2010) Technology Strategy Board Knowledge Transfer Partnerships Strategic Review; *http://webarchive.nationalarchives.gov.uk/20140827133341/http:/www.innovateuk.org/_assets/pdf/corporate-publications/ktp%20strategic%20review%20feb%202010.pdf*.

Source: Based on information from Regeneris Consulting (2010) and Technology Strategy Board

Strengthening intellectual property rights

Both company and brand names are given general intellectual property protection in the Russian Federation, usually in the form of a trade mark, and once protection is granted, infringement can lead to prosecution. However, other aspects of SME intellectual property such as knowhow and creative works (software and data bases, inventions, industrial designs etc.) are more difficult to protect. This reflects a relatively fragmented legal framework for intellectual property rights (IPRs). In addition, the Russian Federation has no law of precedence, which means that a court does not need to adhere to prior decisions made by other courts of the same level.

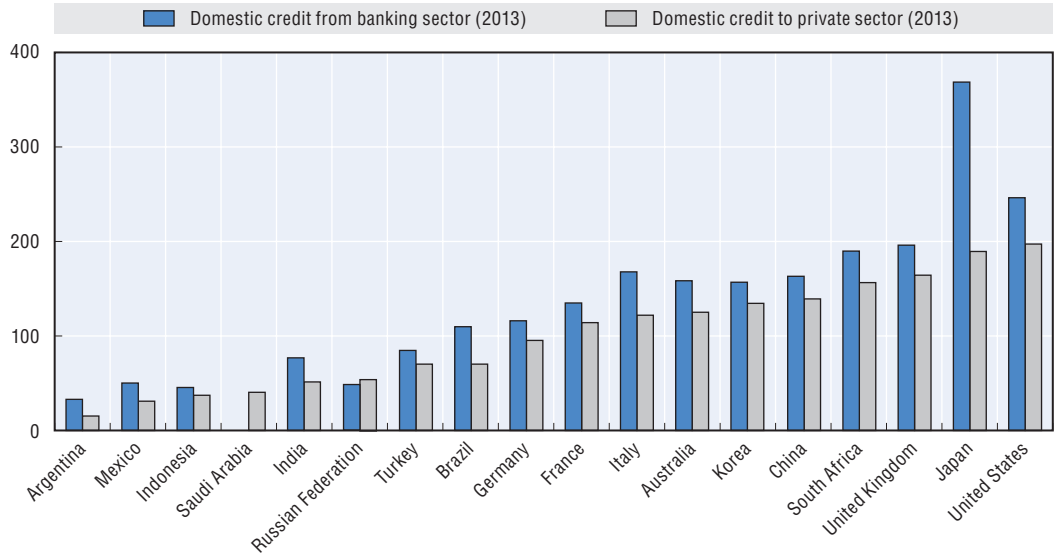
The Competition Road Map calls for the Russian Federation to commit to strengthening IPR protection in order to address these issues. This effort needs to cover the enforcement and implementation of legislation as well as the design of the legislation itself. Some lessons can be drawn from the USA's experience with the Joint Strategic Plan on Intellectual Property Enforcement. This involves the coordinated development of a strategic intellectual property protection plan across numerous government agencies and departments and a set of agreed actions such as ensuring that the federal government does not purchase or use infringing products, supporting transparency in the development of enforcement policy, and improving data and information collection on intellectual property related activity.

Access to finance

Well-functioning financial markets are essential for channelling an adequate supply of finance to those SMEs and start-up entrepreneurs for which risk-adjusted rates of return are sufficient to cover finance costs. They should also offer a mix of financial products that are well adapted to different types of business project at different stages of business development, including various loan products, asset-based services such as factoring, and equity instruments. There are three main requirements for well-functioning finance markets. First, lenders and investors on the supply side should have adequate finance and capacities to assess the risks and returns of investment in SMEs and entrepreneurs. This normally involves a mix of deposit-taking banks, insurance companies, pension funds, investment banks, microfinance institutions, trade credit and leasing companies, venture capital funds and business angels. Second, entrepreneurs and SME managers on the demand side should have the skills, knowledge and financial literacy to locate and draw down the most appropriate available sources of finance and act as competent stewards of investments. Third, there should be an infrastructure for financial intermediation that is transparent, so as to minimise informational asymmetries among parties, and embedded within a regulatory and legal framework that protects the legal rights of all market participants.

However, the overall finance market in the Russian Federation is relatively weak, and this affects the supply of finance for SMEs and entrepreneurs. For example, compared with the majority of G20 countries (including China and Brazil), the volume of domestic credit provided by the banking sector and the volume of domestic credit to the private sector in the Russian Federation represents a relatively small share of GDP, as shown in Figure 3.21. Although the situation has improved over the last five years, the Russian Federation continues to lag substantially behind developed OECD and Euro area countries and somewhat behind Eastern European and Central Asian countries in the supply of credit to the economy (Figure 3.22).

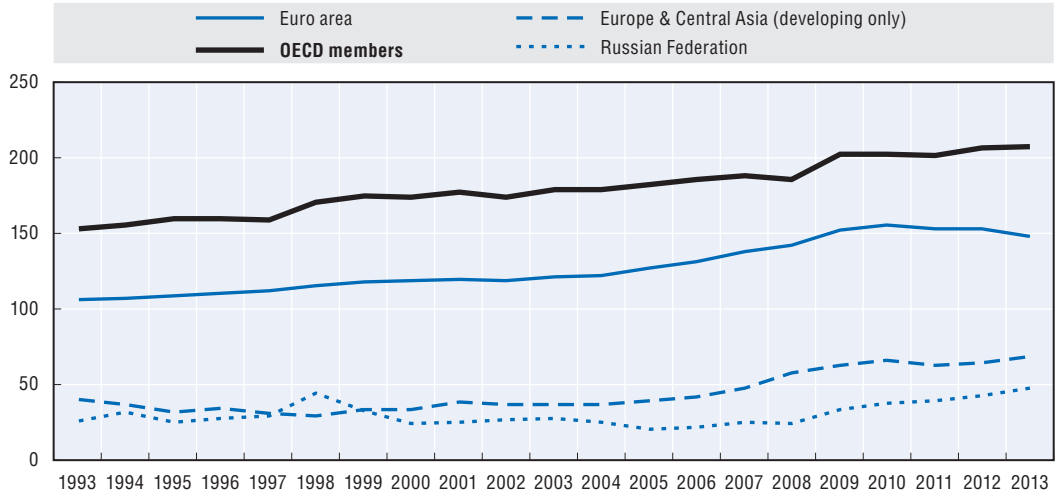
Figure 3.21. **Domestic credit as a percentage of GDP**



Source: World Development Indicators Database, World Bank *http://databank.worldbank.org/data/home.aspx.*

StatLink *http://dx.doi.org/10.1787/888933271960*

Figure 3.22. **Domestic credit from the banking sector as a percentage of GDP 1993-2013**

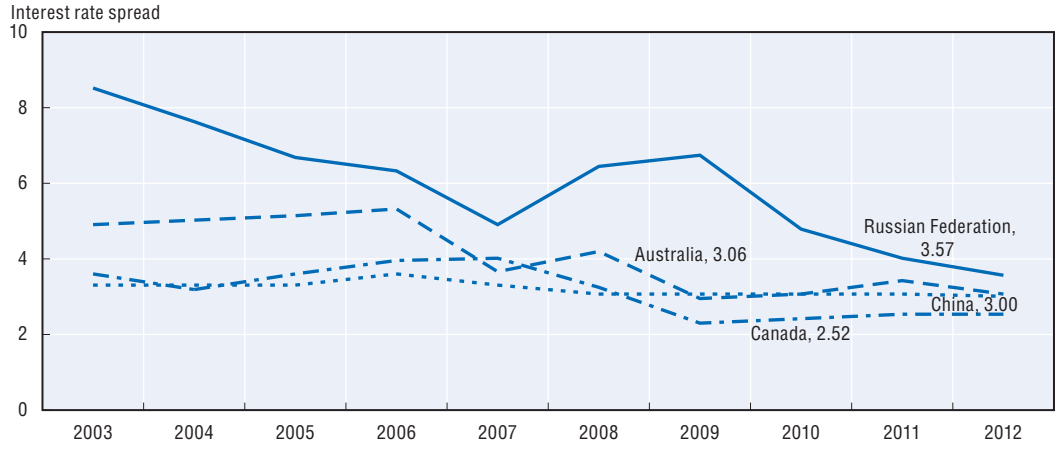


Source: World Development Indicators Database, World Bank *http://databank.worldbank.org/data/home.aspx.*

StatLink http://dx.doi.org/10.1787/888933271974

Furthermore, the relatively limited volume of bank lending is accompanied by relatively high credit costs. As shown in Figure 3.23, despite a substantial reduction in the overall spread between bank lending interest rates in the Russian Federation since 2003, the interest rate spread is still high relative to key comparator countries. The historically high cost of loans in the Russian Federation is likely to have dampened demand for external capital from SMEs and entrepreneurs, and acted as a constraint on the development of the SME finance market.

Figure 3.23. **Interest rate spreads (bank lending rates less deposit rates), 2003-12.**



Source: World Development Indicators Database, World Bank *http://databank.worldbank.org/data/home.aspx.*

StatLink http://dx.doi.org/10.1787/888933271986

Improvements in volumes and terms of lending in financial markets are therefore needed in the Russian Federation as well as interventions designed specifically for SMEs and entrepreneurs, which are discussed further in chapter 6. Two important policy priorities are increasing the density of banks and increasing legal protection for investors.

With respect to the former, the Russian Federation had only 1 112 registered banks in 2011 (RSBF, 2012, p. 7) and only 0.169 bank offices per 1 000 inhabitants in 2008 compared with a global average of 0.346 (OECD, 2009). Given geographic concentration of bank branches, particularly in Moscow, banking coverage is limited in some regions. Bank density in the Russian Federation is affected by strong concentration and high levels of state control in the banking industry. The twenty largest banks accounted for more than 70 per cent of assets, credit and corporate loans in the Russian Federation in 2011. The five largest banks accounted for more than 50 per cent. State-controlled banks collectively held 53 per cent of total banking sector assets (RSBF, 2012). These problems are likely to be exacerbated by increases in the capital-to-loan ratios of banks seeking to reduce risks following the global financial crisis and take up new Basel III standards.

With respect to investor protection, the World Bank Doing Business index attributed a score to the Russian Federation of only 3 out of 10 for the legal rights of borrowers and lenders compared with 7 in the OECD and ECA countries as a whole, while the Russian Federation ranked 115th of 189 countries in 2014 with respect to regulations protecting minority investors against misuse of corporate assets by company directors for their personal gain. Improvements in investor protection in terms of regulations on disclosure of transactions by directors, liability of directors to damages, and ease of access to corporate information for litigation could increase the flow of finance to SMEs and entrepreneurs, particularly in the area of equity finance.

Conclusions and recommendations

There have been some substantial improvements in several aspects of the framework conditions affecting SMEs and entrepreneurship in the Russian Federation. These include increased openness to trade following the Russian Federation's adhesion to the World Trade Organisation, the introduction of substantial competition development and privatisation programmes, considerable reductions in the administrative and regulatory burdens on businesses and the introduction of a federal anti-corruption initiative. For example, the time needed to start a business has been brought down to that of the leading countries in the world. It is important to keep these reform programmes developing in these directions and ensuring their effective implementation on the ground.

In addition, there are a number of areas in which further improvements could bring a significant boost to SME and entrepreneurship development. These include opening the economy up to more private sector activity by further reductions of state control, encouragement of inward FDI activity, strengthening vocational and entrepreneurship skills, strengthening investment in R&D and the commercialisation of public research, enhancing the rule of law, including protection of business property and the rights of external investors in SMEs, and increasing bank lending to SMEs to counter significant constraints on SME liquidity and investment.

As well as being critical to addressing the SME and entrepreneurship gap in the Russian Federation discussed in the previous chapter, further improvements in framework conditions will be very important in responding to the challenges of increased foreign trade, which brings both new opportunities for domestic firms to access export markets and the challenge of responding to increased foreign competition.

The following policy recommendations are offered:

Key policy recommendations for the business environment and framework conditions

- Continue to reduce the regulatory barriers and stimulate the attraction of inward FDI in order to reinforce its role in upgrading SME technologies and expanding their markets.
- Build technical capacities in competition policy assessment within the competition authority by providing analytical guidance and training for officials and establish a system for monitoring the uptake of recent product market competition reforms.
- Pursue plans to privatise SOEs and reduce state subsidies and price controls; all of which would help to create a more benign environment for SME and entrepreneurship development.
- Bolster SME procurement policy by initiating targeted information and training programmes to increase the ability of SMEs successfully to compete for public procurement contracts. Ensure that recent commitments to improving public procurement from SMEs are fully implemented and monitored.
- Further reduce regulatory burdens on SMEs and entrepreneurs by legislative reforms in lagging policy areas such as construction permits and trading across borders, training public officials in dealing with businesses, increasing the use of e-government services for businesses (e.g. on-line business registration, tax declarations and reporting), extending RIA procedures to cover existing government laws and regulations as well as new ones and creating a body to enforce RIA procedures across government and to ensure that RIA results are translated into changes in policy.
- Maintain the emphasis on rolling back corruption in the dealings of public officials with SMEs and entrepreneurs, paying attention to implementation and enforcement of existing regulation and introducing further legislation to tackle remaining gaps. Provide logistical and operational support to the Federal Business Ombudsman.
- Strengthen judicial independence through greater transparency in appointment and promotion processes, better pay and rotation of judges, and providing better protection against outside interference in court cases.
- Boost subsidies for continuous training and workforce development in SMEs, improve the quality of training in vocational education colleges and increase apprenticeships and student placements in SMEs.
- Expand and consolidate the promotion of entrepreneurial skills and competencies in formal education by introducing national incentives and support structures (such as resource banks of pedagogical materials) for entrepreneurship education and graduate business start-up support (e.g. student entrepreneur clubs and incubators) in universities, introducing entrepreneurship as a specific competence in the formal curriculum at elementary and secondary levels and developing a methodological base and training programme for school teachers in entrepreneurship education.
- Increase the emphasis of public innovation investments on the market commercialisation of research, especially in relation to individual entrepreneurs and SMEs, improve the intellectual property rights system with regard to the clarity of the law and its enforcement and take active steps to promote research, innovation and training co-operation between universities and SMEs.
- Increase legal protection for external investors in businesses and promote liberalisation and competition in the supply of finance for business.

Notes

1. The average public procurement value to a small business is about RUB 4 million.
2. "Progress Report on the Education and Entrepreneurship Programme", The Hague, 19 November 2008.

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OECD Studies on SME and Entrepreneurship
Russian Federation

Chapter 4

Strategic Framework and Delivery Mechanisms For SME and Entrepreneurship Policy in the Russian Federation

This chapter examines the legal framework for SME and entrepreneurship policy in the Russian Federation, the distribution of responsibilities across federal government for different aspects of SME and entrepreneurship policy, and the extent of policy leadership and co-ordination. It also assesses the major strategic directions in SME and entrepreneurship programme support that the federal government has chosen to pursue and the distribution of federal SME programme spending across different activities. Recommendations include developing an integrated master plan for SME and entrepreneurship promotion and shifting the weight of programme expenditures away from general SME investment and start-up subsidies towards more targeted subsidies aimed at innovation and exporting and more business development services such as company diagnostics and consultancy.

The legal framework at federal level

Evolving federal legislation for SME and entrepreneurship policy

The foundations for SME and entrepreneurship policy in the Russian Federation were originally created at the end of the 1980s, when legislation was passed to recognise the private ownership of enterprises, enable the privatisation of state-owned enterprises (SOEs) and create market institutions. These reforms were an essential platform for future SME and entrepreneurship development but were not sufficient to see the emergence of a sizable SME sector. More specific SME policies were required. The first step to achieve this was taken in 1995 in the form of the Federal Law on State Support of Small Business, which established the Federal Foundation for Small Business Support as a mechanism to channel financial subsidies to small businesses and create a business development support infrastructure. It supported the creation of many business development support organisations at federal and regional levels in the late 1990s, including agencies for small business support, business training and information centres, science parks, and legal and accounting firms providing advice and consultancy to small enterprises. However, the development of a systematic and high-quality business services infrastructure was held back by under-funding, lack of funding continuity, lack of transparency in the expenditures and activities of the business support organisations, inadequate recognition of the needs of entrepreneurs in the choice of support tools, and failure to monitor outputs and make appropriate adjustments (Chepurenko, 2011). The Foundation was shut down in the early 2000s.

Federal small business support then became the responsibility of the Ministry of Economic Development, which initially shifted to a more indirect strategy of reducing the administrative and regulatory costs of entry and operation for SMEs and entrepreneurs. At the same time, with the withdrawal of public funding, the system of business support organisations that had emerged in most regions collapsed. Direct support to SMEs was reintroduced in 2005 via the Target-Oriented Programme for the Support of SMEs, which focused on SME financing and management skills development. The programme had a number of important strengths. It aimed to target those segments of the SME population where policy impacts could be expected to be the greatest – nascent entrepreneurs, start-ups, growth-oriented SMEs, and innovative SMEs. It emphasised decentralised SME support mechanisms using federal and regional co-funding, competition among SME support organisations, identification and dissemination of best practices, lowering of exit barriers for less successful SMEs, and incentives for co-operation between small, medium and large businesses. It also set targets for expected attainment and established indicators for monitoring progress that were to be reported on in an annual update on programme implementation.

However, the government failed to achieve a balanced approach in implementing the programme, awarding substantially more federal funding to some priorities than others. For example, 45% of expenditures in 2005-07 went to the formation of 21 venture capital funds and 23 regional loan guarantee funds and a further one-third went to the creation of 111 local, municipal and university-based business incubators whereas only 2% was

directed to export support. In addition, inadequate efforts were made to inform the relevant audiences, including possible beneficiaries of the support services available. Although the programme did succeed in making financing and business development support more accessible to SMEs, the impact on the development of the SME sector was only modest, with the slowest progress made in increasing the entry of new businesses, the numbers of exporting SMEs, and the involvement of SMEs in public procurement (Chepurenko, 2011).

The current legal framework for SME and entrepreneurship policy in the Russian Federation is the 2007 federal SME Act (Federal Act Number 209-FZ of 18 October 2007 "on Development of Small and Medium Business in the Russian Federation"), which came into force on 1 January 2008. There were two important additions to the target groups of this new framework compared with previous legislation, namely the recognition of "micro" and "medium" enterprises in addition to small businesses, including definitions for each of the new categories, and official recognition for the first time of the issue of entrepreneurship.

The main goals of today's policy, as stated in the 2007 federal SME Act are:

- increasing the number of SMEs, their share of GDP and their share of federal and local taxes collected;
- providing employment through the development of SMEs and self-employment; and
- promoting competition through the development of new and small enterprises.

The federal SME Act also makes special reference to policy support for developing SMEs in the crafts and agricultural sectors and SMEs involved in export and/or innovation activity.

The Act identifies the operational instruments to be used in implementing federal SME and entrepreneurship policies, including:

- simplified procedures for tax accounting and reporting by SMEs and privileged payment procedures for acquisition of privatised state and municipal property by SMEs;
- special procedures to facilitate SME access to state and municipal public procurement contracts;
- funding for SME support infrastructure including entrepreneurship centres and agencies, technoparks, innovation and technology centres, technology commercialisation centres, business incubators, training and marketing centres, consulting centres, and export centres;
- financial support measures including credit and credit guarantee funds, investment funds, and leasing companies;
- support for SME development programmes operated by regional and local governments and non-governmental organisations;
- awareness-raising initiatives on the benefits of entrepreneurial activity in the general population; and
- creation of co-ordination or consultative bodies in the sphere of SME policy development.

Expansion of SME and entrepreneurship policy

Alongside the federal SME Act, a strong impulse was given to SME and entrepreneurship policy from two further sources. First, President Putin stated his commitment to revitalisation of the Russian Federation as a more entrepreneurial society and underlined it with highly visible government targets for SME development; by 2020, SMEs should contribute 50% of Russian Federation GDP (from a base of less than 25% in 2008) and 50% of total employment. Second, there was a step increase in the federal budget for SMEs

and entrepreneurship. Whereas the annual federal SME programme budget had been RUB 4 billion in 2008, it soared to RUB 19 billion in 2009, and increased further to RUB 20 billion in 2012 and RUB 23 billion in 2014. In 2009, the public development bank, Vnesheconombank (VEB), also embarked on a major SME financing programme by extending lines of credit to partner banks at subsidised interest rates and financing a range of non-bank financial institutions for purposes of SME lending. VEB also acquired SME Bank as a subsidiary, serving both to support the sustainability of the bank and to offer government rapid access to an infrastructure for reaching out to SMEs with financing.

Policy leadership and co-ordination at federal level

Several federal ministries and agencies have active SME and entrepreneurship policies

Several federal ministries and agencies operate SME and entrepreneurship policies, ranging from regulatory, tax and competition reforms to programme support for specific types of SMEs and entrepreneurs. For example, the Ministry of Agriculture allocated a budget of RUB 8.9 billion (USD 278 million) in 2015 for the development of farming businesses, and the Ministry of Education and Science allocated RUB 4.1 billion (USD 130 million) for the development of small enterprises in the scientific and technical spheres. Alongside this, the Ministry of Health and Social Development's self-employment assistance programme for the unemployed was estimated to have resulted in the creation of at least 127 000 new microenterprises and as many jobs in 2009 (NISSE, 2010). In all, 11 federal ministries and 13 federal agencies are involved. Table 4.1 presents the main policy thrusts of the most active federal ministries and agencies,

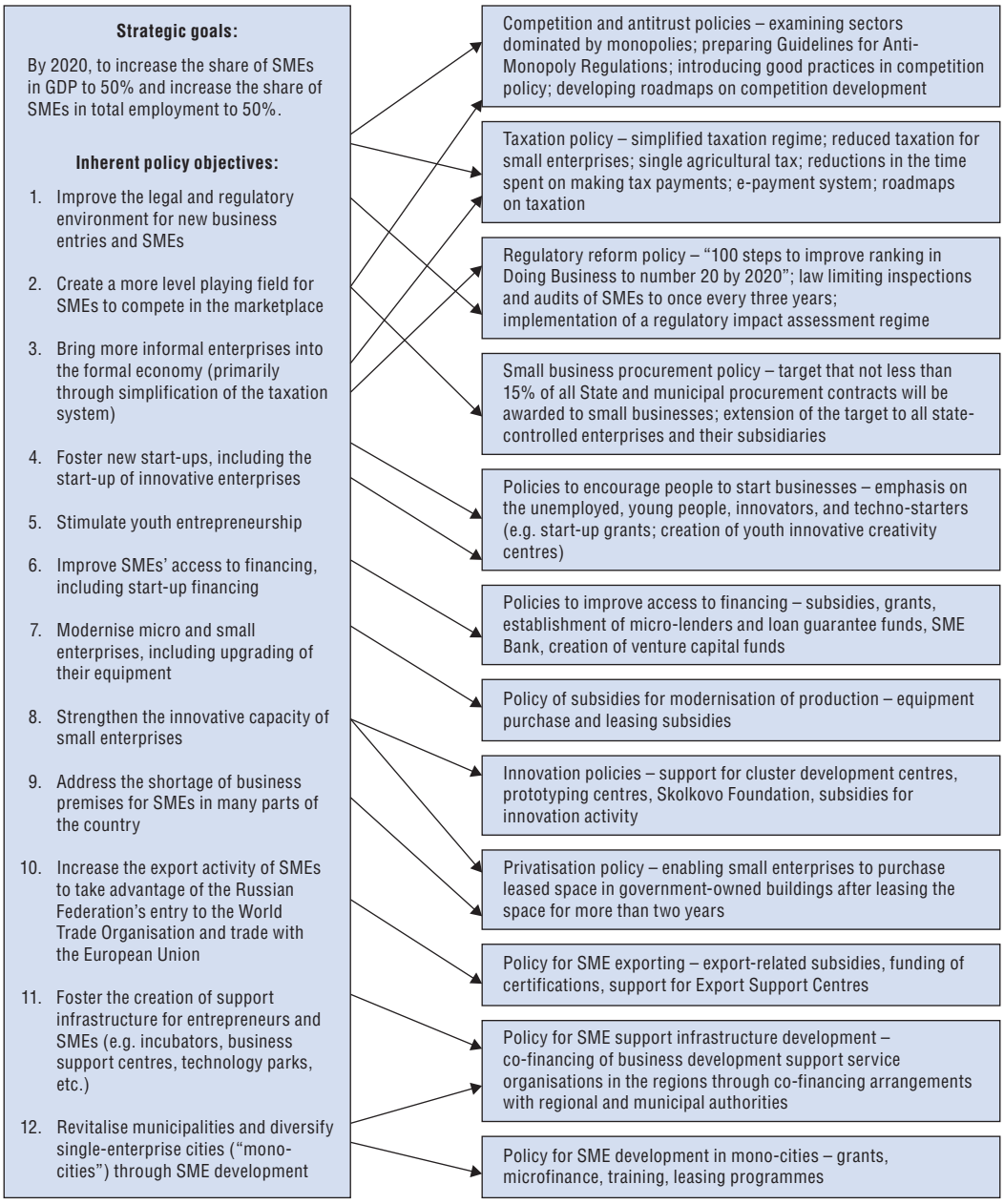
Table 4.1. **The SME and entrepreneurship policy activities of key federal ministries and agencies**

Ministry/Agency	Key activity
Ministry of Economic Development	Implementation of the federal SME support programme in collaboration with regions and municipalities
	Inter-ministerial co-ordination
	Monitoring and evaluation
Ministry of Agriculture	Business development support for farmers
	Access to finance for farm businesses and agricultural co-operatives
	Registration of land ownership rights for farm enterprises
Ministry of Labour and Social Protection	Promotion of self-employment
	Start-up grants for the unemployed
	Grants for rural enterprises
Federal Agency for Youth Affairs	Support for young entrepreneurs
Ministry of Education and Science	Support to innovative SMEs and start-ups
	Commercialisation of public R&D results
	Management skills for business innovation
Ministry of Public Health and Social Development	Subsidies for self-employment and placement of unemployed workers in SMEs
	SME development in the health and social services sectors
Ministry of Mass Communication and Media	Support to innovative firms
	Technopark programmes for high-tech industries
	Development of information and communications technologies in SMEs
VEB	Funding of credit institutions supporting SMEs

Source: Based on information from the Ministry of Economic Development, Russian Federation.

while Figure 4.1 identifies 12 major SME and entrepreneurship policy objectives and 12 major related SME and entrepreneurship policy activity areas across government.

Figure 4.1. **Federal SME and entrepreneurship policy objectives and activities in the Russian Federation**



Source: Based on information from Ministry of Economic Development, Russian Federation.

The Ministry of Economic Development steers and co-ordinates within government

Internationally, three main alternatives have been pursued for leading and co-ordinating public actors in SME and entrepreneurship policy. They involve either establishing:

i. a specific department for SMEs and entrepreneurship, usually within a Ministry responsible for industry, trade, commerce, or economic affairs; or

ii. an autonomous state agency for SMEs and entrepreneurship, often also tasked with overseeing regional support structures; or

iii. an independent SME and entrepreneurship agency, in which the private sector plays a key role.

The Russian Federation has adopted the first model, led by the Department of Small and Medium Business and Competition within the Ministry for Economic Development. This Department is responsible for designing and managing the federal SME support programme and co-ordinating with other ministries and agencies in identifying the broader needs and priorities of government intervention.

To facilitate SME and entrepreneurship policy development and co-ordination, the Ministry of Economic Development has established a cross-governmental working party on the implementation of SME support programmes including representatives of the Ministry of Economic Development, the Ministry of Labour and Social Protection, the Ministry of Agriculture, the Ministry of Regional Development, the Ministry of Education and Science, the Ministry of Industry and Commerce, the Ministry of Finance, and the public development bank VEB. The working party has elaborated and approved joint guidelines for ensuring co-ordination of state SME support programmes, facilitating self-employment by the unemployed, and supporting small innovative business and small business development in rural areas. It also monitors policy implementation across government.

Further inter-departmental co-ordination is provided by the State Government Commission for Competition and SME Development, chaired by the Deputy Prime Minister and involving several ministries, and by the State Duma, which is involved in strategy setting through its Committee on Economic Policy, Innovation and Entrepreneurship Development. These are clear and effective arrangements for inter-ministerial co-ordination.

Consultation with external stakeholders is strengthening

In addition to cross-government co-ordination, it is important that there are effective mechanisms to obtain the input of SMEs and entrepreneurs in policy formulation (OECD and UNIDO, 2004). This has been recognised by the 2007 federal SME Act, which specifies that consultative bodies will be created for SME policy. Thus, the cross-governmental working party on the implementation of SME support programmes includes representation from the national chamber of commerce and industry, the national branches of two major entrepreneurs' associations – OPORA Russia and Delovaya Rossiya (Business Russia)[1] – and the National Association of Peasant (Farm) Enterprises and Agricultural Cooperatives. Similarly, the State Government Commission for Competition and SME Development obtains inputs for policy proposals from the Russian Federation Chamber of Commerce and Industry, OPORA Russia, the Bank of Russia, and the Russian Union of Industrialists and Entrepreneurs.

There is evidence that some of these SME and entrepreneurs' associations are working very effectively in providing evidence and views on SME and entrepreneurship policy requirements. For example, the SME Committee of the Russian Federation Chamber of Commerce and Industry prepares an annual work plan dealing with SME issues, such as exporting, innovation, financing and training, and puts its proposals forward to the State

Duma and Ministry of Economic Development as well as attending weekly meetings of the Duma. Similarly, OPORA Russia produces annual surveys of the entrepreneurship climate that are used by various ministries.

A problem faced, however, is that the memberships of many of the major, established Russian business associations are focused on larger and more internationally-oriented SMEs and are not representative of micro and smaller businesses. Additional mechanisms are therefore needed for the effective "bottom up" articulation of SME needs for the design of programmes and regulations. Possible mechanisms for this purpose include support for the establishment of, and dialogue with, private-sector led forums and councils, associations of small and micro businesses and independent SME experts. A step forward has been made in this respect by the Agency for Special Initiatives (ASI), which has developed a highly consultative mechanism that engages a broad range of private sector actors and business associations in the process of constructing policy reform roadmaps. The recent creation of the Federal Business Ombudsman and the network of regional business ombudsmen will also help input information on SME concerns into government policy making.

It is also important to disseminate information to the public, media and key SME and entrepreneurship stakeholders to create widespread awareness of SME and entrepreneurship development challenges, policy directions and available policy support. Among the most common ways of achieving this are equipping organisations that have important interfaces with SMEs (such as banks, professional services and regulatory authorities) with appropriate information dissemination capacities on government policies and programmes; issuing regular bulletins in small business publications; appointing local ombudsmen who can answer queries on key issues; and making use of government websites to communicate information on SME policies and programmes. In the Russian Federation, work is underway to present accessible information in a single format on the official websites of federal authorities on SME and entrepreneurship regulations and support measures and how to access them. For example, *www.smb.gov.ru* provides information on how to start, develop and close a business and information on federal, regional and municipal support programmes. This is an important development, which could be enhanced with a range of other information dissemination activities.

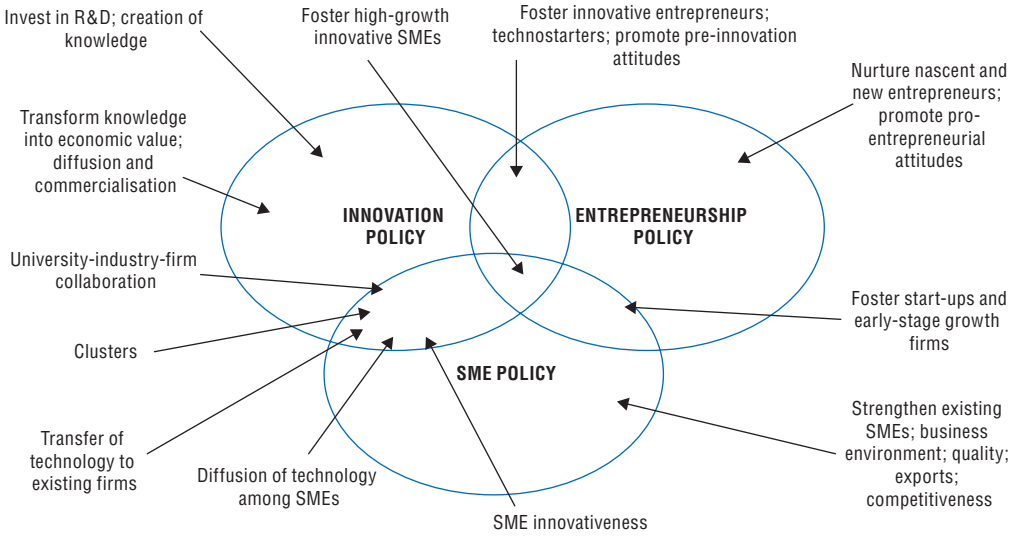
Room for more synergies between innovation, SME and entrepreneurship policies

Innovation is a national priority in the Russian Federation, as guided by the Innovative Russia 2020 Plan, including the key objectives of raising SME innovation capabilities and increasing the commercialisation of public research through innovative start-ups. The innovation and SME and entrepreneurship policy fields are therefore highly complementary. However, the policy fields are not currently integrated, resulting in missed opportunities for synergies.

Figure 4.2 presents a generic framework identifying typical SME, entrepreneurship and innovation policy interventions internationally and where they overlap. As a first step in building synergies within the Russian Federation, it would be helpful to build a specific map of the targets of existing innovation, SME and entrepreneurship policies in the Russian Federation. Having identified policy actions with linked objectives, efforts can then be made to create synergies, for example by promoting simultaneous

or graduated participation by SMEs and new enterprise in related programmes so they are able to benefit from spillovers of "Innovative Russia 2020" policy directions, increasing linkages between SMEs and the outputs of the largely state-driven research and development (R&D) system to help improve market-driven commercialisation outcomes, or targeting related programmes on the same geographical locations or industrial sectors.

Figure 4.2. **Intersection of SME, entrepreneurship and innovation policies**



Source: OECD categorisation of typical policy strands across countries.

Evaluation should be strengthened

The 2007 SME Act specifies that the efficiency of support measures is to be evaluated on an annual basis and communicated in an annual report on the state and development of SMEs. A single monitoring system is being introduced for the federal SME support programme, which will provide a picture of budget allocations and expenditures by region and type of intervention. In addition, regional and municipal authorities must provide information on the activities, outputs and outcomes of the programme components that they participate in, for example the number of new businesses started, the number of new jobs created and the number of existing jobs maintained as a result of the support.

However, there are a number of areas in which SME and entrepreneurship policy evaluation can be strengthened in the Russian Federation. First, the evaluation of outputs, outcomes and impacts should emphasise methods that enable the establishment of impacts net of the counterfactual. The key challenge is to ensure that programme impact, in terms of job creation or any other metric, is assessed on the basis of the additionality of the funding to the outcome achieved, which is generally based on control group studies (OECD, 2007). The evaluation information that is currently used usually comes directly from the beneficiary SMEs or support organisations, which is not a robust approach. In future, information on tax returns of assisted and non-assisted start-ups and SMEs could be more

systematically collected and used for this purpose. Second, the range of outcomes assessed should be widened to reflect the whole spectrum of objectives of the policy measures. In addition to stimulating business start-ups and creating and maintaining jobs, SME and entrepreneurship programme objectives commonly include increasing SME productivity, exporting, innovation, new firm survival, the creation of high-growth SMEs, a reduction in scale of the informal sector, and so on. These outcomes should also be assessed where relevant to the intervention objective. Third, it is important to extend monitoring and evaluation arrangements to all government programme interventions across all active government ministries and agencies.

Lack of an integrated SME and entrepreneurship master plan

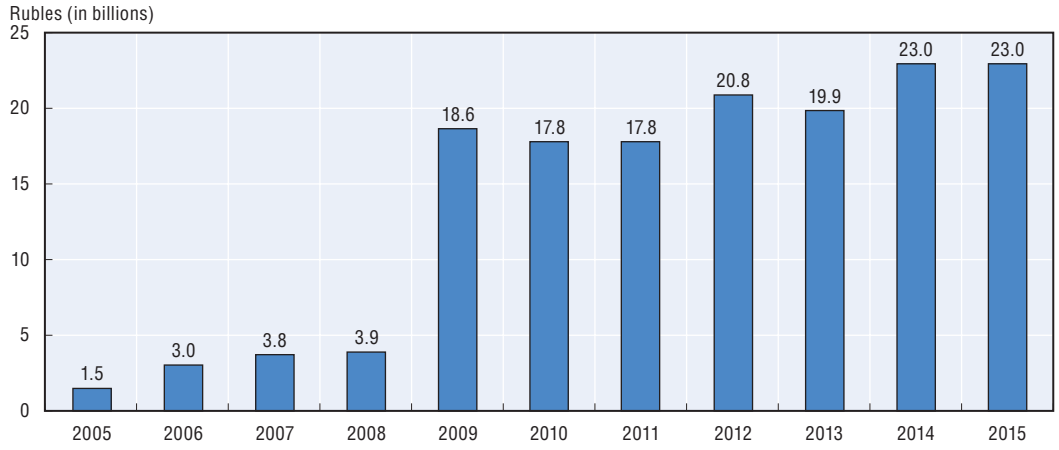
SME and entrepreneurship policy is most effective when guided by an integrated and well-defined vision across government that enables diverse policy instruments and programmes to be designed and implemented in a complementary manner. In the Russian Federation, however, a significant weakness is the absence of a comprehensive and coherent master plan document that lays out the federal SME and entrepreneurship development strategy and the associated objectives, responsibilities and measures of all the relevant policy actors. Crafting such a master plan would be very helpful in ensuring synergies and filling policy gaps across the relevant ministries and agencies. The development of the plan should follow the principles of, and provide a mechanism to promote, inter-governmental co-ordination, consultation with external stakeholders, synergies across policy areas and the use of monitoring and evaluation evidence.

The federal SME support programme

An enlarged budget, but room to grow

The federal SME support programme is the largest single support programme for SMEs and entrepreneurship in the Russian Federation, managed by the Ministry of Economic Development through co-financing agreements entered into with Russian regions and municipalities. The federal funding commitment to the programme has grown substantially in the last 10 years, from RUB 1.5 billion (USD 47 million) in 2005 to RUB 23 billion (USD 600 million) in 2015 (Figure 4.3). For 2013, an additional RUB 12.7 billion of support for SME development came from the Russian Federation Ministry of Agriculture (RUB 8.6 billion to support agricultural enterprises and peasant farmers) and the Russian Federation Ministry of Education and Science (RUB 4.1 billion to support the development of small enterprises in the scientific and technical sphere). Thus the total Russian Federation budget to SME support in 2013 amounted to RUB 32.54 billion. Regional and municipalities also committed budget funds for SME support, either as co-financing of Russian Federation SME support programme components or their own support initiatives, so the total public support for SME and entrepreneurship development is somewhat higher than that of the federal contribution to the federal SME support programme. However, although difficult to compare precisely, the level of funding of SME and entrepreneurship policy in the Russian Federation still appears to be far below that of the rates of approximately 0.02-0.04% of GDP found in countries such as Mexico, Poland and Thailand on narrow measures of SME spending (OECD, 2011; 2013; Swedish Agency for Growth Policy Analysis, 2011).

Figure 4.3. **Federal budget funds allocated to the SME programme, 2005-15**



Note: Expenditures for 2014 and 2015 are estimates.

Source: Data from the Russian Federation Ministry of Economic Development.

StatLink http://dx.doi.org/10.1787/888933271990

Over-emphasis on general financial subsidies

The federal SME support programme has the following major components:

1. Promotion of entrepreneurship.
2. Subsidies for business start-ups.
3. Assistance to the development of young people's enterprises.
4. Support of small innovative companies.
5. Support for leasing and purchase of modern production equipment and facilities.
6. Support of export-oriented SMEs.
7. Microfinance development.
8. Development of loan guarantee funds.
9. Support for municipal programmes.
10. Diversification of mono-industry cities.
11. Other direct SME support, e.g. entrepreneurial, management, and personnel training.
12. Support for the creation and development of business support infrastructure.

Together, these components aim to support the creation of new enterprises, motivate SMEs to modernise their production facilities and equipment, encourage SMEs to undertake innovation activity, expand the number of SME exporters and the volume of their export activity, improve access to financing for new enterprises and existing SMEs, and contribute to the development of entrepreneurial and management skills. The ultimate goals appear to be the creation and retention of jobs, regional development and diversification, and an enhanced contribution of SMEs to the Russian Federation's innovation, export, and economic growth performance.

As shown in Table 4.2, the different federal SME support programme components target different groups of SMEs and entrepreneurs, including support measures for building an entrepreneurship culture, for new entrepreneurs, and for existing smaller and larger SMEs. There appears to be a reasonable balance across these different SME target groups across the SME support programme.

Table 4.2. **Target groups of the Russian Federation SME Support Programme**

SME Support Programme Priority	Entrepreneurship promotion	Start-ups and new enterprises	Micro and small enterprises with less than 30 workers	Small and medium enterprises with 30 or more workers
1. Promotion of entrepreneurship	Yes			
2. Subsidies for business start-ups		Yes		
3. Assistance to the development of young people's enterprises	Yes	Yes		
4. Support of small innovative companies		Yes	Yes	Yes
5. Support for leasing and purchase of modern production equipment and facilities		Yes	Yes	Yes
6. Support of export-oriented SMEs			Yes	Yes
7. Microfinance development		Yes		
8. Development of loan guarantee funds			Yes	Yes
9. Support of municipal programmes	Yes	Yes	Yes	Yes
10. Diversification of mono-industry cities		Yes	Yes	Yes
11. Creation and development of business support infrastructure	Yes	Yes	Yes	Yes

Source: Information provided by the Russian Federation Ministry of Economic Development.

However, the weighting of the budget allocation across programme components should be reviewed. Table 4.3 presents how the budget was distributed during 2011-12. In 2012, around one-quarter of federal funds was allocated to microfinance and loan guarantee funds, a further one-quarter was allocated to grants and loans for leasing development and production modernisation and nearly 10% went to support for entrepreneurship and business start-ups, of which a significant proportion involved grants for unemployed people to start-up in self-employment. Thus more than one-half of the SME support programme budget was geared to widely distributed grants or loans to SMEs and start-ups. Much smaller budget allocations went to small innovative companies or SME exports, although these are key development priorities. In addition, relatively little was allocated specifically to the development of business support infrastructure as a platform for delivering support such as advice, consultancy, awareness, and networking, although some of these services were included to some extent as part of other programme components. The budget distribution was similar in 2011, although the budget for the leasing and production modernisation component was lower and support for small innovative companies and start-ups was higher.

At first sight, there appears to be an over-emphasis on generalised grants and loans to SMEs and start-ups. One of the concerns is the sector distribution of the grant and loan assistance, which includes a significant volume of state subsidy to enterprises in the wholesale and retail sectors. For example, although self-employment has increased, the principal activities of the newly self-employed were in domains such as beekeeping, tailoring, repair of household appliances, computer repair, mushroom cultivation, hairdressing, carpentry services, and apartment renovation. These sectors tend to have less potential for driving economic growth in the Russian Federation than enterprises in manufacturing in particular, and to a lesser extent in knowledge intensive business services. Whereas manufacturing has strong potential for productivity growth and exporting, wholesaling and retailing SMEs often suffer from problems of tax avoidance, low value added, low salaries and limited growth potential. Another issue is that the financial subsidies are not tied to the achievement of innovation, exporting and

productivity improvements or complemented by measures to develop entrepreneurial potential and help SMEs to grow by building their managerial and organisational capabilities.

Table 4.3. **Allocation of federal funds for the SME Support Programme in 2011-12**

No.	Measure	2011		2012	
		Funds allocated, RUB billions	Percentage of funding	Funds allocated, RUB billions	Percentage of funding
A.	*Subventions to regions for the state support of small and medium enterprises*	*16.0*	*89.7*	*18.57*	*92.3*
1.	Promotion of entrepreneurship and subsidies for business start-ups	2.04	11.4	1.86	9.2
2.	Assistance to the development of young people's enterprises	0.41	2.3	0.65	3.2
3.	Support of small innovative companies	2.48	13.9	1.95	9.7
4.	Support for leasing and purchase of modern production equipment and facilities	1.90	10.7	4.5	22.4
5.	Support of export-oriented SMEs	0.26	1.5	0.39	1.9
6.	Microfinance development	2.06	11.6	2.06	10.2
7.	Development of loan guarantee funds	3.42	19.2	3.31	16.4
8.	Support of municipal programmes	1.72	9.6	1.87	9.3
9.	Diversification of mono-industry cities	0.55	3.1	0.54	2.7
10.	Other	1.16	6.5	1.44	7.2
B.	*Creation and development of business support infrastructure*	*1.83*	*10.3*	*1.56*	*7.7%*
	Total	*17.83*	*100.0%*	*20.13*	*100.0%*

Note: "Other" is not specified in the information supplied but includes support for activities to promote entrepreneurship and to develop a system of personnel training, retraining and advance training for the small business sector (training vouchers, compensation for training/ retraining costs, and organisation of training events).

Source: Information provided by the Russian Federation Ministry of Economic Development.

StatLink http://dx.doi.org/10.1787/888933272304

Clearly there is a role for some direct grants to SMEs and start-up entrepreneurs in the public support system. However, some reduction in the proportion of expenditure allocated to generic financial subsidies could allow increased spending on more targeted support for specific kinds of enterprises that have important possibilities for growth and development, in particular manufacturing SMEs and start-ups, high growth potential firms, and exporting and innovating SMEs, and the development of an extended business services infrastructure offering diagnostic tools and consultancy, financing, management and workforce training support, and technical and incubation support to improve the management and organisational capacities of entrepreneurs and enterprises in key areas such as strategic management, innovation, and growth planning.

In order to make an informed judgement on the weighting that should be given to different programme components it is important to have information on the cost-effectiveness of the different actions with respect to the key objectives of the federal SME support programme as well as the budget distribution. Such information is not yet systematically available across the portfolio, which underlines the need for increased monitoring and evaluation activity. However, there is some more limited information from the Ministry of Economic Development's monitoring system on the cost of creating and maintaining jobs in SMEs for certain federal SME support programme components as well as some broader, not cost specific, information on expected targets and achieved results of all of the programme components. This information is presented in Table 4.4.

Table 4.4. **Summary of expected and achieved results across the Federal SME Support Programme portfolio**

SME Programme Component	Expected and achieved results	Measure of efficiency
Promotion of entrepreneurship	Expected: Not specified Achieved: Not specified	No performance data available
Subsidies for business start-ups	Expected: Annual target to support more than 10 000 start-ups. Achieved: In 2011: 9 400 supported entrepreneurs started new businesses, creating more than 26 000 new jobs. In 2012: 12 000 new businesses were started, creating 30 000 jobs.	Budget allocation of RUB 3.9 billion 2011-12; cost per new enterprise created RUB 182 242; cost per job created RUB 69 642.
Assistance to the development of young people's enterprises	Expected: Target to reach at least 30% of young people in every region using print, broadcast and social media, reach 100 000 young people each year through various activities, and create 2 000 enterprises annually.	No performance data available
Support of small innovative companies	Expected: Initial goal to support more than 4 000 innovative activities, creating more than 12 000 new workplaces and maintaining about 30 000 existing jobs. Achieved: In 2011: supported 2 300 small innovative enterprises creating 8 000 jobs and maintaining 22 000 jobs. In 2012: supported 1 500 innovative companies (no data available on jobs created or maintained). In 2012, the Innovation support infrastructure programme component attracted RUB 1.56 billion of the RUB 1.95 billion allocated for "support of innovative companies".	Budget allocation of RUB 4.4 billion in 2011-12 (RUB 2.48 billion in 2011); cost per assisted enterprise RUB 1.16 million; cost per job created or maintained (2011 only) RUB 82 666.
Support for leasing and purchase of modern production equipment and facilities	Expected: Not specified Achieved: More than 3 500 small companies received support in 2011-12, creating 13 000 jobs and maintaining 30 000 jobs.	Budget allocation RUB 6.4 billion in 2011-12; cost per assisted SME RUB 1.8 million; cost per job created or maintained RUB 148 837.
Support of export-oriented SMEs	Expected: Not specified Achieved: 2 200 export-oriented SMEs received support in 2011. As of 1 January 2012, 34 regional Export Support Centres had supported 2 859 entrepreneurs.	Budget allocation RUB 260 million in 2011; cost per assisted SME RUB 118 181. No data on jobs created or maintained. No budget or outcome data on Export Support Centres.
Microfinance development	Expected: Not specified Achieved: 70 regional and 60 municipal micro-lenders carrying out activities under the SME Support Programme. 20 000 loans advanced with an average loan size of RUB 450 000.	Budget allocation RUB 4.1 billion in 2011-12. No performance outcome data available.
Development of loan guarantee funds	Expected: Not specified. Achieved: 82 guarantee funds operating with total capitalisation of RUB 33.1 billion. Since 2006, 33 300 guarantee obligations approved to a value of RUB 92.9 billion.	Budget allocation RUB 6.7 billion for 2011-12. Insufficient performance data to measure impact.
Support of municipal programmes	Expected: Not specified. Achieved: 818 municipal programmes and 13 885 recipients supported in 2011, creating 17 083 new jobs and maintaining 29 784 jobs.	Budget allocation of RUB 3.6 billion 2011-12 (1.72 billion in 2011); cost per recipient (2011 only) RUB 123 874; cost per job created and maintained (2011 only) RUB 36 699.
Diversification of mono-industry cities	Expected: Not specified. Achieved: 84 municipal programmes have been supported during 2010-12, 34 500 enterprises supported and 20 000 jobs created.	Budget allocation of RUB 1.1 billion 2011-12. Insufficient data to calculate cost per assisted SME or per job created.
Creation and development of the business support infrastructure	Expected: Not specified Achieved: No available output data available for most support infrastructure organisations. In 2012 104 active business incubators were hosting about 1 600 small enterprises, employing 7 860 workers and generating combined annual turnover of more than RUB 7.4 billion. More than 1 000 companies have already passed through the incubation process.	Insufficient budget data to calculate the cost per enterprise or jobs created.

Source: Data supplied by the Russian Federation Ministry of Economic Development .

Some caution is needed in interpreting this information because interventions may have important objectives other than jobs and because the estimates of jobs created and/or maintained are not based upon robust control group evaluation methods. However, the data suggest two tentative conclusions. First, overall the programme interventions are creating businesses and jobs in the Russian economy. According to the monitoring data, more than 10 000 new businesses were started, more than 170 000 jobs were created and approximately 450 000 jobs were maintained in 2011. Second, when looking across those programme components for which information is available, it appears that the "support of municipal programmes" (RUB 37 000 per job created or maintained) and the "support of small innovative companies" (RUB 83 000 per job created or maintained) components of the budget were more efficient than the "leasing development and production modernisation" component (RUB 149 000 per job created or maintained). This backs up to some degree the notion that there may be an overemphasis on general financial subsidies in the federal SME support programme. This is also in line with much international experience in SME and entrepreneurship support programmes – blanket subsidies tend to be less effective than targeted support.

The federal SME support programme has demonstrated an ability to evolve in line with new priorities in recent years. For example, new programmes have recently been introduced for creating social enterprises, outsourcing goods and services by SOEs to SMEs, supporting Youth Innovation Creativity Centres, and promoting the energy efficiency of SMEs. This flexibility can be used to refocus the programme in the future on the most important priorities and the interventions that can demonstrate the greatest impacts and efficiency.

Conclusions and recommendations

SME and entrepreneurship policy has moved up on the government agenda in the Russian Federation during the last 10 years, reflecting an increased recognition of the role that new and small firms play in economic growth and diversification. A clear legal framework for policy has been set out in the 2007 federal SME Act, which identifies the basic objectives and instruments of policy. Presidential targets have been announced for growing SME activity. Budgets have also increased substantially through the federal SME support programme, the programmes of other federal ministries and the public development bank's SME financing interventions, although programme expenditure levels still appear to be low relative to several other countries.

There are also clear arrangements for steering and co-ordinating policy across government ministries and agencies, led by the Ministry of Economic Development, the State Commission for Competition and SME Development and the State Duma Committee on Economic Policy, Innovation and Entrepreneurship Development. Attention is also being paid to increasing consultation with SME associations on draft laws and regulations and providing better information on government websites on SME and entrepreneurship policies and programmes. On the other hand, the Russian Federation lacks an integrated medium-term strategic planning document for SMEs and entrepreneurship that outlines the higher-level goals of policy, the priority policy thrusts, the associated rationales, objectives, targets, measures, and expected impacts on the growth of the SME sector. Such a document could serve to guide different federal ministries and agencies in their policy development, make links across different SME and entrepreneurship policy interventions and between innovation policy and SME and entrepreneurship policy, and highlight how different target

groups of SMEs and entrepreneurs will be addressed by policy (distinguishing for example nascent entrepreneurs, new enterprises, existing SMEs and high potential entrepreneurs and SMEs). The use of policy evaluation could also be more strongly emphasised in the policy framework.

There is a strong emphasis on financial subsidies to SMEs and start-ups within the largest single programme for SMEs and entrepreneurship, the federal SME support programme, which comes at the expense of greater potential spending on targeted support for internationalising SMEs, business development services and management and workforce training. Better evaluation evidence is needed on the relative costs and benefits of the different programme components and target groups. However, the currently available information on costs per job created or maintained suggests that support for leasing and production modernisation is less cost effective than support for small innovative companies or support for tailored municipal programmes, while international experience suggests that more targeted support focused on innovative entrepreneurship and SME innovation tends to be more effective than blanket subsidies to existing enterprises.

The following recommendations are therefore offered to improve the strategic framework and delivery arrangements for SME and entrepreneurship policies in the Russian Federation:

Key policy recommendations on the strategic framework and delivery arrangements for policy

- Develop an integrated, standalone, medium-term, strategic master plan for SME and entrepreneurship policy through an inter-government and public-private consultative mechanism. The strategy should outline the vision, goals, targets, and main policy thrusts of government policy actions that will guide and co-ordinate all the relevant federal, regional and municipal ministries and agencies.
- With the master plan as the foundation, implement a mechanism for developing annual SME and entrepreneurship promotion work plans that integrate the actions of the relevant federal ministries and agencies. These work plans should show how the different actions will support SMEs and entrepreneurs at different stages of their development (e.g. nascent entrepreneurs, start-ups, growing SMEs, and restructuring in SMEs). They should also distinguish the support that is to be specifically targeted to manufacturing, innovative and exporting SMEs and high-growth entrepreneurship.
- Implement a formal system of independent SME and entrepreneurship policy evaluation. The system should define the primary and secondary objectives of each action and introduce robust evaluation methodologies, including control group studies, of the outputs, outcomes and impacts of the action as compared with the objectives. Utilising standard policy cycle models, it should also include arrangements for making use of the evaluation results to design more effective programmes and institutional delivery mechanisms.
- Reduce expenditure on automatic property and equipment grants to wide categories of existing SMEs and use the resources released for subsidies that are more targeted to investment in innovating, exporting, manufacturing, and high growth potential SMEs and start-ups, for expanded business diagnosis, advice, mentoring and consultancy services and for SME workforce training activities

Note

1. Business Russia is an independent non-profit organisation representing SMEs in dialogues with the government on policy setting. It has over 2500 members, 60 regional offices, and operates with more than 20 expert committees and 50 sector branches. See: *http://www.mgodeloros.ru/en*.

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OECD Studies on SME and Entrepreneurship
Russian Federation

Chapter 5

Federal SME and Entrepreneurship Programmes in the Russian Federation

This chapter examines federal programme support for building the capacities of SMEs and entrepreneurs and developing the business support infrastructure. It examines existing programmes for building an entrepreneurial culture, start-up grants, youth entrepreneurship support, support of innovative SMEs, support for production modernisation, support for export-oriented SMEs, microfinance, loan guarantees, support for tailored municipal programmes, support for diversification of mono-industry cities and development of the business support infrastructure. A number of areas for improvement are identified in these programme areas. The chapter also recommends introducing new measures for entrepreneurship awareness, entrepreneurship training, high-growth enterprises and large firm-SME supplier linkages and further increasing the scale and quality of the business development services infrastructure, including the business incubator system.

Improving existing measures

Entrepreneurship promotion

A number of relatively isolated actions for promoting positive attitudes to entrepreneurship are being developed in the Russian Federation through the federal SME support programme. These actions include profiling entrepreneurship and entrepreneurial role models in the mass media (e.g. through radio programmes and media articles) and supporting entrepreneurship conferences at national and local levels, although they are particularly aimed at young people rather than society as a whole. In addition, the federal SME support programme offers co-financing to regions and municipalities to offer training in entrepreneurship to people who express an interest. For young people in formal education, an additional set of federal SME support programme actions finance entrepreneurship education courses and workshops and entrepreneurship competitions. In parallel, the Federal Agency for Youth Affairs runs a competition programme for promoting school youth entrepreneurship, and the non-governmental organisation Junior Achievement Russia facilitates invitations to entrepreneurs to speak to students in school classes as well as offering entrepreneurship-related courses to school students at various levels. These courses include financial literacy, entrepreneurship in action, business games, the company programme, and business competitions. During the 2010-11 academic year, Junior Achievement Russia offered its business and entrepreneurship education programmes in 18 500 educational institutions, reaching 1.27 million students.

These existing actions are important but do not go far enough in their reach. For example, there is no widespread and persistent media campaign on entrepreneurship across the country and the entrepreneurship training offers are fragmented and not always of high quality. Given the importance of turning around a relatively weak entrepreneurship culture and creating a pipeline of future entrepreneurs in the Russian Federation, stronger efforts should be made to promote entrepreneurial attitudes and skills in the population.

Start-up grants for vulnerable people

A range of business start-up subsidies are offered across the Russian Federation with the aim of reducing tensions in the labour market and creating employment opportunities for people at risk of unemployment. The main scheme, called “Grants for Budding Entrepreneurs”, awards grants of up to RUB 300 000 (USD 9 400) to individual start-up entrepreneurs or owners of existing enterprises that have been operating for less than one year to cover the operating costs of a start-up. Priorities are given to the registered unemployed, workers at risk of dismissal, ex-military personnel, and youth (under the age of 30 years). To qualify for the subsidy, applicants must complete and pass a short-term training course that is offered on business basics and provide a plan for the proposed business project. No more than 10% of the assisted start-ups are to be in the retail and wholesale trade sectors.

A target has been established to provide subsidies to more than 10 000 new entrepreneurs per year. This implies that the subsidy programme is used by approximately 10% of new business entries annually. Programme monitoring data indicate that the subsidies are associated with good quality projects. Thus the Ministry of Economic Development estimates that the average employment per supported start-up is 2.5 jobs and that the survival rate after two years of operation is 91% of the assisted start-ups. This is much higher than the average two-year survival rate of employer enterprises typically recorded in OECD countries, which ranged from approximately 50% in Portugal to approximately 78% in Luxembourg in 2009 (OECD, 2014).

In addition, the Ministry of Labour and Social Protection offers a similar "Self-Employment Support Programme", offering a start-up grant of RUB 58 800 (USD 1 800) to unemployed persons who start an enterprise (the equivalent of 12 months of unemployment benefits), plus the same amount for each new job created for other unemployed persons. Alongside the grant, the beneficiaries can obtain help with developing a business plan and are given access to lawyers and accountants who can answer any questions they have. They are also offered training on how to start a business through the Ministry of Education. It is estimated that between 5% and 6% of registered unemployed persons apply for the self-employment benefits. Since 2009, about 600 000 unemployed persons have become self-employed through the programme, creating jobs for themselves as well as other unemployed persons. Of 68 000 people who applied for the programme in 2012, 19 000 opened a business (28%). The two-year survival rate of the businesses is approximately 60%.

From 2009-2012, the Ministry of Labour and Social Protection co-financed this programme with regional and municipal authorities. Including federal and regional funds, RUB 34 billion (USD 1 billion) was spent. However, there was evidence of programme abuses connected with funding going to businesses which did not start or hire. This led the federal government to stop its co-funding in 2012, except in 15 regions.

One of the strengths of the Self-Employment Support Programme is that it follows international good practice in complementing financial support with basic coaching and advice for start-up. This blending of support could usefully be built into the parallel Grants for Budding Entrepreneurs programme. Indeed, increased co-ordination between the two programmes would enable the building of a common base of advice and support.

Two other areas for improvement can also be suggested. First, admission to the Self-Employment Support Programme is somewhat complex. This adds to the cost of administration and does not necessarily increase the quality of supported projects, while also providing scope for abuse. The applicants are assessed for support on the basis of a written questionnaire and a meeting with a psychologist on their "business inclination" together with an assessment of the level of demand for the products or services being proposed, the qualifications and experience of the applicant, and the reasons why they are unemployed. If admitted to the programme, applicants must defend their business plans before an inter-ministerial committee, which is an intimidating process for the applicants. In other countries, the development of a business plan is usually part of the training provided once the applicant is admitted to the programme. Second, the level of coaching is very limited and could be boosted with more proactive help from a group of business support advisors who could guide new entrepreneurs through the start-up process. These issues can be addressed by simplifying the system of entry to self-employment support, for example by replacing the meeting with a psychologist and the presentation in front of

a committee with a more simple interview on the viability of the business idea and the commitment of the applicant to it and by offering systematic advice as well as financing to start-up entrepreneurs. Consideration should also be given to replacing some of the entry steps with the offer of a one-day orientation session for interested unemployed people so they can get a better idea of what it takes to be an entrepreneur and start and run their own business. This would be likely to result in some of the candidates realising that the self-employment option is not suitable for them and or could enable programme staff to identify inappropriate candidates.

In 2013, a new measure was introduced to the federal SME support programme for the creation of new SMEs for outsourcing. This measure involves provision of subsidies for up to RUB 20 million (USD 630 000) of the costs associated with the creation of new SMEs that provide business process outsourcing and services to SOEs through an agreement whereby the SOE agrees to transfer the provision of these services to the new company for at least two years from the date of the start-up grant.

Youth entrepreneurship

Support for youth entrepreneurship is provided by the "Assistance to the Development of Young People's Enterprises" component of the federal SME support programme, administered by the Ministry of Economic Development in partnership with the Federal Agency for Youth Affairs and regional and municipal governments. The main actions involve promotional campaigns, training programmes and the creation of Youth Innovative Creativity Centres aimed at potential young entrepreneurs of 16 to 30 years of age.

With respect to the promotion campaigns, the Federal Agency for Youth Affairs has set the target of reaching at least 30% of young people in every region using print, broadcast, and social media, attracting the participation of 100 000 young people each year in various promotion activities and events, and contributing to the creation of 2 000 youth-led enterprises annually. Regions that participate in the promotional activities are required to conform to the federal corporate identity programme, "You – The Entrepreneur", which is deemed important to ensuring a degree of national consistency in the mass media messaging.

The training programmes are required to involve not less than 72 hours of classroom time (although there is also an option to deliver it through distance learning and the internet). This comprises modules on "what is a business", "how to come up with a business idea", "how to formalise a product/service", and "building a business model" (phase one); "business planning", "technical sales", "company registration and organisational forms" (phase two); and "business management" (phase three). The training is linked to regional staging of the national business plan competition, "Young Entrepreneur of Russia", with participants in the competition being offered this training. It is also complemented by the provision of advisory services by coaches, business consultants and entrepreneurs who have successful experience in teaching young people about business to help young people start their businesses. In addition, the new starters can access the subsidy programme "Grants for Budding Entrepreneurs".

Support for the creation and maintenance of Youth Innovation Creativity Centres was introduced in 2013, with federal grants available of up to RUB 7 million (USD 220 000) per centre. It is planned to have 55 of these Centres, mostly located at higher education institutions, which will be equipped with the latest production technologies such as 3-D scanners and printers and laser cutters. The aim is to introduce young people working in

SMEs, or having an interest in entrepreneurship, to science and technology activities and to plant the seeds for commercialisation of scientific research and the creation of small innovative companies.

These interventions respond to a number of deficiencies in the business environment for youth entrepreneurship, including negative attitudes to entrepreneurship, the shortage of entrepreneurship-related skills and knowledge, and barriers to accessing financing. However, the targets for the numbers of participants have been set very low. In particular, only 2 000 youth business creations annually are targeted to be influenced by the national promotional campaign.

SME innovation

The SME innovation activity of the federal SME support programme supports new and existing companies to commercialise research and introduce innovative products and services and innovative technologies.

One of the major lines of support is the offer of subsidies, which are differentiated by the following classes of SMEs:

- *Start-ups and new enterprises*. Subsidies of up to RUB 500 000 (USD 16 000) for new innovative companies within their first year of operation, including companies created under the jurisdiction of higher educational institutions, for commercialisation of the results of intellectual activities (e.g. programmes for electronic computing, databases, inventions, utility models, industrial designs, typologies of integrated circuits, trade secrets and know-how).
- *Micro and small enterprises with less than 30 workers*. Subsidies of up to RUB 5 million (USD 150 000) to innovative micro and small enterprises for the costs of developing new products, services and production methods; purchasing machines and equipment related to technological innovations; purchasing new technologies (including rights to patents, licenses for use of inventions, industrial designs, utility models); and other pre-production costs.
- *Small and medium-sized enterprises with 30 or more workers*. Subsidies of up to RUB 15 million (USD 470 000) to innovative small and medium-sized companies for the costs of developing new products, services and production methods; purchasing machines and equipment related to technological innovations; purchasing new technologies (including rights to patents, licenses for use of inventions, industrial designs, utility models); and other pre-production costs.

Training certificates/vouchers can also be provided to all classes of innovative SMEs for training services from external providers to help improve their know-how in undertaking innovative projects (e.g. training on how to obtain a patent, how to conduct a marketing study, how to market abroad) and how to prepare for certification.

In parallel, the SME innovation support infrastructure is being developed through capital spending on new innovation support centres and funding towards the operating costs of existing centres such as technology commercialisation centres; cluster centres for shared access to high-tech equipment (Common Usage Centres); regional engineering, testing, prototyping and industrial design centres; technological competence and transfer centres; certification centres; and centres that train people in the use of equipment in the Common Usage Centres. There is also support available for centres of cluster development that will provide consultation and services to participants in innovative regional clusters.

In 2011-12 some 3 800 small innovative enterprises participated in these actions. However, there has been a recent decline in the number of companies participating and the share of the federal SME support programme budget allocated to the activity declined from almost 14% in 2011 to less than 10% in 2012 (a reduction of RUB 530 million or USD 17 million). One of the reasons may be that although the actions have been designed to support all types of innovation, including marketing, organisational, process and product innovations, there has been a strong emphasis on high-tech innovation to date. A broader interpretation of the types of companies and innovation projects that should supported would give a boost to this important programme activity. In addition, the existing subsidies and training vouchers for innovative SMEs should be complemented with business diagnostic support to identify the key development challenges for each firm together with targeted consultancy and networking support to help the firms to meet these challenges.

Plant and equipment subsidies

The goal of this activity of the federal SME support programme is to encourage small businesses to upgrade and modernise their equipment and production facilities. It offers various kinds of subsidy support for the leasing and/or purchase of new equipment and/or production facilities, which depend on the stage of development and size of the enterprise:

- *Start-ups and new enterprises*. A subsidy of up to RUB 1 million (USD 31 000) to defray the costs of leasing new production equipment.
- *Micro and small enterprises with less than 30 workers*. A subsidy of up to RUB 3 million (USD 95 000) to defray the costs of leasing new production equipment.
- *Small and medium-sized enterprises with 30 or more workers:* A subsidy of up to RUB 10 million (USD 315 000) to defray the costs of leasing new production equipment, together with an interest rate subsidy of up to a maximum of RUB 10 million (USD 315 000) per company for loans to construct new production buildings or acquire new modernised production equipment, and subsidies for the purchase of new equipment worth up to 30% of the cost of the new equipment to a maximum of RUB 10 million (USD 315 000).

The intent of the subsidies is essentially to enable SMEs to purchase the production equipment or facilities at the end of the lease, so in practice, the SMEs use the subsidy to cover their leasing instalments in such a way as to see the equipment or facilities transferred permanently to them at the end of the lease.

Although there is a clear need to improve the production capabilities of SMEs and evidence of market failure with respect to SMEs' access to financing in the Russian Federation, there is a danger that the operation of this programme could be associated with low additionality of public funding and high public costs compared with benefits. For example, in the case of the subsidy for the purchase of new equipment, assisted SMEs must first provide proof of purchase and registration of the equipment before they apply for the subsidy, which suggests that the beneficiary firms may not be those most in need of the subsidy. Furthermore, the subsidies may be used by beneficiary firms to reduce their costs rather than to change their business operations, for example by pursuing new markets, securing new supplier contracts, upgrading their production quality to compete in international markets, and improving their efficiency and productivity.

A welcome recent development in the effort to improve SME production practices, and productivity, is the introduction in 2013 of subsidies to promote the energy efficiency of SMEs through the use of energy-saving technologies and energy conservation practices. In this area, the federal SME support programme offers grants towards the costs of training professional staff on energy management systems, conducting energy audits, implementing energy management systems (and obtaining ISO 50001 certification), and acquiring energy-saving technologies (e.g. interest rate subsidies on lease payments and loans).

Export subsidies and Export Support Centres

State support of export-oriented SMEs has been a component of the federal SME support programme since 2005. The objective is to increase the volume of exports by Russian SMEs and increase the share of SMEs in Russian exports by addressing difficulties in obtaining credit, high interest rates, the complicated search for partners in foreign countries, a shortage of information on the conditions of product entry into foreign markets, a shortage of skilled personnel, and problems related to customs procedures.

Two main types of subsidy are provided:

- *Subsidies for first-time exporters:* A subsidy of RUB 660,000 (USD 21 000) towards the costs of a first export activity, such as interest on export credit loans, certification of goods, legal protection of intellectual property, participation in overseas exhibitions, and/or for training and professional development in exported-related issues.[1] The subsidy is issued upon proof of the first export transaction.
- *Subsidies for existing exporters*. Compensation for costs of interest on export credit loans, certification of goods, legal protection of intellectual property in foreign markets (e.g. inventions, brand names trade marks) and participation in overseas exhibitions.

In addition, the activity provides support for the creation and operation of Export Support Centres in the regions providing business development services to exporters.

During the period 2005-09, the exporter support reached RUB 392 million (USD 12 million) but benefited only 575 enterprises in total, located in 36 regions. To increase impact, an additional federal budget allocation of RUB 2 billion (USD 63 million) was introduced in 2010 and the co-financing rate offered to regions increased to 95%. However, even with these changes, only 42 regions received the support in 2011 and only 40 in 2012. Overall, less than 2% of the Federal SME Support Programme budget was allocated to SME export promotion in 2011 and 2012. This does not reflect the level of priority that SME exporting should be receiving in the context of the recent increases in the Russian Federation's trade integration.

One of the potential downsides of the operation of the subsidy programme for first-time exporters is that the subsidy is only issued upon proof of the first export transaction. This may be associated with two problems: the assistance may not be additional to what enterprises would otherwise undertake; and SMEs may be deterred from exploring risky markets because the compensation will only be provided for successful export sales. Consideration should therefore be given to offering subsidies for export-related activities in advance of export sales.

Subsidised micro-loans

The micro-finance activity of the federal SME support programme aims to improve access to financing for non-bankable young enterprises by creating and capitalising microfinance organisations. To receive the support, these organisations must not offer

loans of more than RUB 1 million (USD 31 000) and 12 month terms, must charge an interest rate of 10%-12%, much lower than the usual rates of 30% or higher offered by other microfinance institutions, and must offer loans to young enterprises that have been registered for less than one year.

This action is very important for providing access to credit for new micro enterprises that are seeking a small credit amount, lacking a credit history and track record, or are remotely located. Some 70 regional and 60 municipal micro-lenders are supported, which account for approximately 21% of the microfinance market in the country. In return for funding support, the supported microfinance organisations are required to undergo annual performance assessments that evaluate the efficiency of their personnel, the quality of their business processes and internal accounting information, the quality of their loan portfolios, and the reliability of their accounting data.

Regional loan guarantee schemes

This line of the federal SME support programme aims to improve access to bank and lease financing for SMEs by providing capital to public regional loan guarantee funds that guarantee credit extended to SMEs by commercial banks, insurance companies, and leasing companies. The selection of regional loan guarantee fund organisations for support is carried out on a competitive basis. The amount of the guarantee that these organisations can offer must not exceed 70% of the loan amount to a maximum of RUB 100 million (USD 3.1 million) per SME. The guarantee can also apply to loans to SME support infrastructure organisations to a maximum of RUB 1000 million (USD 31 million). In April 2013, there were 82 supported loan guarantee funds in 70 regions, which had approved about 33 300 guarantee obligations totalling more than RUB 92.9 billion (USD 2.9 billion). The guarantees are associated with about 2% of the loans to SMEs in the Russian Federation, which provides valuable assistance to otherwise potentially un-bankable SMEs.

Tailored municipal programmes

The federal SME support programme supports approximately 800 municipal SME support programmes each year with a 70% funding contribution for actions that are tailored to their economic development priorities. The major measures for which co-financing is available include: 1) creating an entrepreneurship support centre or business incubator; 2) providing grants to novice entrepreneurs for starting their own business, including for settling the first instalment of lease payments; 3) capitalisation of micro-lenders; 4) training programmes for novice entrepreneurs; 5) funding part of the costs associated with the payment by SMEs of the interest on leases, linking to power grid facilities, etc.; and 6) marketing research, investment environment assessments, exhibition/trade-fair activities, and media promotion of local entrepreneurial activities. The amount of funding support available depends on the population size of the municipality: up to RUB 80 million (USD 2.5 million) for municipalities with a population of less than 50 000 residents; up to RUB 150 million (USD 4.7 million) for municipalities with a population of between 50 000 and 300 000 residents; and up to RUB 300 million (USD 9.4 million) for municipalities with more than 300 000 residents. This is an effective mechanism for providing support that takes into account the sector development priorities, specific features and economic capacities of specific municipal corporations.

Diversification in mono-industry cities

An additional line of federal SME support programme funding is available to selected municipalities that depend on single industries ("mono-industry cities"). These cities have typically lost their previous economic function under central planning and are now suffering from high unemployment and outmigration. They have low shares of SMEs in their economies and are struggling to create new activities. The support is available to encourage every fourth mono-industry city to develop local SME and entrepreneurship support programmes, which can include support to SMEs for finance, access to property/premises, consulting and information services and workforce training support, grants and training for new entrepreneurs, and the creation of business incubators and technoparks. The Russian Federation share of co-funding of these activities is up to 95%.

The criteria for categorising localities as mono-industry cities were approved at meetings held in 2009 of an inter-agency working party dealing with reducing the negative impact of the financial crisis on the social and economic development of mono-industry cities. This led to a list of more than 330 mono-industry cities in the Russian Federation, of which 84 were supported during the 2010-12 period. The priority municipalities for assistance are selected through annual plans developed together by federal, regional, and municipal authorities. This provides important support to economic diversification and job creation in the places with the most promise, while accepting the need for some shrinkage in this settlement type.

Filling programme gaps

An entrepreneurship promotion campaign

A key policy priority in the Russian Federation must be to generate more favourable attitudes to entrepreneurship in society and increase the numbers of people interested in becoming entrepreneurs. However, existing entrepreneurship promotion activities are carried out separately and to varying degrees by regional and municipal authorities. These local efforts should be supported by a broader-based, comprehensive, national entrepreneurship promotion campaign. This should be aimed at promoting a change in mind sets among potential entrepreneurs and at promoting the institutional changes needed to transform the Russian Federation into a more entrepreneurial society. The campaign should be co-ordinated by the national government working in partnership with private sector organisations and the media.

There are an increasing number of examples of federal governments initiating and supporting the implementation of national entrepreneurship promotion campaigns with the intent to stimulate a more entrepreneurial society and economy. The first step in achieving this is creating more awareness of entrepreneurship among the population to attain an improvement in pro-entrepreneurial attitudes and reinforce the fact that entrepreneurs come from all walks of life and can make their first step into business at any age. These campaigns can include a combination of policy measures, such as entrepreneurship-oriented television or radio programmes to raise the profile of small business/entrepreneurs in regions of the country, entrepreneurship awards and recognition programmes to recognise achievements of entrepreneurs, coverage of entrepreneurial stories in the print and social media, and large entrepreneurship-related conferences and events, which not only serve to promote entrepreneurship but also offer learning environments for attendees. The Russian federal SME support programme provides funding

support for "promotion of entrepreneurship" to create a positive image of entrepreneurs, which can include use of the mass media, regional entrepreneurship conferences, and activities to promote entrepreneurship in the education system, but this is all done on a local and regional level, depending on the interests of regional and municipal authorities. The Russian Federation Ministry of Economic Development has not yet developed a national strategy for entrepreneurship promotion, with common messaging and national reach that could have more of a significant impact on raising the level of entrepreneurship in the country.

An example of an integrated approach to the promotion of entrepreneurship is illustrated by the case of Finland, where the lack of such promotion was identified by Finnish experts as a barrier to building an entrepreneurship culture. Thus, this became a policy priority of the Ministry of Trade and Industry when launching its Entrepreneurship Policy Project in the late 1990s (see Box 5.1).

Box 5.1. **An Integrated Approach to the Promotion of Entrepreneurship in Finland**

In the 1990s, the lack of entrepreneurship promotion was seen by experts as a barrier to building an entrepreneurship culture. Although attitudes to entrepreneurship in Finland were highly favourable, this had not translated into higher start-up rates. For Finns to embrace entrepreneurship, they required a higher degree of "societal readiness", which could be created through awareness-raising activity.

Within the context of the government-wide Entrepreneurship Project in 1999, led by the Ministry of Trade and Industry (MTI), events to promote entrepreneurship – conferences and seminars – were coordinated as part of an overall entrepreneurship policy. Regional Entrepreneurship Forums were built into the framework of this project and arranged throughout Finland to increase the positive image of entrepreneurship and business activity, to increase regional co-operation in the promotion of business activity, to convey the interests of public authorities towards business and to create more awareness of the role of the Employment and Economic Development Centers (EECs) as regional operators promoting and supporting business. These regional forums were organised on a regular basis in co-operation with the EECs.

A new initiative of the Entrepreneurship Project was the Golden Key Award (Kultainen Avain), a project to promote Finnish entrepreneurs. Each month, each of the 15 EECs selected 10-12 good candidates from their region and presented these nominations to an Awards committee chaired by the Minister of Trade and Industry and including MTV3 and a number of other high level Finnish leaders. Four or five entrepreneurs were chosen every month to receive the Golden Key Diploma and presented with awards by the Minister at Regional Forums.

To support these promotional efforts, MTV3 produced a weekly television programme based on features about these award-winning entrepreneurs and aired them each Saturday and Monday. This was a partnership between MTV3 and the MTI and partly financed by MTI. This initiative led to increased media exposure of entrepreneurship. The print media also became more active in writing about local and regional entrepreneurship and enterprise policy. A spin-off of this promotion activity was the creation of more Finnish entrepreneur role models.

Source: Ministry of Trade and Industry, Finland

A basic entrepreneurship training course

Everybody with the intention to start a business in the Russian Federation (both youth and adults) should have access to a good quality, basic, low cost entrepreneurship training course that covers technical issues in how to start-up and key practices for business success. However, this is not currently in place, since although the federal SME support programme includes entrepreneurship training in the list of actions it can support, there is uneven availability across the country and the quality of the courses offered is very variable. There is therefore scope for introducing a standardised basic course across the country, which could be offered physically in face-to-face workshops, or as a virtual training course delivered through the internet.

A promising recent development to build on is the introduction to the Russian Federation of the international EMPRETEC training programme (created by the United Nations Conference on Trade and Development) by the SME Bank arm of the Vnesheconombank (VEB). This 6-day programme, given by certified EMPRETEC trainers, aims to impart personal entrepreneurial competencies to aspiring entrepreneurs and help promising entrepreneurs build innovative and internationally-competitive SMEs. In many countries, the programme has managed to create a new breed of dynamic, highly-motivated, self-confident and focused entrepreneurs. Therefore an option for providing appropriate basic entrepreneurship training would be to provide federal resources for delivery of EMPRETEC Russia entrepreneurship training workshops in all parts of the country by training trainers and subsidising the training costs for a large number of aspiring entrepreneurs through the use of training certificates/vouchers. This would help bring aspiring entrepreneurs closer to starting a business and improve their chances of success once started.

Further efforts should also be made to make standardised entrepreneurship training programmes available for potential entrepreneurs ready to actually pursue the starting of their new business. Some organisations do provide entrepreneurship training programmes in the Russian Federation, such as the Russia Centre for Entrepreneurship, but they are not available regularly and in all regions, and are also of variable quality and consistency. Thus, Russians wanting to learn start-up knowledge and skills are disadvantaged in being able to access the information and training they need. Various approaches have been taken to resolving this challenge internationally. One option is to offer a globalised recognised and standardised entrepreneurship training programme, such as Start and Improve Your Business (SIYB), a practical business skills training package for existing and aspiring entrepreneurs and small business owners/managers.[2] The SIYB programme is a product of the International Labour Organisation (ILO) and has been used in over 100 countries, including a pilot project in the North Caucasus (in Russian). The programme is generally delivered by small enterprise development organisations with training by the ILO (training of trainers, training of institutions, training of Master Trainers), and includes all the guides and materials (manuals, kits) necessary to train entrepreneurs on generating their business idea, starting their business, and improving their business. Upscaling the SIYB programme for implementation across the Russian Federation would provide a standardised approach to making entrepreneurship and business management training available in all regions. The federal Ministry of Economic Development could spear-head this initiative in co-operation with regional and municipal authorities with support from the federal SME support programme.

Another option is to develop and offer online access to entrepreneurship training programmes, which could provide even broader coverage. For example, in the United States, the SCORE Foundation provides access to a free online training programme that includes a five-module "Simple Steps to Starting a Business" workbook that takes nascent entrepreneurs through start-up basics, the business concept, marketing planning, financial projections and funding sources and next steps.[3] In addition to this online resource material, which includes templates and tools, five 3-hour module workshops based on the workbook material are offered in local communities, including one-to-one mentoring with a trained SCORE expert.[4] An example of a federal government initiative to offer web-based information to large numbers of entrepreneurs and SME managers to improve their knowledge and skills is the US Small Business Administration's (SBA) on-line Learning Centre. Through this mechanism, the SBA offers several online training courses for new entrepreneurs and existing small businesses aimed at enhancing their knowledge base in a number of business-related areas (see *https://www.sba.gov/tools/sba-learning-center/search/training/*).

A high-growth enterprise programme

Missing from current federal SME and entrepreneurship programmes is a set of specific and tailored measures for high-growth potential start-ups and SMEs. The development of these enterprises, and the entrepreneurs who lead them, has become a strong focus of policy in many other countries, reflecting the disproportionate benefits they have for employment generation and economic growth (OECD, 2013a). There are of course lines of assistance for start-ups and for SME development more generally that high-growth potential firms can access, but more specific and targeted support is merited for this group. For example, whereas the start-up subsidies offered by the federal SME support programme, the Ministry of Agriculture, the Ministry of Labour and Social Protection and the Ministry of Public Health and Social Development aim to increase the quantity of new start-ups, with priority given to assisting the unemployed and at-risk individuals, a high-growth entrepreneurship programme would focus more on the quality of the entrepreneurial activity, with efforts made to attract and support starters with higher entrepreneurial ability (measured for example in terms of their education, technical knowledge, experience, social capital). Similarly, existing high-growth potential SMEs may access standard subsidies for equipment, innovation and exporting, but a high-growth entrepreneurship programme would go further by offering a small number of firms business diagnosis, mentoring and consultancy support alongside the subsidies. The total value of support offered per high-growth potential entrepreneur or SME would generally be higher than for standard entrepreneurs and enterprises, but with many fewer companies supported than the standard schemes. For example, Denmark's Regional Growth Houses initiative targets less than 3 000 enterprises per year (OECD, 2013a).

A high-growth entrepreneurship programme in the Russian Federation would firstly require a method for identifying high growth potential enterprises. Often, these are associated with founding entrepreneurs and entrepreneurial teams that have a high degree of human and social capital and are based on technology development or innovative business models. Some basic information would be needed on the characteristics of prospective programme participants to permit an initial assessment

of their likely growth propensity, including for example education level and size of the founding team and the product and sector of the enterprise. In addition, an interview with the entrepreneurial team would be needed to establish their level of growth ambition for their enterprise and the realism of this ambition. Selected enterprises would then be offered an integrated package of assistance that includes such supports as coaching and mentoring by experienced entrepreneurs, consultancy services, technology development, management training in growth strategies and market development, leadership development, network building, and access to seed and venture capital.

There are different models in operation internationally for working with high growth-potential enterprises. An example is the package of initiatives for supporting High Potential Start-Up (HPSU) Companies that has been developed in Ireland, as described in Box 5.2. Another type of approach is Finland's Growth Firm Development Service (MTI, 2007). Instead of waiting for firms to approach it, the Service actively scans the environment for potential high-growth firms with the idea of developing individually-customised support packages for them. When identified, the consultants working in the Growth Firm Development Service offer growth analysis sessions to the firms. Based on the growth analysis, the firm-specific needs for achieving growth are prioritised and appropriate services provided such as financing, internationalisation support, mentoring, technology support, training, and other forms of intensive consultancy aimed at addressing particular growth challenges.

A business accelerator model could also be tried, such as Mexico's Business Acceleration Programme (OECD, 2013b). In 2011, the Mexican programme supported 50 business accelerators, mostly in Mexico but with a handful in key foreign markets such as the United States in order to provide Mexican firms with better international market access. The accelerators work with the most promising start-ups from the National System of Incubation and help existing companies in specialised technology fields (e.g. medical devices, aerospace, automotive, biotechnology, cloud computing, micro-electronic devices) to migrate to higher value markets. Activities include workshops on market and technology trends and opportunities, diagnosis of company development needs, creation of company development action plans and innovation strategies, integration of management tools, assessments of technical and marketing readiness, and identification of partnering opportunities with companies in other locations.

Such a high-growth enterprise programme could be developed in the Russian Federation as a separate line of the federal SME support programme. The success of such an initiative would be down to identifying small numbers of high-growth potential firms, diagnosing their growth challenges and providing a range of support to help them meet these challenges. It should be recognised that only a small proportion of the selected firms would be successful and that it will not be possible in advance to identify these specific firms. It is the growth benefits from the subset of successful firms from among the programme participants that would justify the programme expenditure.

Box 5.2. **Support Package for High Potential Start-Ups, Ireland**

The approach

This programme, run by Enterprise Ireland, provides an integrated support package to help high potential start-ups (HPSUs) to start, grow, innovate and win export sales on global markets. A HPSU is defined as a company which is: based on technological innovation; likely to achieve significant growth within 3 years of start-up (at least sales of EUR 1 million per annum and employment of 10); export-orientated; and led by an experienced team with a mixture of technical and commercial competencies.

An extensive range of services is offered, all geared towards helping the companies win international sales. Between EUR 150 000 and 400 000 is available to HPSUs in government equity investments (depending on the company's funding need and expected value for public money in terms of job and export creation), with an average funding package of EUR 250 000. The provision of financing in the form of equity rather than grants ensures that the companies are funded up front but that the state shares in the success of the enterprise if it is successful. The private sector also makes equity investments in these firms alongside the government.

Together with the equity financing, HPSUs are offered the following wide package of Enterprise Ireland services throughout their development (some of these services are also open to other types of firms):

HPSU Feasibility Grant	To investigate the viability and potential of a high potential start-up and develop an Investor Ready Business Plan.
Mentor Grant	To support the cost of an experienced business mentor to assist in the start-up phase or advise on specific areas of the plan.
Excel at Export Selling	A series of workshops aimed at rapidly embedding good practice international sales tools into the sales teams of Irish companies.
Innovation Voucher	Innovation Vouchers, worth EUR 5 000, to assist a company to work with a registered college or knowledge provider to explore a business opportunity or technical problem.
New Frontiers Entrepreneur Development Programme	A national incubation programme that offers successful applicants a package of supports to accelerate their business development including leadership skills development.
Innovative HPSU Fund (Equity)	Both first-time and follow-on equity investments in HPSUs are made on a co-funded basis with private investors.
Internet Growth Acceleration Programme (iGAP)	An intensive six-month management development programme aimed exclusively at high potential internet companies that succeed in a competitive application process including practical learning from world-class facilitators.
Competitive Feasibility Fund - Aviation	A fund to assist start-up companies to investigate the viability of a new growth-oriented business proposition in the aviation sector. It is also open to established companies or groups of businesses that wish to examine the potential for expansion, diversification or spinning out a new enterprise in the industry.
Competitive Start Fund	A EUR 50 000 equity investment to support the growth of start-up companies that have the capability to succeed in global markets.
Competitive Feasibility Fund for Female Entrepreneurs	A fund to assist female entrepreneurs to investigate the viability of a new growth orientated business that can succeed in global markets.

Results

Enterprise Ireland supported 97 new HPSUs in 2012, including 14 spin-outs from HEIs. All the firms received government equity investments, worth a total of EUR 22 million and leveraging an additional EUR 23 million from private investors. In addition, 60 HPSUs accessed the Competitive Start Fund and 12 participated in the New Frontiers Programme. In all, the 2012 start-ups committed to creating a total of 1 586 new jobs and generating over EUR 300 million in annual sales by the end of 2015. From 2000-12, a total of 965 HPSUs were supported, which were responsible for employing over 30 000 people directly and indirectly in the wider economy, and had combined exports of over EUR 1.5 billion.

Box 5.2. **Support Package for High Potential Start-Ups, Ireland** *(cont.)*

Success factors

The success of the programme is based on two factors:

- Clear targeting on companies which have high potential growth.
- A comprehensive package of support measures.

Problems and responses

Some entrepreneurs reported that the early support package did not meet some of their needs. In response, several new initiatives were introduced. For example, Competitive Feasibility and Competitive Start Funds were introduced to provide young companies with early stage funding to test the market for their products. A new initiative was also established to boost the number of innovative, export-oriented businesses led by female entrepreneurs.

Relevance to the Russian Federation

This is an example of an effective high growth enterprise programme combining targeted equity investments in selected companies with access to existing strategic management, innovation and growth planning support.

Further information

www.enterprise-ireland.com/en/funding-supports/Company/HPSU-Funding/

Source: Information supplied by Enterprise Ireland.

A supplier development programme

Many governments operate programmes to support local SMEs to act as suppliers to large, internationally-active firms, and principally inward foreign direct investment operations, with the aim of improving the market access of SMEs and upgrading their capabilities, as well as improving conditions for further inward investment (OECD, 2008). The programmes generally involve a combination of matchmaking among foreign firms and domestic SMEs, i.e. brokering supplier partnerships, and provision of diagnosis, consultancy and financing support to small groups of SMEs identified as having the potential to supply international firms if they increase their quality, efficiency and timeliness of supply. Although the Russian federal government has programmes for building SME linkages with SOEs and public sector purchasers, as well as an innovative clusters programme, there is not a dedicated supplier development programme targeted at creating linkages between SMEs and foreign inward direct investors.

Supply chain development programmes are based on the principle that, as well as offering new sales opportunities, local linkages between SMEs and foreign direct investors assist SMEs to adopt best practice technologies through a range of channels such as demanding contracts, rigorous quality monitoring, sharing of information on production processes, sharing of product specifications and company visits for joint product and process development. SMEs may also be able to build on the initial connection with a particular foreign investor to supply other large firms or to start to export directly, while the improved techniques they develop often spread to other domestic SMEs through a demonstration effect, mobility of staff, and linkages down their own supply chain. However, the linkages often have to be created, since foreign investors are more likely to focus initially on their existing supply chains in their home country and third countries.

A supplier development programme in the Russian Federation could include actions to identify large FDI 'anchor firms' willing to develop a local supply chain, identify potential local SME suppliers to these anchor firms, provide diagnosis of the improvements that would be required for SMEs to gain the supplier contracts (in terms of reducing costs, increasing quality, shortening delivery times and increasing consistency of supply), and offer capacity-building support in the form of training, consultancy and financing to potential suppliers to reach these standards. The anchor companies themselves could be enrolled in the programme to act as coaches to potential supplier firms, either directly or in supplier development conferences or circles, and potentially to participate in the funding of some of the SME support. The National Supplier Development Programme in Mexico is presented in Box 5.3 as an example of such a programme.

Box 5.3. **National Supplier Development Programme, Mexico**

The approach

The Mexican National Supplier Development Programme supports groups of SMEs of various kinds (size, growth phase, etc.) and sectors (aerospace, auto parts, electronics, agri-food, construction, tourism, retail, etc.) to access international markets and upgrade their competences by creating a series of local SME supply chains each revolving around one export-oriented large firm or foreign investor. It works in four major steps:

Step 1: Active promotion to identify large "anchor" firms that can benefit from strengthened local supplier relationships and are willing to co-operate in helping to develop the capacity of a group of potential SME suppliers.

Step 2: Identification of a small cluster of SMEs that are interested in acting as suppliers to the anchor firm. For each anchor firm, approximately 10 potential suppliers tend to be selected.

Step 3: Intensive diagnosis of the necessary improvements to the capacities of the potential SME suppliers.

Step 4: Consultancy and training to the SMEs to upgrade their products and production processes to meet the standards and quality specifications of the anchor firm.

The Ministry of Economy maintains a body of approved consultants who receive standardised training on how to deliver the programme. Their task is to recruit the anchor companies and potential SME suppliers, perform a diagnostic of the financial, technical and operative capacities of the SMEs in relation to the requirements of the anchor firm, and help the SME owners develop and implement an improvement plan. The process often involves coaching the SMEs through an ISO9000 certification process.

For example, in the retailing sector, a "Buy from Mexico" initiative was developed to train buyers from large international retail chains (e.g. Costco, Walmart) on how to work with small Mexican enterprises to improve their quality and to train SMEs on the capabilities they needed to sell to the big chains. The goal for the pilot phase was to work with five retail chains and 100 Mexican small businesses to produce 200 new business relationships over a six-month period. The SMEs were offered training courses on how to integrate into the supply chains of large retailers, mathematics for retailing, how to manage inventory levels, and how to negotiate, including online courses, webinars, and lunch and learn sessions. This was followed by coaching for 6-12 months as they started to receive opportunities to list their products with the chains. The government covered one-half of the project cost and each participating small business paid about USD 2 000. The SMEs were expected to increase their sales by 50%-75% over the following year as a result.

Box 5.3. **National Supplier Development Programme, Mexico** *(cont.)*

Results

SDPs have been developed in 20 different cities, producing significant regional benefits. In 2010, 80 large companies developed supply chain relationships with 5 674 SME suppliers. This enabled the supplier firms to increase their efficiency, improve their skills and management, and move into other markets, and seems to result in a wider change of mind set. The large firm buyers have also benefited from decreased lead times and cost reductions in supplies.

Success factors

Key factors behind the success of this programme are:

- a systematic implementation model that is applied across diverse sectors;
- an approved list of consultants who are knowledgeable about the model and competent in its execution;
- the availability of funding to the SMEs to make necessary quality improvements.

Problems and responses

One of the main problems has been recruiting anchor firms to the programme. This has been overcome by aggressive efforts by the programme consultants to sell the benefits of participation to large firms. Another challenge has been to develop consultants and consultancy firms to deliver the SME support. Consultants have been trained in the approach and have developed a high degree of competency in the area following several years of programme implementation.

Relevance to the Russian Federation

Opportunities to use foreign investors and large private domestic firms to increase the market access and competences of SMEs are not fully exploited in the Russian Federation. Those efforts that do exist focus on improving linkages between SMEs and SOEs. This suffers from two limitations. First, they do not address non-state-owned anchor firms. Second, they do not incorporate the intensive capacity building work of the Mexico SDP. Without training and consultancy and targeted investment support, only SMEs with current capacity can benefit from the linkage opportunities.

Further information

Ministry of Economy, Mexico: *www.economia.gob.mx*

Source: OECD (2013b) Mexico Key Issues and Policies, OECD Studies on SMEs and Entrepreneurship, OECD Publishing, Paris.

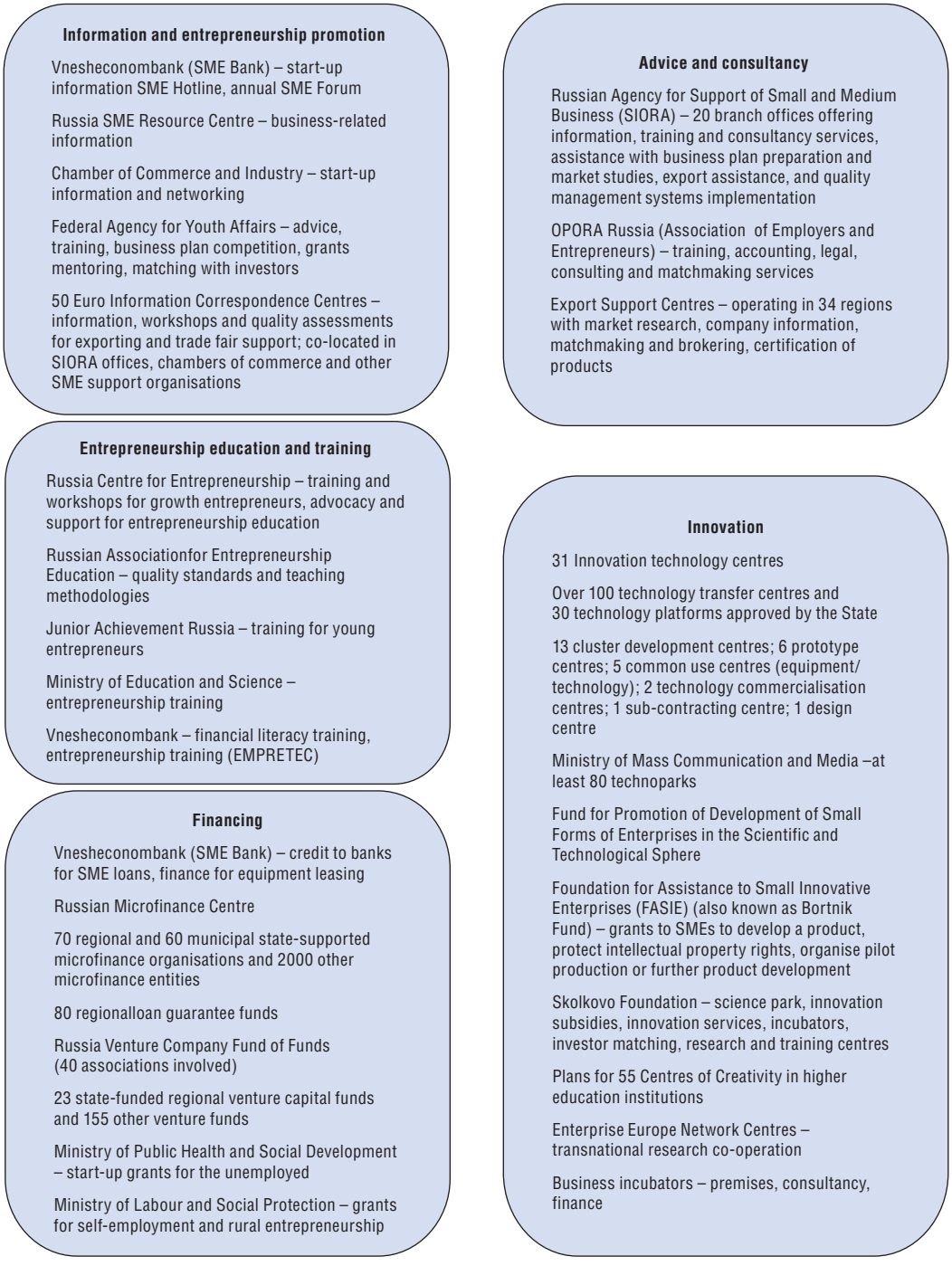
Strengthening the business development services infrastructure

Thin business development services system

Figure 5.1 identifies the key actors involved in business development services support and their facilities such as business incubators, centres for entrepreneurship support, technology and innovation centres, export support centres, technology parks, industrial parks, and Euro Info Correspondence Centres. Many receive funding contributions from the federal SME support programme. Others operate fully in the private or non-governmental organisation sectors or with funding from other ministries and agencies.

However, despite the large number of organisations listed, the number of business development services support centres is very limited when compared with the numbers of regions and SMEs and entrepreneurs needing support. For example, there are only 20 SIORA branches in the Russian Federation, only a quarter of the number that would be required to cover all 82 regions. Similarly, there were only 45 Euro Information Correspondence Centres in 2012 and only 9 682 SMEs obtained their support services. Export Support Centres existed in only 34 regions and had provided support to only 6 000 SMEs by 2013.

Figure 5.1. **Map of the business development services system in the Russian Federation**



Source: Information supplied by Ministry of Economic Development, Russian Federation

There is a similar story with respect to business incubators; the most common business development services organisation in the Russian Federation. In 2012, there were 104 state-supported business incubators, with a total area of 212 500 square metres. Out of this total, 16 were "innovation" incubators, 45 "office" incubators; 6 "production" incubators; and 37

"combined-use" incubators. Together they hosted 1 554 small enterprises (an average of about 15 enterprises per incubator), that employed 7 860 workers (an average of 5 jobs per enterprise), and generated combined annual turnover of approximately RUB 7.4 billion (USD 233 million) (an average of RUB 4.7 million per enterprise or approximately USD 150 000). Approximately 1 000 companies had passed through the incubation process since the implementation of the measure in 2005. While the incubators have the potential to play a significant role in fostering start-ups and sustainable SMEs, their numbers are small. The density of incubators in the Russian Federation, of only one incubator per 1.36 million persons is approximately one-fifth of the density in the United States, where there is about one incubator for every 280 000 persons (Ernst&Young, 2010).

The numbers of state-supported technology parks is also low. From 2007-11, only seven projects were funded: industrial parks in the Belgorod region, the Ivanovo region and the Republic of Tatarstan; technology parks in the Orenburg region, the Penza region and the Republic of Sakha (Yakutia), and an agro-industrial park in the Republic of Tatarstan. Most regions do not have such facilities. On the other hand, substantial state investment (approximately RUB 150 million from 2010-14) has gone into the development of an innovation hub at Skolkovo science park in the Moscow suburbs, with the participation of the Skolkovo Foundation, the Skolkovo Moscow School of Management and the Skolkovo Institute of Science and Technology. The aim is to stimulate innovative start-ups in key technology sectors in which the Russian Federation has scientific strengths, such as information technology, biomedical, nuclear, and aerospace technologies. Skolkovo hosts corporate R&D centres, business incubators and accelerators, an innovation centre, a new graduate research university and a Centre for Entrepreneurship and Innovation, which integrates education, research and practice in entrepreneurship and innovation with the research results of the Skolkovo Institute of Science and Technology's research centres. Innovation-oriented companies in the Skolkovo Park can also access innovation grants (up to RUB 5 million for initial marketing, patent and prototype development; up to RUB 30 million for early product development; up to RUB 150 million for mid-phase product development and up to RUB 300 million for later-stage projects), corporate, customs and social security tax breaks and services for mentoring and marketing, links to global private seed and venture funds, protecting intellectual property, importing goods, and networking to academic, legal and entrepreneurial resources. As of November 2012, 162 innovation grants had been made (totalling RUB 8.5 billion), involving 750 participants. However, while this is a promising initiative, and there are good arguments for supporting an innovation pole in the Moscow region, it is just one innovation pole, and there is a danger that it will become an enclave with limited spillovers to other regions.

Increasing the density of business development service centres

In recognition of the lack of scale and uneven regional coverage, the Ministry of Economic Development is making it a priority to increase the numbers of business development services organisations and the numbers of professional consultants working in the system by offering regional and municipal authorities co-funding of between 50% and 95% of the capital costs of establishing new facilities and of the operating costs of facilities during 10 years, which helps ensure a level of sustainability.

The limitation of the expansion strategy, however, is that each sub-national authority decides whether it wants to participate in co-financing the creation and development of each support infrastructure organisation, and only a small number of regional and

municipal authorities participate in the business support infrastructure component of the federal SME support programme: 14 in 2011 and 16 in 2012. Further efforts should therefore be made at federal level to secure a basic minimum provision of each type of relevant service in each region. The recent decision to allow private sector companies to participate in the co-financing of projects to create technology parks and incubators, with access to funding of up to RUR 200 million from the federal SME support programme, should help accelerate this process by enabling the federal government to provide funding for private initiatives for key services where regional and municipal authorities do not act. In addition, the Ministry of Economic Development should engage regional and municipal authorities in a mapping of their business development services structures to identify gaps in the presence of different types of SME and entrepreneurship support across the country, and review the incentives to sub-national governments to participate in the business support infrastructure component of the federal SME support programme.

A recent promising development is that since 2013, federal co-financing of up to RUB 5 million (USD 160 000) has been made available for the creation of Centres of Social Innovation. These Centres will promote social enterprises by providing training and certification for social entrepreneurs and managers of socially-oriented organisations, offering advisory services for business planning and development, helping to attract potential investors, providing consultancy support for the preparation of applications for state support for socially-oriented entrepreneurs and the creation of marketing strategies; and raising awareness of the development of social entrepreneurship in regional media. Examples of social enterprises that are targeted include those that provide vocational guidance and placement services, social services to citizens, health care, sale of prosthetic equipment, sports activities, children's programmes, cultural and education activities, helping victims of natural disasters and enterprises that employ at least one-half of their workers from among disabled persons, young mothers, ex-offenders, or other socially-disadvantaged groups and whose salaries comprise at least 25% of their wages.

Creating "first-stop shop" business support centres

A business support system should have accessible entry points that offer basic business development advice and information on government regulations and programmes direct to SMEs and entrepreneurs and refer them where appropriate to other more specialised government, non-profit and private sector services. For maximum impact, these entry points should be nationally branded and networked and controlled for quality standards. However, the Russian Federation currently has no national system or network of business information and advisory services for SMEs and entrepreneurs with a presence in all regions.

Around the world, governments have adopted different models for establishing networks of business support centres. One system that is working well is the Canada Business Network, as described in Box 5.4. It illustrates how the federal government can play a co-ordinating role in developing a regionally-located but national system of business support centres by developing the concept, building partnerships with regional authorities, providing common information technology and data platforms, defining common standards for service offerings, investing in training of centre staff, and co-operating with other service delivery partners that can reach out to more SMEs and entrepreneurs.

Box 5.4. **National Network of Business Centres, Canada**

The approach

A national network of "one-stop shop" business centres has been operating in Canada since the 1990s under the heading of Canada Business; so that entrepreneurs can easily locate the information and advice they need. The network consolidates all government business information and referral services into one Canada Business Centre (CBC) in each of the 13 Canadian provinces/territories. In addition, there are upwards of 500 Regional Access Partners (e.g. provincial and municipal governments, business associations, chambers of commerce, and community economic development organisations) which help direct entrepreneurs into the information and services available from the CBCs.

Clients can call in, access information through a toll-free 1-800 telephone line, or contact the centres through the Internet and email. Staff can offer information on government services, programmes and regulations and advice about starting or improving a business, or make referrals for more in-depth services to other support organisations including government departments and agencies, non-governmental organisations and private sector firms. Online services such as interactive business planners and entrepreneurship/small business workshop material are also available. Core services are offered free of charge, although some centres charge for supplementary services.

The network is managed by the Federal Ministry of Industry (Industry Canada) in co-operation with other federal ministries, provincial and territorial governments (which share the costs of the CBCs in their regions), and in some cases, the private sector, business associations and the academic and research communities. The Canada Business National Secretariat (housed in Industry Canada) is responsible for developing policies, standards and practices to promote a consistent national network operation, and maintaining the technical network, information databases, and products, as well as the national website. [5] In addition, regional development agencies are accountable for federal management of CBCs located within their jurisdictions. These two lead agencies co-ordinate their activities nationally through the Canada Business Managing Partner Committee, composed of senior officials from each organisation and from the Ministry of Industry. This Committee is instrumental in developing consensus on major operational decisions as well as in defining core services, new services and products, and national standards.

Results

The federal cost of maintaining the network of 13 Canada Business Centres averages about CDN 1.15 million per centre per year. The online Business Start-up Assistant is accessed by over 1 million visitors a year.

Success factors

The success of the network is based on partnership between federal and provincial/territorial governments (co-location, shared services, co-funding), outreach to other regional SME support organisations (i.e. Regional Access Partners), training and on-going professional development of Centre staff, innovations in the use of information technology platforms to amass a variety of business-related government databases and disseminate information and services, and responsiveness to the needs of entrepreneurs and SMEs as identified in client usage and satisfaction surveys.

Problems and responses

One of the initial challenges for federal government was to convince some of the provincial governments to partner with them on the initiative, especially in cost-sharing arrangements. In cases of reticence, the federal government moved ahead anyway and eventually, all provincial and territorial governments realised the benefits of co-operation.

Since there is considerable regional variation in the funding and service priorities of CBCs, the network faces a continual challenge to maintain a cohesive and consistent level of service. Considerable investment is therefore made to facilitate communications through a variety of committees and communities of practice. This contributes to a shared vision and sense of purpose and allows the network to share good practices.

Box 5.4. **National Network of Business Centres, Canada** *(cont.)*

Another challenge has been to offer accessible services in rural areas. This has been facilitated through the extensive use of information and communications technologies. In addition, in the Province of Manitoba, the CBC invested in a Mobile Business Service Centre in the form of a 30-foot trailer that travels to rural parts of the province.

Initially created before the emergence of the Internet as a dominant service delivery channel, the network has strived to transform its business model to one that produces information and services that can be easily and conveniently consumed on the Internet. Of approximately 7.3 million clients in 2005-2006, 7 million accessed services offered through the Internet. One of the Internet-based services is BizPal, a web-based platform for identifying all of the permits and licenses required when starting or operating businesses of different types.[6] Social media tools (e.g. Really Simple Syndication feeds, blogs and Twitter) are also used to raise awareness of services.

The majority of clients are potential and new entrepreneurs. However, over time, the CBCs have attempted to improve their appeal to existing SMEs by marketing value-added services such as seminars and mentorship/advisor programmes. Development of new products and services and improvements in service standards are based on client satisfaction studies and research. A Client Tracking System has been developed to systematically collect data on clients to help better target messages and improve services.

Relevance to the Russian Federation

A partnership between federal and regional governments in the Russian Federation could create a national network of business centres that would fill the gap for a unified and co-ordinated point of entry for information and services to SMEs and entrepreneurs and provide a hub for networking and good practice exchange among existing business support organisations.

Further information

Canada Business Network Operations, Service Delivery and Partnerships, Small Business and Tourism Branch, Industry Canada, Ottawa. Website: *http://canadabusiness.ca*

Source: Information supplied by Canada Business.

There are various options for developing a first-stop shop network in the Russian Federation. For example, the centres of the Russian Agency for Support of Small and Medium Business (SIORA) or the European Information Correspondence Centres could be expanded and brought together in a network and gaps in certain locations filled using financing from the federal SME support programme.

Increasing quality in the system

Quality also needs to be upgraded in the business development services system by upgrading the skills and competences of managers of business development services centres and their consultants and by introducing stronger quality and performance standards. In many cases, business support infrastructure organisations are either not well staffed or staffed with unqualified people. Arrangements should therefore be put in place for recruitment to increase the numbers of business development advisors and consultants, and for development of professional standards and provision of training and continuing professional development activities for new and existing staff.

There are many examples of countries that have established quality standards for SME advisors and consultants. These can include national vocational qualifications for business advisors and professional development programmes leading to certification as a small business advisor. For example, the United Kingdom government has in the past required all SME business advisors and consultants working on government-supported programmes to be accredited (see Box 5.5).

Box 5.5. **National Professional Development for Business Advisors, United Kingdom**

The approach

In the early 2000s, the accreditation of small business advisers and counsellors who were providing services to SME clients through government SME support centres and government funded organisations was a priority of the Department of Trade and Industry (DTI). The aim was to better ensure the quality and consistency of advisory services to SMEs by building a network of accredited advisors and counsellors. At that time, the United Kingdom was the most advanced in the world in the area of setting standards for small business advisers and counsellors. National Vocational Qualifications (NVQs)[7] had existed for small business counselling since 1994. In 1993 the sector skills body (now the Small Firms Enterprise Development Initiative)[8] with the Institute of Business Advisers (IBA)[9] and others established six standards in NVQs for Business Counselling with a guide on how to attain the NVQ through professional practice and upgrading. A Joint Awarding Bodies was formed with the Royal Society of Arts (RSA) for NVQs in Business Counselling. In 1994, the IBA joined the National Federation of Enterprise Agencies and Durham University Business School to accredit and promote Training Courses in Small Business Support. A number of UK universities now offer related training programmes and a comprehensive list of accredited courses is published each year.

In 2000, the DTI adopted a set of seven common core Standards of Professional Competence for all those delivering services on behalf of the Small Business Service (the small business policy and support entity in the UK government at the time) and worked with the IBA to monitor these standards through an Accreditation Advisory Board.

The Department of Business, Innovation and Skills (which has replaced DTI) continues to promote the demand of small firms for business advisory services. In 2014, it introduced the roll-out of the Growth Vouchers Programme, a new GBP 30 million scheme that offers matched-contribution subsidies of up to GBP 2 000 to make it easier for small businesses that do not normally use these services to access expert advice and guidance. Areas of advice available through the Growth Vouchers Programme are: raising finance and managing cash flow; recruiting and developing staff; improving leadership and management skills; marketing, attracting and keeping customers; and making the most of digital technologies. The programme is complemented with access to an online "Marketplace" of Advice Suppliers (accredited members of relevant professional bodies) from which small firms can secure services once their specific needs are identified through completion of an online diagnostic questionnaire, followed by a face-to-face, skype or telephone assessment session with a delivery partner business advisor.

Further information

Information on business support standards is available from *www.sfedi.co.uk*. Information is available from the UK Institute of Consulting on their competency, training and professional development programmes: *http://www.iconsulting.org.uk/training_and_qualifications/qualification_and_training_course_information/consultancy_qualification_framework*

Source: Stevenson and Lundstrom (2001), Department of Trade and Industry (2000) and Department for Business Innovation and Skills.

Upgrading business consultancy has also been a priority of the Asia-Pacific Economic Co-operation (APEC) member countries, which developed the APEC Training and Certification for Small Business Counsellors programme in the late 1990s. It then launched the APEC International Network of Institutes for Small Business Counsellors (APEC-IBIZ) in 2002. More than 16 APEC economies are participating in the APEC-IBIZ project, including Australia, Canada and the United States and a fledgling initiative in Mexico. As part of the initiative, Economy Institutes in each country oversee the training and certification of small business advisers to an APEC-wide recognised standard. Ten self-directed core learning modules leading to the APEC designation are delivered in workshop or online formats covering Code of Ethics, Counselling and Interpersonal Skills, Problem Solving, Client Assessment, Business Planning, Marketing, Financial Analysis, Human Resources, Government and E-commerce. The cooperative and interactive training develops business acumen, counselling, coaching, and facilitation skills to enhance the effectiveness of professionals in the field of small business development. The final certification requires the completion of three programme components within a three-year period. To qualify for certification, professionals must demonstrate their mastery of the 105 internationally-recognised competences by documenting their prior experience in a professional portfolio and being judged on a counselling intervention. The completed portfolio is reviewed by a certified APEC assessor who evaluates the ability of the counsellor to apply the required competencies in various counselling settings. A successful portfolio assessment is the final step in receiving designation as an APEC Certified Business Counsellor. With the APEC-IBIZ certification, consultants are qualified to work domestically as well as in all other APEC economies.[10] The Russian Federation is a nascent participating country in the APEC-IBIZ programme, but the scope of its impact has been limited to date. One option to strengthen the skills, competencies and service standards of business consultants and advisors is therefore for the Russian to more fully develop this programme.

Another method available to upgrade quality is to create networks for mutual learning that can convey information on best practice experiences across similar organisations. This type of best practice exchange is limited in the Russian Federation because the connections between support organisations and interventions are not well enough developed. On the other hand, there are some models to build on. For example, in 2012, the Russia Centre for Entrepreneurship signed Partnership Agreements with leaders of Russian regional entrepreneurship development organisations to create the Alliance for Entrepreneurship Development, which focuses on supporting entrepreneurship education, including conducting training in entrepreneurship education methodologies for university teachers.[11] Members include the Institute of Public Administration and Entrepreneurship at the Ural Federal University, the Regional Information Consulting Centre and the Association of Exporters and Importers of Kuban, the Agency for Development of Qualifications in Kaliningrad, and Startup Women. Other such networks could be promoted for other types of business development services organisation.

Weak networks between the organisations also increase the probability of overlaps or gaps in service provision and inconsistency in the ways that similar organisations operate in the delivery of support to SMEs and entrepreneurs. Currently, there is no national co-ordination of any of the SME and entrepreneurship support delivery systems. Neither is there evidence that the Ministry of Economic Development is taking actions to promote linkages between the various supported "infrastructure" organisations, for example for cross-referral. Networking for the integration of services and for mutual learning is

an important aspect of the management of business development services in other countries, together with the monitoring of performance standards across publicly-funded organisations. In addition to the case of the Canadian business services network described in Box 5.4, another example of a highly-networked business development services system, which also provides accessible first-stop shop services, is the National SME Services Network supported by the Polish Agency for Enterprise Development in collaboration with Polish regional governments (Box 5.6).

Box 5.6. **The National SME Services Network, Poland**

The approach

The Polish Agency for Enterprise Development (PARP) is responsible for running the National SME Services Network (KSU), established in 1996 as the national umbrella for business support centres across Poland. The network gathers over 200 member organisations providing state-co-financed business development services to SMEs and entrepreneurs. The members include non-governmental organisations, regional development agencies, employers' organisations, credit guarantee funds, loan funds, business schools, crafts associations, technology centres, incubators, foundations, chambers of commerce and industry and small consulting firms.

There are about 40 *consultation points*, which help entrepreneurs in developing their businesses at every stage of the business cycle: from starting a company, through business management, to suspension or closing of the business. In addition, over 18 *innovation centres* offer innovation audits, diagnoses of innovation potential and facilitation of innovation processes in companies. Entrepreneurs can access *KSU specialised advisory services* in areas such as environment protection law, quick optimisation in business financial management, marketing and sales in the agro and food industry, energy efficiency management, and advisory services in planning and financing business undertakings. Financing and financial advice are offered by the *loan and loan guarantee organisations* within the KSU network. The costs of all these services are partially covered by PARP.

PARP also provides a range of operational, technical and capacity-building support to the network organisations. The support includes information exchange systems to enable the business support centres to refer clients to the appropriate expertise in the network; co-ordination of promotional activities for the network (meetings, conferences, etc.); providing common information on the services of the network and training for KSU consultants to ensure adequate quality of the services.

Results

The KSU network has succeeded in upgrading the quality and uniformity of standards of publicly-supported business support services in Poland and stimulating SMEs to benefit from business support services available for strategic planning and business growth.

Success factors

One of the key factors behind the success of the network in upgrading the quality of business support organisations is the method of accreditation of institutions providing services to enterprises. All members must be evaluated to have the technical and financial capacity to adequately provide advisory, training, information or financial services to start-ups, microenterprises, and SMEs; ensure that services are provided by staff and consultants with the appropriate skills; have a quality assurance system for their services; and act in accordance with professional ethics standards. Consultants providing business development advice also need to be accredited individually by PARP. One of the main criteria is that they have adequate skills and experience in a given area of specialisation related to the assistance funds provided by the business support organisation on behalf of PARP. Over 1 400 consultants have been accredited to work in the system.

Box 5.6. **The National SME Services Network, Poland** *(cont.)*

Another success factor has been the attention paid to developing and improving the services and delivery approach over time. To support this, PARP undertakes on-going research, monitoring and analysis of economic trends to ensure that services remain relevant in changing business conditions. It also tests and introduces new services (through so called *pilot services*) that are tailored to SME's needs and established according to defined and monitored standards. Furthermore, PARP monitors the activities of the business support organisations, including collecting data on the number of clients, the percentage of start-ups versus established SMEs supported, and the content of the services provided. This information helps in identifying imbalances in the allocation of services and identifying necessary adjustments. Client satisfaction surveys are also undertaken to assess the quality of services provided by the business support centres as well as research on the demand for and supply of business support services. This provides important insights on how to customise services to better meet the needs. The planning and development of services is supported by a *coordination council* with representation from different types of service providers (including the consultation points, innovation centres, and finance providers). The council meets regularly and helps to generate synergies in the system and increase relevance to needs.

Relevance to the Russian Federation

The KSU network that is organised by PARP illustrates a potential approach to upgrading business support services across the Russian Federation using systems of accreditation, monitoring, co-ordination and capacity building undertaken at the central level.

Further information

See: *http://en.parp.gov.pl/ (in English) and http://ksu.parp.gov.pl/* (in Polish).

Source: OECD (2010), *Poland Key Issues and Policies*, OECD Studies on SMEs and Entrepreneurship, OECD Publishing, Paris, and information supplied by the Polish Agency for Enterprise Development.

The Polish system emphasises quality monitoring across the system. This does exist in the Russian Federation for the federally-funded business development services infrastructure, but it is still at a formative stage. For example, federal funding guidelines include an extensive description of the services to be provided by supported organisations, the qualifications of persons to be hired, the composition of governance structures (e.g. requiring representation from SME associations), and the types of costs that can be covered within the scope of state support. For example, in the case of business incubators, technology parks and industrial parks, the physical size of the facility (minimum square metres required) and percentage of spaces to be dedicated to SMEs are specified. The Ministry also requires infrastructure organisations to obtain the relevant quality certifications (e.g. ISO9001) within a year of being funded by the programme and requires annual performance reviews of supported infrastructure. On this basis, the activities of business development services organisations are subject to a number of controls. However, more emphasis is needed on assessing the quality and impacts of services provided and on focusing resources on the best performing organisations.

A related issue concerns the need for continuity of funding. Both the Ministry of Economic Development and sub-national government authorities use competitive processes for providing core and programme funding to SME support service providers. This may be a way of reducing patronage and capture by poorly performing incumbents, but it may also create an unstable system of support delivery. For example, an SME

Resource Centre may be successful in obtaining core funding, but not successful in a competitive process in securing additional programme funding for special activities or events. Similarly, an organisation funded in early rounds of support may not be funded in subsequent rounds forcing closure or cutback in the quality and extent of services. Attention must therefore be paid to offering continuity and coherence in the funding of business support organisations and their activities as well as to ensuring some competition for funds.

Upgrading the service offer of business incubators

Some of the existing business incubators in the Russian Federation are in line with international good practice (see Box 5.7 as one illustration). However, many concentrate simply on providing physical space for incubating enterprises, often with subsidised rents and access to state loans and loan guarantees. Few directly offer the range of other services commonly seen in incubators in developed countries, such as entrepreneurship training, help with business plan development, advice on marketing, links with external mentors, or channels to business angels and venture capitalists (Ernst&Young, 2010). Furthermore, many incubators are located in reconstructed buildings that were not designed for this purpose and do not have open plans and shared common areas that encourage networking among tenants.

Box 5.7. **The Moscow State University business incubator**

Moscow State University has a special incubator programme with several complementary elements that have been developed to encourage start-ups by students. These include: i) awareness and information; ii) a three-month education programme in high-technology entrepreneurship provided by multidisciplinary teams; iii) business plan competitions, with the support of FASIE; and, iv) a START programme with two years of support (OECD, 2011, p. 233). This incubator programme is being replicated in Zelenograd and at the Moscow State Baumann Technical University.

Source: Information supplied by Moscow State University

In following a common international classification (InfoDev, 2010a), most of the existing incubators would fall into the category of "first-generation" incubator models – consisting of real estate, shared facilities and reactive support to tenants. A few may be "second-generation" incubators; ones that provide pro-active business advisory support services. Not many at all could be considered "third-generation" incubators, a model which is characterised as offering a wide range of business support services (including pre-incubation services to support potential entrepreneurs define their business ideas and develop their plans to a point where they can be evaluated as a potential investment), access to sources of financing, mentoring/coaching, technology labs, techno-entrepreneur development programmes, etc. The emergent fourth-generation incubator models are more commonly referred to as "business accelerators" and focus on fast-tracking start-ups by entrepreneurs with high-potential business ideas and rapid growth ambitions. There appear to be no accelerators following this model in the Russian Federation system. There is therefore a need to upgrade the majority of

existing business incubators towards more comprehensive and pro-active business development support services.

Creating a national business incubator co-ordination unit

Attention should also be paid to increasing standards within the business incubator system, reflecting both the relatively large numbers of incubators compared with other business support facilities and weaknesses in the capacities of some of them. A significant step forward has been taken with changes in 2013 to the legislation governing the implementation of the federal SME support fund, which categorised incubators into standard incubators and innovative incubators and specified their different functions. The functions of standard incubators include: increasing the volume of start-up and business activity, training, occupational retraining, consulting, and outreach services. The functions of innovative business incubators include: the search for potential entrepreneurs with innovative ideas, pre-incubation processes (project attractiveness assessment), and incubation processes (marketing, finance, investment project development, attracting investment, prototype creation, and industrial engineering). Staff of an innovative incubator (director and team members) must be specially trained in incubating small innovative enterprises.

Incubators have also been required to conduct annual performance appraisals, including providing evidence of compliance with established requirements, organisational effectiveness, quality of management and staff efficiency, and the quality of the system for monitoring the activity of SMEs that use their services. Criteria used for the annual assessment of innovative incubators include: the number of utility models and/or industrial designs put into practice; the number of patented utility models and/or industrial designs; the number of projects brought to the international market; the number of projects receiving investment; and the volume of attracted investments.

To upgrade the system further, consideration should be given to setting up a national co-ordination unit for business incubators. The unit would be responsible for developing a more thorough manual of standard operating guidelines, services and performance standards that are to be applied across the incubator system; facilitating network exchanges between incubator managers to promote the transfer of learning; and introducing professional development programmes to upgrade the skills and capacities of incubator managers, staff and consultants. In addition, the unit would assume national responsibility for co-ordinating annual assessments of the performance of each incubator on the quality of its operation, capabilities, management, financial performance and planning, and impact (e.g. portfolio quality, number of successful exits, capital raised for clients, average export revenues of graduate companies, new initiatives, influence in their local community). The results would be used to ensure that the best performing incubators remain well supported and that low performing incubators take remedial action.

The experience of the business incubation system in Brazil may offer useful insight on expanding the number and standards of incubators in the Russian Federation (see Box 5.8).

Box 5.8. **Building a business incubator infrastructure, Brazil**

The approach

There were 384 business incubators in operation in Brazil in 2011, up from 135 in 2000, representing one incubator per 495 000 inhabitants (as compared with one incubator per 1 360 000 inhabitants in the Russian Federation). Some 40% were technology-based; 18% were for traditional enterprises; 18% were mixed (for technology-based and traditional enterprises), 7% were for agri-industrial enterprises; 8% were for services enterprises; and 9% were social. The average incubator had five staff. Many are situated on or close to university campuses and are often managed by a university employee.

The services include physical space and hard infrastructure, but softer services are emphasised even more, such as counselling, advice, financial and legal consulting, networking, and access to financing. Pre-incubation support is also offered to help entrepreneurs to develop a viable business project, for example for consulting, technical and economic feasibility studies, R&D and development of a marketing strategy.

The selection process for supported companies varies with each incubator, but the most important criterion is innovation. Accepted enterprises can be incubated in a space inside the incubator or incubated as a non-resident. The average incubation period is three years, but varies with the characteristics of the enterprise. For example, Information and Communications Technology enterprises tend to need less time than biotechnology ventures. The critical consideration is that the incubating project should be prepared for the market on graduation from the incubator programme. Enterprises can continue to receive advisory and follow-on support for up to one year after leaving the incubator.

The development of a relatively dense incubator system has been enabled by federal government funding from the national Programme for Support of Technological Parks and Incubators. The programme is implemented by the Brazilian Innovation Agency in collaboration with a wide coalition of government partners and managed by a steering committee that monitors its implementation and strategy. It offers competitive incubator grants worth up to 80% of the project cost to public administrations, universities and non-profit bodies responding to calls for proposals, which should have a value ranging from BRL 4 million (EUR 1.8 million) to BRL 8 million (EUR 3.6 million).

In addition, co-ordination and support is provided by a national business incubator association, ANPROTEC, which has approximately 280 members, including business incubators, technology parks, research and education institutions and government agencies. ANPROTEC encourages various entities to support incubators, offers training courses, organises meetings that facilitate knowledge exchange, encourages the creation of regional networks of incubators, gains university support and helps voice incubator concerns to policymakers.

Results

In 2011, the incubators were home to 2 640 enterprises (an average of about 7 enterprises per incubator) generating 16 394 jobs (an average of 6.2 jobs per enterprise) and had graduated 2 509 enterprises employing 29 205 workers.

Success factors

Several factors are associated with the success of the Brazilian incubator system:

- *Government support*. Incubators have been funded by the government's national incubator programme and a multitude of other federal, state and local government organisations.
- *Private sector involvement*. Private sector business associations are often active partners in the consortiums establishing incubators. In some cases business associations assist incubators by offering mentoring and in-kind support to incubated enterprises. In other cases large corporations invest in incubators.

Box 5.8. **Building a business incubator infrastructure, Brazil** *(cont.)*

- *University involvement*. Universities have played a pivotal role. They typically support incubators by providing buildings, staff and the use of laboratories. The technical universities and technological research institutes also constitute the knowledge base for many incubators, supply technical skills and innovations and offer access to professional innovation networks.
- *Networking*. National and regional incubator networks play a significant role in information sharing, mutual learning and resource sharing as well as in influencing government policy directed at the growth of business incubators.
- *Innovative models*. The business incubation landscape in Brazil is now varied and complex with a plethora of incubation models, some of which have evolved in response to specific local needs. For example, the social model of incubation has developed in response to the need for job creation in poor areas.

Problems and responses

A challenge has been a lack of visibility of business incubator services to potential entrepreneurs and newly-established enterprises. Efforts are therefore being made to provide more information and to increase the co-ordination of the range of SME and entrepreneurship support services available at national and local levels.

An additional issue was the lack of a national monitoring and evaluation system to assess the performance of incubators and identify areas for improvement. A Tracking System for Business Incubators and Technological Parks (SAPI) has therefore been developed (*www.portalinovacao.mct.gov.br/sapi/*), which includes indicators on the performance of graduated companies, taxes generated, the empowerment and dedication of incubator teams, the financial sustainability of incubators and the volume and quality of services provided.

It has also been necessary to reinforce the training and professional development of incubator managers and staff. This includes creation by ANPROTEC and SEBRAE (the Brazilian Micro and Small Business Support Service) of a **Reference Centre for Support of New Ventures (CERNE)** offering training workshops for incubator managers and consultants on generating innovative companies, managing and organising an incubator, and building and managing social networks.

Relevance to the Russian Federation

A national incubator programme and incubator association could help expand, upgrade and co-ordinate the more than 100 business incubators operating throughout the Russian Federation, including arrangements for competitive funding, performance monitoring and enhancing the skills and competences of incubator managers and consultants.

Further information

Department of Technological Development and Innovation), Ministry of Science, Technology and Innovation, Brasilia (*www.mct.gov.br; parques.incubadoras@mct.gov.br*) and National Association of Incubators and Science Parks (ANPROTEC), Brasília (*http://anprotec.org.br/*).

Source: InfoDev (2010b), *Global Good Practice in Incubation Policy Development and Implementation: Brazilian Incubation Country Case Study*, Washington, DC: World Bank; ANPROTEC and Ministry of Science, Technology and Innovation (2012) Study, Analysis and Propositions on Business Incubators in Brazil, ANPROTEC, Brasilia.

Conclusions and recommendations

A wide set of federal programme interventions are in place for SMEs and entrepreneurship in the Russian Federation. Major initiatives include support for building a culture of entrepreneurship, grants for start-ups, promotion of youth entrepreneurship, encouraging SME innovation, investing in new plant and equipment, promoting exports, improving access to finance through micro-loans and loan guarantees and supporting tailored municipal

economic development strategies and strategies for the diversification of mono-industry cities. However, certain modifications could be made to existing programmes to increase their impact. For example, the system of start-up grants would benefit from simplified access, increased coaching and mentoring support offered in parallel to grants, and increased co-ordination between different start-up programmes. Similarly, the range of SMEs that benefit from innovation support could be widened to cover more non high technology firms and the numbers of young people targeted by entrepreneurship support could be increased. In addition, subsidy payments could be stopped for expenditures already made by SMEs, since there is a risk that a high proportion of these state expenditures would be non-additional and represent windfalls for the recipient firms.

One of the strengths of federal programmes has been their flexibility to adapt to emerging priorities and opportunities. During the last five years, for example, positive developments include the introduction of new programmes for social enterprises, Innovation Creativity Centres for young people, SME energy efficiency actions and support for outsourcing by SOEs to new enterprises. However, achieving the objective of SMEs generating 50% of the country's GDP by 2020 will require a much accelerated approach to developing the SME sector, both to increase the rate of new business start-ups and to stimulate the growth, productivity, and competitiveness of existing SMEs. One of the important steps that can be taken is to fill gaps in the current system of programme support to SMEs and entrepreneurs corresponding to particular areas of opportunity in the Russian Federation. Key areas where new national programmes could make an important difference are a national campaign for promotion of entrepreneurship, access of aspiring entrepreneurs to standardised and proven entrepreneurship training workshops, a programme to support the development of high-growth enterprises and a programme to strengthen the absorptive capacity of SMEs in order to enable greater access to FDI supplier markets and technologies.

Another central challenge is to shift away from the current largely hands-off subsidy-based system (e.g. subsidies for export activity, enterprise creation, innovation-related activity, and equipment leasing and purchasing) towards a system providing diagnosis of business development challenges backed up by an offer of training, advisory and consultancy services, incubation, and innovation support for promising SMEs and entrepreneurs as well as some more targeted financing support to the firms most likely to expand and undertake additional innovative projects. This will require further strengthening of the business development services infrastructure that is now starting to emerge with policy support. Despite recent growth, the business support infrastructure remains relatively thin, showing up in a low density of business incubators and technology parks and gaps in the availability of other key services in certain regions (SME resource centres, entrepreneurship support centres, export support centres, innovation-related centres etc.). A business support infrastructure mapping exercise at national and sub-national levels would help to identify the gaps to fill. A national system of first-stop shop business support centres should also be considered to serve as entry points for SMEs and entrepreneurs to access public information, advice, and referral services. Such first-stop shops are usually most effective when they are nationally branded, which provides for high visibility to SMEs and entrepreneurs and for controls for minimum quality standards.

In parallel, the quality of service needs to be upgraded in terms of the scope of support offered, the operating standards of business support organisations and the professional competencies of their management and staff. As a major co-financer of the business support infrastructure, the Ministry of Economic Development should be

playing a stronger leadership, co-ordination, and capacity building role to ensure that funded support organisations are delivering quality services and that the priority business support needs of different groups of entrepreneurs and SMEs are being met. This could be promoted by increasing the application of performance monitoring of state-funded business development services centres aimed at increasing the quality and consistency of service provision. The Ministry of Economic Development could also play an important role by creating networks for regular exchanges and sharing of experience and providing professional development and training opportunities to enhance the knowledge and skills of business support staff. The density, scope of services and performance standards of business incubators should be a particular target for upgrading.

The following recommendations are offered to improve federal SME and entrepreneurship support programmes in the Russian Federation:

Key policy recommendations for federal SME and entrepreneurship programmes

- Adjust the business start-up grant programmes for the unemployed by targeting financial awards towards sustainable business proposals, simplifying administration for accessing the programmes, offering additional business diagnosis and advice services to greater proportions of entrepreneurs supported with grants and improving co-ordination and synergies between different start-up programmes.
- Broaden SME innovation support to include non-technological companies and non-technological innovation projects, tie a proportion of the subsidy awards to a diagnosis of the enterprise development needs of potential innovator SMEs, and combine financial awards with advice, coaching, consultancy and workforce training to help deliver agreed company action plans. Consider the introduction of highly targeted tax incentives for investment in innovation in innovative SMEs.
- Build the pipeline of future entrepreneurs by launching a national entrepreneurship promotion campaign to give positive images of entrepreneurship through the media and other channels.
- Introduce a standard, subsidised basic national entrepreneurship training course for adults and youth with the intention to start a business, which could be a virtual training course delivered through the internet or could be provided through physical workshops.
- Introduce a high-growth entrepreneurship programme to identify high-potential SMEs and entrepreneurs, diagnose their business and personal development needs, and offer them tailored packages of coaching, mentoring, consultancy, technology development, management training, network building and access to seed and venture capital.
- Introduce a supplier development programme to build linkages between SMEs and inward FDI operations. The programme should identify potential FDI anchor firms and SME suppliers, diagnose how the SMEs could reduce their costs, increase their quality and reduce their delivery times in order to gain contracts with the anchor firms, and offer the necessary training, consultancy and financing support to the SMEs in order to meet their supply standards. The FDI anchor companies themselves could be engaged in providing expertise and funding to the initiative.
- Expand the numbers and quality of business development services centres (incubators, entrepreneurship centres, export support centres, etc.). This should include assessing gaps in the presence of different types support across the country to inform public investment decisions. Incentives and opportunities should also be provided for public, private and non-profit organisations to create and run facilities, with part of the public funding based on results achieved. In addition, training and certification should be provided for business development service centre managers, staff and consultants, networks created for peer learning and cross-referrals of clients and more stable core funding supplied.

Key policy recommendations for federal SME and entrepreneurship programmes *(cont.)*

- Create a national system of first-stop shop business information and advisory centres based on an integrated national platform and brand. The first-stop shop would provide basic information and advice on business start-up and development directly to entrepreneurs and make referrals to other public, private and non-profit business service providers for more detailed information and advice.
- Upgrade the business incubator network by introducing more soft services (advice, mentoring, consultancy etc.) for enterprises at incubation and pre-incubation stages, creating a national incubator co-ordination and management unit responsible for preparing standard operating guidelines and performance monitoring of incubators, promoting mutual learning networks for incubator managers, and introducing professional development programmes for incubator managers and staff, with a particular emphasis on creating an adequate supply of qualified consultants for business diagnosis and advice through recruitment and training.

Notes

1. Under WTO rules, public funding support for the provision of professional advice and training and for participation in trade fair activities are allowable
2. *http://www.ilo.org/empent/areas/start-and-improve-your-business/lang--en/index.htm*
3. *https://www.score.org/getstarted*
4. SCORE is a programme of the US Small Business Administration (SBA) that makes use of retired executives and business leaders who are trained to serve as counsellors, advisors and mentors to aspiring entrepreneurs and business owners. These services are offered at no fee, as a community service. There are more than 11 000 SCORE advisors across the United States
5. *www.canadabusiness.ca/eng/*
6. *www.bizpal.ca/*
7. An NVQ is a statement of competence in the ability to perform to national standards in a real working environment.
8. See: *http://www.sfedi.co.uk/standards-setting-body/standards/introduction-to-business-support-standards*
9. The Institute of Business Advisors (IBA) was formed in 1989 as a professional membership and accreditation organisation (renamed the Institute of Consulting [IC] after a merger with the Chartered Management Institute in 2007) to enhance the competencies of business advisers. Benefits of membership in the IC include a Code of Conduct, Professional Indemnity Insurance, continuing professional development, networking, professional magazines and designation letters.
10. See: *http://www.apec-ibiz.org*
11. See: *www.cfe.ru/alliance/*

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OECD Studies on SME and Entrepreneurship
Russian Federation

Chapter 6

Access to finance for SMEs and entrepreneurship in the russian federation

Although recent state interventions have significantly increased the supply of external financing to SMEs and entrepreneurs, further increases in the scale and sophistication of financial markets for SMEs and entrepreneurship will be critical for the growth of SMEs and entrepreneurship in the Russian Federation. This chapter examines the nature of the SME and entrepreneurship finance gap and how policy is seeking to address it in the Russian Federation, covering bank loans, microfinance, and equity finance. It makes a number of recommendations for further improvements, including strengthening the operational arrangements of credit guarantee funds, expanding credit history information and credit bureaus, and increasing the remit of the public Vnesheconombank and SME Bank to cover new financial products and roles such as education in SME financing for investor institutions.

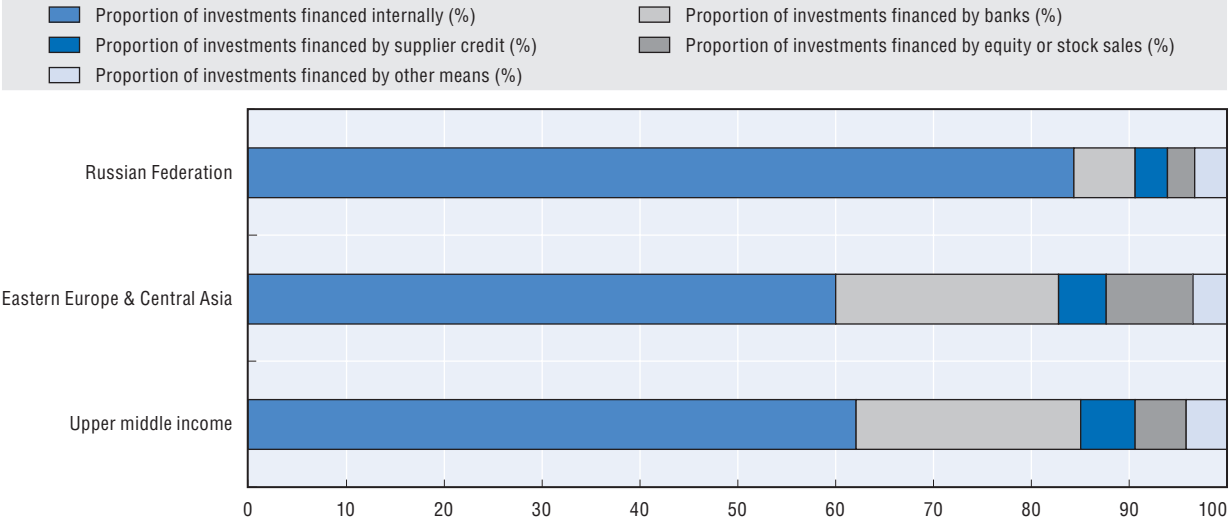
The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Over-reliance of SMEs on internal funding

Although SMEs and entrepreneurs can draw on their own resources for investment and working capital, such as reinvested profits, the personal savings or credit card borrowing of owners, or borrowing from friends and family, a strong reliance on internal funding tends to be associated with relatively low growth in the SME economy (OECD, 2006). Internal finance is not enough to enable all SMEs to access the finance they need for start-up and growth and to respond, when required, to fluctuations in their liquidity. Furthermore, in general internal funding tends to come at a high price. It is therefore concerning that SMEs in the Russian Federation depend disproportionately on internal sources of finance compared with firms elsewhere in ECA and Upper Middle Income countries.

As shown in Figure 6.1, according to the IFC/World Bank Enterprise Survey, internal sources of finance accounted for 84% of the investments of firms surveyed in the Russian Federation in 2012, compared with only 60% elsewhere in ECA and 62% in Upper Middle Income countries as a whole. By contrast, bank financing, trade credit and other forms of external financing were used infrequently. External financing also represented a relatively small share of the total working capital of surveyed enterprises in the Russian Federation compared with ECA and Upper Middle Income countries as a whole (Figure 6.2).

Figure 6.1. **Sources of financing for investment by enterprises**

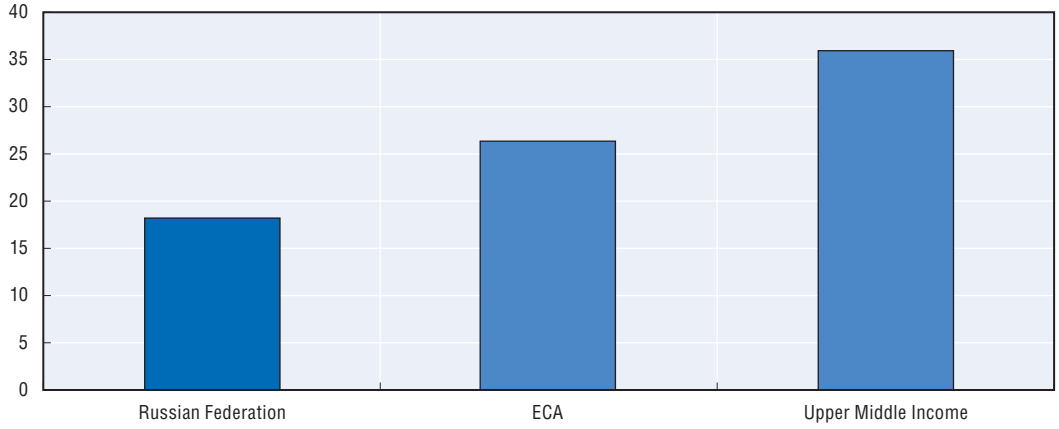


Source: World Bank/IFC (2012) Enterprise Surveys: Russian Federation Country Profile 2012. Washington DC World Bank Group.

StatLink http://dx.doi.org/10.1787/888933272002

This chapter examines issues affecting the availability of external funding for SMEs and entrepreneurs in the Russian Federation in the areas of bank lending, microfinance and equity, including the actions being taken by government and the public development bank to improve the situation. It proposes relevant interventions in finance supply, finance demand and intermediation.

Figure 6.2. **External financing as a percentage of working capital**



Source: World Bank/IFC (2012) Enterprise Surveys: Russian Federation Country Profile 2012. Washington DC World Bank Group.

StatLink http://dx.doi.org/10.1787/888933272014

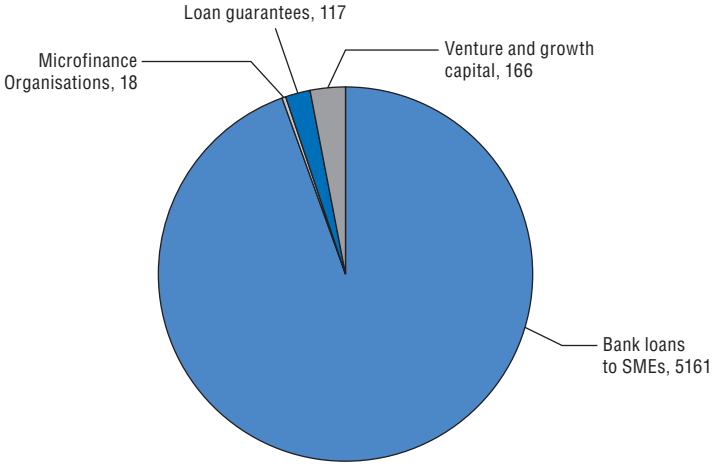
Bank lending for SMEs and entrepreneurs

Limited SME access to bank lending

Bank loans are by far the most important source of external financing for SMEs in the Russian Federation (Figure 6.3), as is the case in most other countries. However, there are a number of problems affecting the access of SMEs and entrepreneurs to access bank loans, which helps explain their relatively large dependence on internal finance sources.

Figure 6.3. **Key sources of external capital for SMEs in the Russian Federation, 2013**

Figures in billion RUB



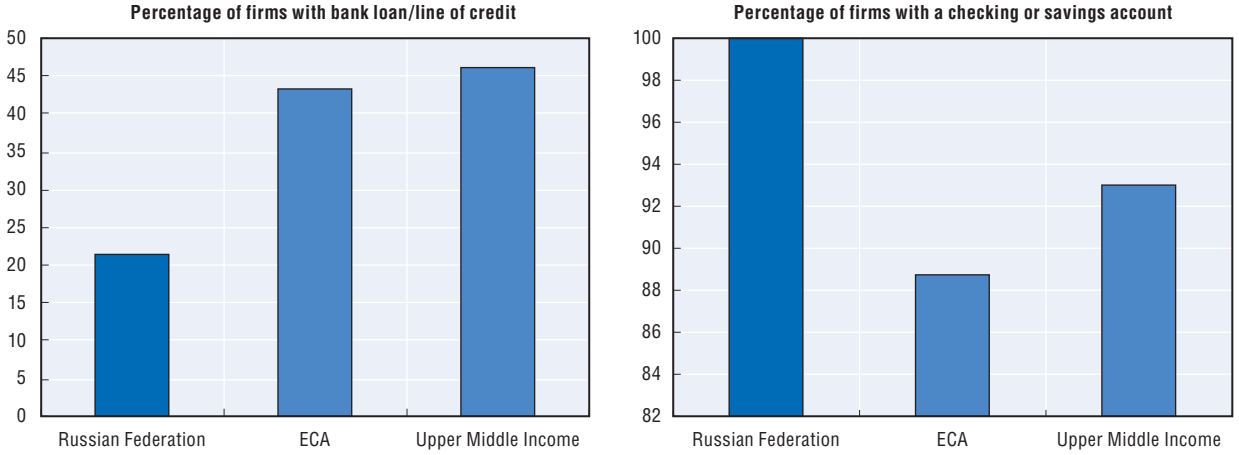
Source: Based on data from OECD (2015a) *Financing SMEs and Entrepreneurs 2015: An OECD Scoreboard*, OECD Publishing, Paris; Russian Microfinance Centre (2013) *Measures to Promote Microfinance in the Russian Federation. www.rmcenter.ru/files/Concept_Access_en.pdf*.

StatLink http://dx.doi.org/10.1787/888933272024

As shown in Figure 6.4, enterprises surveyed by the IFC/World Bank in the Russian Federation in 2012 were significantly less likely to have bank loans than enterprises in ECA or Upper Middle Income countries in general, although they were more likely to have deposit

accounts. Furthermore, information from SME Bank indicates that approximately 45 per cent of SME loan applications were rejected across the Russian banking system in 2011.

Figure 6.4. **Use of financial services from banks, 2012**



Source: World Bank/IFC (2012) Enterprise Surveys: Russian Federation Country Profile 2012. Washington DC World Bank Group.

StatLink http://dx.doi.org/10.1787/888933272031

There are also barriers to SME access to bank lending with respect to the costs, duration and conditions of loans where they are offered. Interest rates for approved SME loans tend to be high. Nominal interest rates were typically 14-17 per cent and real rates were typically 7-10 per cent in 2012. The vast majority of bank loans were also short term. SME Bank indicates that only 7-10 per cent of loans granted to SMEs across the banking system were for more than three years in 2012, while the State Credit Guarantee Agency has recently estimated that there is an unmet demand for long term loans by SMEs for investment purposes ranging from some RUB 365 billion to RUB 670 billion. It is also typically obligatory for an SME or new enterprise to offer collateral in order to obtain a loan, while the ratio of collateral value to loan value tends to be high and assets such as accounts receivable and vehicles are not generally acceptable. This makes it difficult for enterprises without significant eligible collateral to obtain external financing. Even where collateral can be obtained, banks may be reluctant to take it because of long and expensive legal procedures for foreclosure on collateral (Barre, 2005).

Overall, high loan refusal rates, high interest rates, short loan term periods and the need for high values of collateral are likely to stifle new enterprise start-ups and SME growth projects for which returns are not expected to be particularly large and rapid. Moreover, a vicious circle may be in operation in which the high interest rates and short term lending promote high-risk high-return entrepreneurial strategies, encouraging lenders to further protect themselves through high demands for collateral and high interest rates.

Substantial increases in bank lending

Given the shortage of external financing amongst Russian SMEs and the problems they face in accessing bank lending, it is very positive that bank lending to SMEs and entrepreneurs has increased dramatically in the Russian Federation in recent years, although there is still much more to be done. As shown in Table 6.1, the stock of SME loans

increased from RUB 2.5 billion to RUB 5.2 billion from 2008 to 2013 and the SME share in new loans to businesses increased from 19% to 23% from 2009 to 2013. Although some of this increase may be attributed to recovery from the global financial crisis in 2008-09, there is also evidence of a longer term growth trend; according to Barre (2005) bank lending to SMEs increased ten-fold from 2000 to 2005 and Lugovskaya (2010, p. 301) reported that SME lending also increased between 2005 and 2007.

At least in part, the increase in bank lending reflects strong state-driven efforts to expand the market, as suggested by the increase in the value of loans to SMEs with government guarantees to RUB 250 billion in 2013 from only RUB 67 billion in 2010 (Table 6.1).

Table 6.1. **Bank lending to SMEs in the Russian Federation, 2008-13**

Indicators	Units	2008	2009	2010	2011	2012	2013
Outstanding business loans, SMEs (stock)	RUB million	2 522 995	2 647 973	3 227 570	3 843 458	4 494 204	5 160 644
Outstanding business loans, total (stock)	RUB million	12 996 829	12 412 406	13 596 593	17 061 389	19 580 176	22 242 321
SME loan share	%	19	21	24	23	23	23
New business loans, SMEs (flows)	RUB million	..	3 014 572	4 704 715	6 055 744	6 942 525	8 064 759
New business loans, total (flows)	RUB million	..	19 091 541	20 662 219	28 412 267	30 255 044	36 224 567
SME new loan share	%		16	23	21	23	22
Government loan guarantees, SMEs	RUB million	..	18 226	32 460	58 954	87 400	116 900
Government guaranteed loans, SMEs	RUB million	..	38 917	66 824	122 747	185 000	249 000
Non-performing loans, SMEs	%	4.27	7.56	8.80	8.19	8.39	7.08
Non-performing loans, total	%	…	5.83	5.43	4.74	4.57	4.31
Interest rate, SMEs	%	..	..	..	..	..	13.10
Interest rate, large firms	%	14.1	13.8	9.8	10.6	10.6	11.1

Source: OECD (2015a) Financing SMEs and Entrepreneurs 2015: an OECD Scoreboard, OECD Publishing, Paris.

StatLink http://dx.doi.org/10.1787/888933272317

Difficulties in assessing loan applications

One of the issues constraining bank lending to SMEs and entrepreneurs in the Russian Federation is the high costs and workloads for banks to assess the risk of loans to SMEs and entrepreneurs and monitor their performance relative to the size of the loans made. In the case of the Russian Federation, the general problem of small lending balances in the context of the fixed cost of loan administration is exacerbated by an onerous administrative burden with respect to the estimation of loan loss provisioning, which diverts personnel from loan adjudication and monitoring. In addition, the imputed taxation scheme reduces SME borrowers' motivation to be transparent since it does not require the majority of entrepreneurs to provide financial statements. This lack of transparency increases the difficulties for banks to judge the risks of loans using easily available company financial data.

At the same time, lack of an SME lending tradition in the Russian Federation has hampered the emergence of skilled and experienced staff and the use of efficient lending technologies in banks for lending to SMEs and entrepreneurs. While international development banks such as the European Bank for Reconstruction and Development and

the International Financial Corporation have sought to respond by providing training for SME loan account managers in the Russian Federation, much of this learning is confined to the large state-owned banks and has not been of sufficient scale to address the problems. Furthermore, while a few of the larger banks have developed credit scoring algorithms based on their own experience, the vast majority of banks do not have access to credit scoring tools. This problem is exacerbated by the lack of public credit registry information, which limits the ability of banks and other investors to assess SME credit risk for lending purposes. A private bureau, the National Bureau of Credit Histories, started operations in 2006 and provides coverage of 59% of borrowers, compared with typical coverage of credit bureau information of 67% in OECD countries and 33% in ECA countries (World Bank/IFC, 2014). However, there appears to be a limited level of awareness or willingness to use this source of information in the banking industry.

Volatility, uncertainty and lack of securitisation

There are also a number of reasons for the predominance of short-term financing over long-term financing in SME bank lending in the Russian Federation. These include:

- A high and variable rate of inflation (13.3 per cent in 2008; 8.4 percent in 2011; 5.1 per cent in 2012, 7.8% in 2014).
- Under Russian Federation law, individual depositors can terminate any deposits without notice, so reliability of long-term deposits is limited.
- The 2008 global financial crisis prompted a substantial increase in interest rates, which led the state to make injections of relatively less expensive short-term credit through state-owned banks, resulting in a steep yield curve. Enterprises were therefore more likely to use short-term financing for long-term projects.
- Corruption creates uncertainty even about successful borrower firms' future prospects and erodes the trust of entrepreneurs in the banking system in the event, for example, that bribes need to be paid to secure a loan.
- Banks also face considerable uncertainty as to what forms of fees and commissions they may charge. For example, RSBF (2012, p.12-15) reports that the Russian Supreme Arbitration Court has ruled that "commissions which do not produce any additional value or other positive effect for the customer cannot be understood as services" and that has resulted in a high degree of uncertainty about what types of fees are and are not permissible.
- There is an incomplete inter-bank lending market, which limits lenders' ability to refinance long-term loans to SMEs. There is little standardisation across the system (for example, loan contracts differ across banks and even among different branches of larger banks), which limits the scope for securitisation. Legislation to provide for securitisation has been introduced but does not appear to have proceeded.

The short-term nature of lending that these factors brings about is a constraint to SME investment, growth and sustainability. SME growth requires that SMEs add to the stock of producer assets, working capital (inventories and accounts receivable), and human capital (especially for firms in the services sector). In OECD countries, these forms of real capital are generally obtained by incremental external financing, most often in the form of long-term bank lending. This is a market that, in the Russian Federation, requires remediation.

Microfinance for SMEs and entrepreneurs

Large and growing microfinance market

Microfinance involves the provision of retail financial services in small amounts (e.g. less than 300% of a country's per capita GDP) by non-bank financial institutions to customers who lack access to conventional finance. As well as lending to households to reduce poverty, microfinance can play an important role in supporting people in setting up and running micro and small businesses. Indeed, in the Russian Federation this entrepreneurship function appears to have been the dominant motivation for the introduction of microfinance (Buyske, 2007). Because bank financing is very limited for start-up and small firms in the Russian Federation, the establishment of a system of microfinance organisations provides an alternative means of supporting SME development. Additional advantages as compared with bank lending include simplified reporting and documentation requirements, the option of non-traditional forms of loans (solidarity guarantees, group lending, etc.), and comparatively accessible financial resources and convenient services. However, micro finance is not a substitute for the long-term financing required by growth-oriented enterprises.

The numbers of micro finance institutions (MFIs) in the Russian Federation are growing rapidly. In 2008, there were approximately 2 300 MFIs with an aggregate loan portfolio of approximately RUB 25 billion. By 2012, this had grown to 3 570 providers collectively managing a portfolio of approximately RUB 35 billion (Russian Microfinance Center, 2013). They include credit cooperatives funded by their members, who are also the eligible loan recipients (approximately 1 200, the largest category), specialised NGO-type microfinance institutions including co-operatives, state-supported funds, and commercial non-bank financial institutions operating on a for-profit basis, including high price payday loan operations. Approximately 70 per cent of the MFIs lend to SMEs. Approximately 20 per cent of the business loans they make are to start-ups and 80 per cent to more established small enterprises.

The state-supported funds manage a portfolio of approximately RUB 12 billion through approximately 70 regional and 60 municipal micro finance organisations. The funds are primarily provided through the federal Ministry of Economic Development and Vnesheconombank and channelled through regional and municipal governments, which appoint supervisory boards that in turn appoint a credit committee and fund manager. Collectively, the state-supported funds had advanced approximately 20 000 loans at the end of 2012, of which RUB 7.9 billion was outstanding. The loans focused on start-up enterprises (less than one year since registration). Approximately 33 per cent were to firms in the retail sector, 18 per cent to manufacturing firms, and 12 per cent to firms in the agricultural sector. The 2011 loss rate was 7.6 per cent. The state-supported MFIs also provided some degree of training and business education to loan recipients.

Positioned in small, short-term and high-interest loans

The microfinance sector currently plays an important role in offering finance to start-ups and micro and small firms in the Russian Federation, which to some extent mitigates the current gap in bank lending. However, it should not be seen as a long-term substitute for bank lending because it cannot meet the demand for longer-term, lower cost SME finance.

Although there are many organisations, micro finance only reaches a relatively small proportion of the population of SMEs that need loan finance. It is estimated that even in Moscow and St. Petersburg, where microfinance organisations have the strongest implantation, they cover only about 10 per cent of the demand, while in many regions there is very little coverage at all (Russian Microfinance Center, 2013). While it makes sense to fill these main regional gaps, micro finance should not be used as a substitute for bank lending because the loans are generally very small and short term, and therefore appropriate only to the finance needs of the smallest SMEs and start-ups. In 2012, the typical business loans of Russian MFIs ranged between RUB 60 000 to RUB 900 000, with maturities of typically six months to one year (Russian Microfinance Centre, 2013). The average loan from state-supported MFIs was of the order of RUB 450 000, and again the vast majority were for less than one year.

Micro finance is also relatively high cost, which will hold back the rate of SME investment and growth compared with cheaper sources. As a whole the sector charges real interest rates of around 15 to 20 per cent, and although the state-supported funds typically have lower rates, of around 10 per cent annually, this partly reflects the use of stricter lending criteria. High costs are intrinsic to the business model of the sector, which although being very accessible, needs to charge high rates because of the fixed cost element on small loan balances.

Improving regulation and governance

Measures could also be taken to improve the regulation and governance of the microfinance sector in order to favour the growth of the most efficient and fair organisations and ensure the sustainability of the system. One particular issue is that it can be difficult for borrowers to distinguish predatory lenders (including payday loan companies) from reputable institutions.[1] This has prompted the Russian Microfinance Center to outline a series of measures that would help borrowers to distinguish between payday lenders and responsible MFIs and establish protections for clients of payday lenders. These include:

- Payday lenders licensed as MFIs should be separated from the other MFIs in the state register.
- Reporting to credit bureaus should be mandatory for all payday lenders and MFIs.
- The Russian Central Bank and Federal Financial Markets Service should regularly publish average interest rates on retail credit products offered by banks, payday lenders, MFIs and credit cooperatives and establish that interest rates higher than 200 per cent of the average are to be considered usurious (and labelled clearly as such, though not prohibited).
- Payday lenders should be restricted in their ability to raise funding from individuals (something other MFIs are permitted to do under Russian law, but within limits).
- All MFIs should be members of self-regulated organisations, to reduce instances of unethical market conduct.

In addition, the sustainability of the microfinance sector could be strengthened and interest rates reduced somewhat through technical assistance to support MFIs to develop credit scoring systems to assess more effectively the risk of clients.

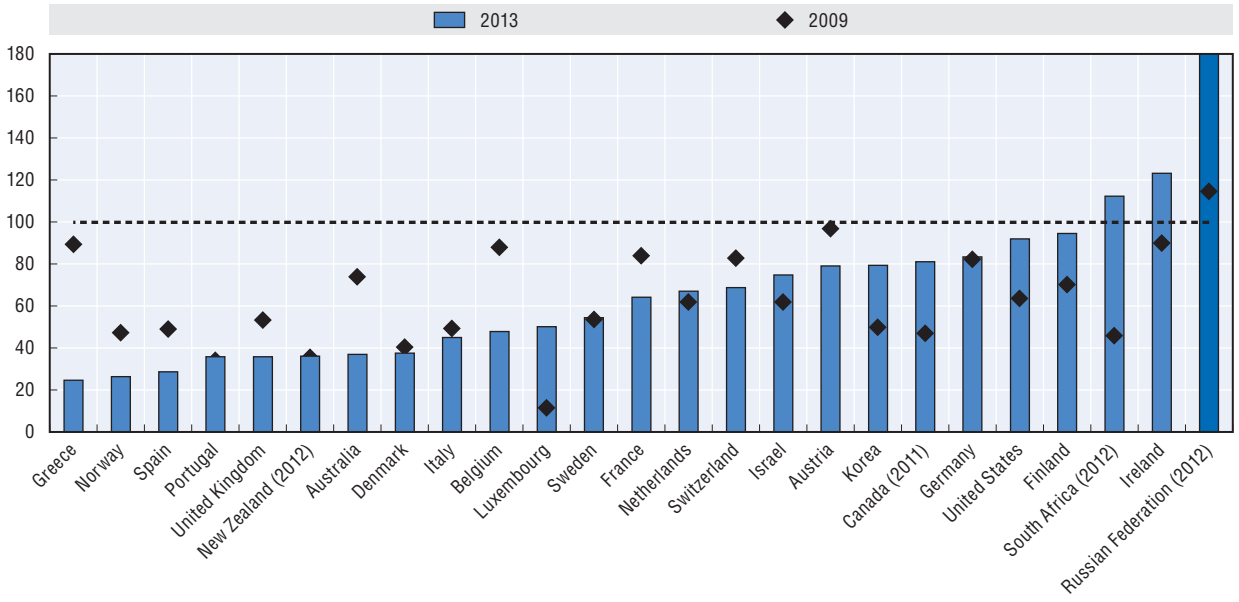
External equity financing

Rapid growth in venture capital

Seed and early stage venture capital investment (i.e. equity capital that is not channelled through stock markets) has increased significantly in the Russian Federation, from approximately USD 108 million in 2007 to USD 398 million in 2012. This rate of growth exceeds that of comparator countries for which data are available (Figure 6.5).

Figure 6.5. **Growth in seed and early-stage venture capital investment flows**

Index 2007 = 100



Source: OECD (2014), Venture capital trends: Index 2007 = 100, in Entrepreneurship at a Glance 2014, OECD Publishing, Paris. DOI: *http://dx.doi.org/10.1787/entrepreneur_aag-2014-graph89-en*.

StatLink *http://dx.doi.org/10.1787/888933272041*

Table 6.2 shows the evolution of private equity and venture capital investment in the Russian Federation from 2009-12, broken down by stage of investment.[2] [3] It illustrates that only a minority of venture capital (less than ten per cent) was invested in early stage firms. Total investment in the expansion, restructuring and later stages involved only 58 investee companies but comprised USD 3.75 billion of the USD 4.15 billion invested in 2012. However, the growth has involved all investment stages. Furthermore, as shown in Table 6.3, the number of active funds increased from 80 in 2008 to 155 in 2012 and the stock of outstanding private equity and venture capital investment increased from USD 14.3 billion in 2008 to USD 26.4 billion in 2012.

Table 6.2. **Recent private equity and venture capital activity in the Russian Federation**

Million USD, flows

	2009		2010		2011		2012	
	Amount	%	Amount	%	Amount	%	Amount	%
Seed & Start-up	13	2.6	22	0.9	129	4.2	129	3.1
Other early stage	110	21.7	132	5.2	143	4.6	269	6.5
Expansion	314	61.9	2 258	89.8	980	31.8	2 037	49.1
Restructuring	70	13.8	3	0.1	7	0.2	353	8.5
Later stages	0	0.0	100	4.0	1824	59.2	1 364	32.9
Total	508	100.0	2 514	100.0	3083	100.0	4 152	100.0

Source: Russian Private Equity and Venture Capital Market Review: 2013 Yearbook (2014). Russian Venture Capital Association, Moscow.

StatLink *http://dx.doi.org/10.1787/888933272326*

The federal government has been an important player in developing the venture capital sector through the establishment in 2006 of the Russian Venture Company, as a federal government financed fund-of-funds seeking to stimulate venture capital investment in the high-technology sector. This enabled the establishment of regional venture capital funds in 19 regions in 2006, which had increased to 22 regional funds by 2011. The Russian

Venture Company held approximately RUB 20 billion under management in 2011 and had made cumulative investments of approximately RUB 4.2 billion. During 2011, 15 companies received investments of approximately RUB 1.4 billion, mostly at early stages of development but with 15% of deal volume at the restructuring stage.

Table 6.3. **Capitalisation of private equity and venture capital funds in the Russian Federation 2008-12**

USD million (stocks)

Year	Amount	Number of active funds
2008	14 327	80
2009	15 192	87
2010	16 787	91
2011	20 092	97
2012	26 419	155

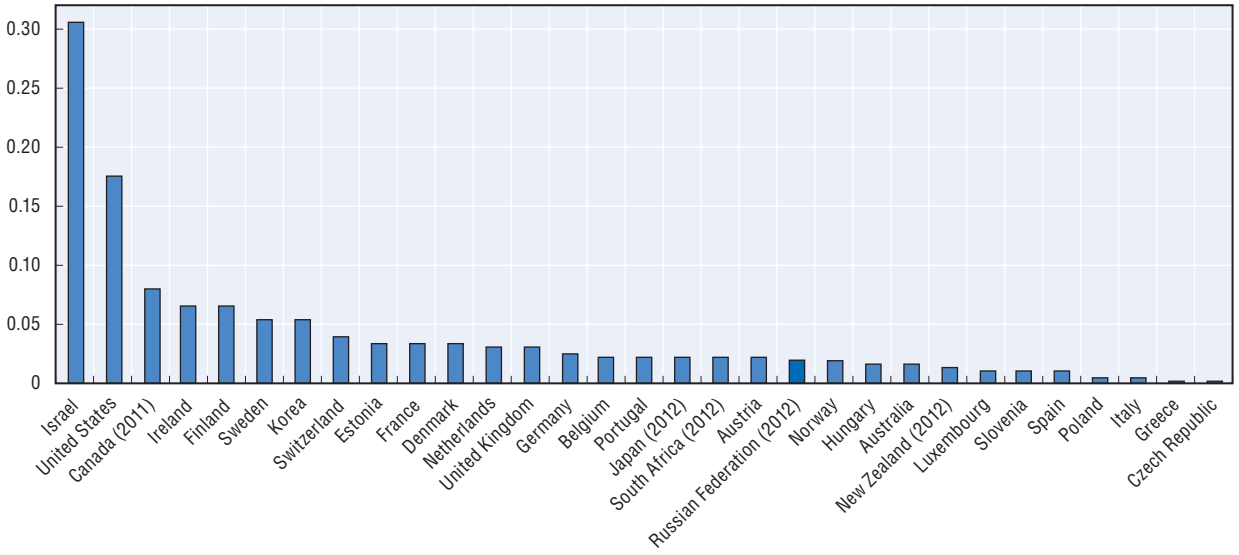
Source: OECD (2014b) Financing SMEs and Entrepreneurs 2014, OECD Publishing, Paris.

StatLink http://dx.doi.org/10.1787/888933272332

As a result of these recent trends, total flows of private equity and venture capital investments in the Russian Federation have reached levels associated with many OECD countries (Figure 6.6). The sectoral distribution of investments is shown in Figure 6.7, indicating that there are external equity investments in quite a wide range of sectors.

Figure 6.6. **Private equity and venture capital investments as a proportion of GDP**

Flows, percentage of GDP



Note: Includes later stage investments as well as seed and early stage investments.

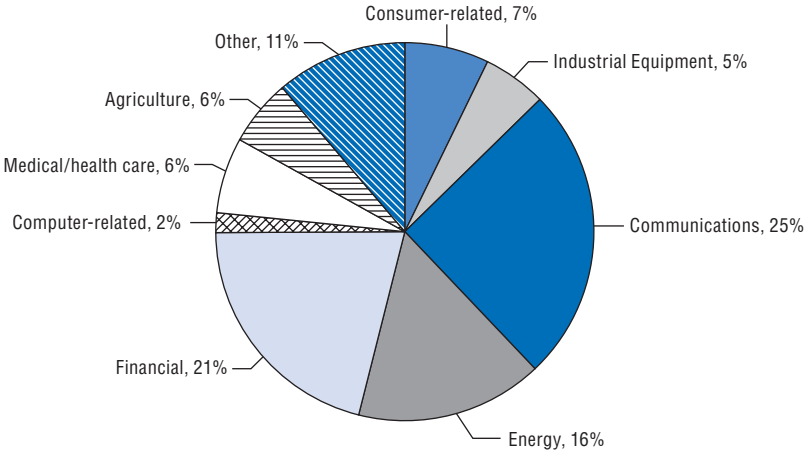
Source: OECD (2014), Venture capital investments as a percentage of GDP: Percentage, 2013, in Entrepreneurship at a Glance 2014, OECD Publishing, Paris. DOI: *http://dx.doi.org/10.1787/entrepreneur_aag-2014-graph88-en*.

StatLink http://dx.doi.org/10.1787/888933272054

With a stock of USD 26.4 billion and a flow of USD 4.15 billion of private equity and venture capital investment in 2012, it does not appear that, overall, there is a shortage of external equity investment. These data suggest that at least six years of supply are under management. It may be true that there are shortages of venture capital supply in certain regions, particularly given that a substantial proportion of total venture capital is associated with the Skolkovo initiative in Moscow. However, any shortfall in the overall scale of venture

capital investment compared with other countries at the current time may be more a consequence of a shortage of demand from investment-ready growth-oriented SMEs than problems in supply, quite possibly reflecting an upstream lack of bank lending for early stage and growth-oriented enterprises. On the other hand, with longer-term actions to expand the pipeline of promising firms coming through for seed and early stage venture capital investments a further long-term growth in the scale of investment could be required.

Figure 6.7. **Sectoral distribution of Russian Federation private equity and venture capital investments, 2012**



Source: Russian Private Equity and Venture Capital Market Review: 2012 Yearbook, (2013). Russian Venture Capital Association, Moscow.

StatLink http://dx.doi.org/10.1787/888933272064

Small venture capital fund sizes

Venture capital funds are nevertheless of relatively small size in the Russian Federation. Of 120 venture capital management companies, the Russian Venture Capital Association classifies 34 as "large," that is, holding more than USD 150 million under management (the largest fund holds USD 2.2 billion). Collectively, these large funds managed USD 15.6 billion. At the small end of the spectrum were 53 management companies, each with less than USD 50 million under management, collectively managing USD 1.38 billion. The remaining 33 funds each held from USD 50 to USD 150 million under management, for a total of just over USD 3 billion. Compared with other countries, this fund size distribution is skewed towards the small end of the spectrum. Given evidence that small funds face significant difficulties in achieving sufficient portfolio spread, scale economies, and funding packages for larger early and follow-on investments, which affects their performance (Murray, 2007; Nitani and Riding, 2013; Söderblom and Wiklund, 2005), this suggests a need to focus any future public interventions aimed at the sector on expanding and consolidating existing funds rather than creating new ones.

Nascent business angel sector

Business angel finance involves investments of their own money by cash-rich and experienced entrepreneurs directly into the equity of growth-oriented start-up companies. Business angels tend to take minority stakes in the enterprises they invest in, play key mentorship roles in the management of the enterprises, seek a return through the sale of the companies through an Initial Public Offering or merger or acquisition, maintain a

small portfolio of investments in enterprises, and reinvest some of the returns in other enterprises. The business angel sector is still at a formative stage in the Russian Federation, but could play an important role in the future, not only in offering financing, but also by offering skills, networks and mentoring to high potential enterprises, if a boost is given to the sector with appropriate public sector interventions.

Initially, public actions are needed to improve legal protection for minority shareholders in order to facilitate the entry and exit of angels from their investments and the ability to influence the management of the enterprises they invest in (Kashirin, 2007). Business angel investment also needs to be recognised in wider investment regulations. For example, although business angels invest their personal wealth as individuals they could nonetheless be considered professional investors for the purposes of regulation, giving them more flexibility to operate.

Angel investing is inherently local. Research shows that the small scale inherent in business angel investment, coupled with angels' need to monitor and mentor their investments, militates strongly in favour of local investment activity. Accordingly, the development of business angel networks in many countries has followed a two-stage process. In the first stage, angel investing at the local level needs to be fostered. Often, this aspect has been accomplished by local or regional economic development agencies that often create local angel-entrepreneur "matchmaking" facilities. This is a process that could be encouraged through federal government financial support and guidance. In the second stage, local networks are connected through a national organisation (see the example in Box 6.1). The role of the national organisation is to provide visibility for angel investing, disseminate best practices, and linkages with government bodies and other initiatives that foster entrepreneurship. This is especially important in the geographically diverse Russian Federation.

Box 6.1. **National Angel Capital Organisation, Canada**

The approach

In Canada, the National Angel Capital Organisation (NACO) acts as an umbrella organisation to support local business angel networks. It "accelerates a thriving, early stage investing ecosystem in Canada by connecting individuals, groups and other partners that support angel-stage investing. NACO provides intelligence, tools and resources for its members; facilitates key connections across networks, borders and industries; and helps to inform policy affecting the angel asset class" (*https://nacocanada.com/about/what-we-do/*).

Results

The following are among the outcomes of the NACO initiative:

- NACO prepares and publishes an annual Report on Angel Investing Activity in Canada. It analyses trends in angel investing and provides a perspective on the national angel market.
- NACO, often working with a counterpart US-based organisation, provides considerable professional development for angels and angel groups. Workshops include: Angel Investing – An Overview; Valuation of Early Stage Companies; Trends in Raising Capital; Due Diligence; An In-Depth Look at Term Sheets; Mentoring and Governance; Starting an Angel Organisation.
- NACO also seeks to represent the national angel community with industry and government partners, seeking to better inform the development of salient policy frameworks and to promote angel investor groups in the context of Canada's innovation and entrepreneurial ecosystem.
- Additional resources that NACO provides for its members include summaries of best practices in angel investing.

Box 6.1. **National Angel Capital Organisation, Canada** (*cont.*)

Success factors

Because NACO acts as a national umbrella organisation for geographically-dispersed local angel groups, success is dependent on the involvement of its various partners. Success depends on fostering trust and value-added for the participants.

Relevance to the Russian Federation

Both Canada and the Russian Federation are characterised by strong geographical dispersion of population and the presence of many local concentrations of wealth and economic activity. Local business angel networks can match with this geography. A national confederation of angel groups can help support such local angel groups.

Further information

https://nacocanada.com/

Source: National Angel Capital Organisation, Canada

Accordingly, public authorities can play a role in funding the set up and/or operational costs of local business angel networks in the Russian Federation and supporting the creation of a national umbrella business angel organisation. Local business angel networks can not only recruit business angels but also help them connect to high growth potential start-ups, increase the awareness of the opportunities for obtaining angel investment among high growth potential start-ups, facilitate the creation of business angel syndicates to undertake certain investments together and support sharing of information and analysis among angel investors. They also raise the visibility of business angels to the officials running public SME support programmes, which in the Russian Federation are often not aware of angel investment.

An important first step has already been taken through the formation in 2006 of the National Union of Business Angels of Russia (RUSSBA) as a non-profit partnership established with the support of the Russian Private Equity and Venture Capital Association and the Chamber of Industry and Commerce of Russia. RUSSBA comprises private and institutional investors who invest in innovative and high technology companies, and assists business angel activity in the Russian Federation through programmes, projects and events, and analysis and information activities. It can also play a role in matching potential investee companies with potential investors. Public support could help expand or replicate this approach. It could also help develop online matching services, which are increasingly being tested in other countries, although elements of face-to-face contact will still be needed.

Another approach to building the business angel sector that could be considered in the Russian Federation is increasing the amount of financing that business angels are ready to channel to growth-oriented start-ups. One method is to offer tax incentives to investors in SME equity, for example by exempting investors from capital gains tax on returns from investments made in start-ups if they meet certain conditions, such as a minimum period of investment or reinvestment of returns in another start-up. Another method is to co-invest public resources together with those of angels, for example through joint investments with business angels or business angel syndicates by state-supported venture capital funds. An example of this type of approach is the Angel CoFund in the UK,

which invests amounts of GBP 100 000 to GBP 1 million in SMEs with high growth potential in partnership with syndicates of experienced business angels (OECD, 2015b).

Business angel support should be seen as an important part of any public programmes for high-growth entrepreneurship, including the package of support offered by innovation incubators and programmes for the commercialisation of university research. As well as network creation and co-investments, support for business angels as part of these broader programmes could provide training, coaching and mentoring to potential business angels in how to make effective investments and contribute effectively to start-up company development as well as activities to build the awareness of high growth potential start-ups on how to access business angel funding and how to make their projects "investment ready".

Key cross-cutting public interventions

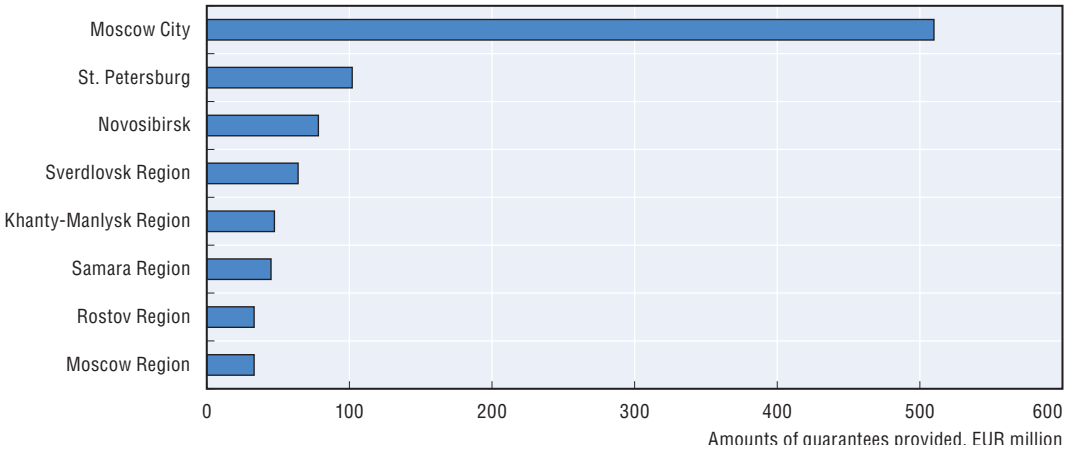
Role of credit guarantee programmes

An important public policy intervention that can help to build up credit to SMEs and entrepreneurs is the award of public credit guarantees to banks and microfinance institutions for lending to SMEs and start-ups that would not otherwise obtain financing, thus providing an alternative form of reliable collateral. Credit guarantee programmes are widely used by national and local governments and public development banks to facilitate access to finance for enterprises that may otherwise be "constrained by information asymmetry, limited credit history and under-collateralisation" (OECD, 2015c, p. 37).[4]

Credit guarantees provide governments with an efficient means of levering state resources in order to achieve much larger amounts of SME lending than could be achieved by direct state lending because the public costs are limited to the administration of the programme and covering a part of the defaults from the minority of firms that does not repay loans. In some credit guarantee programmes, fees paid by borrowers partly offset these costs. Intervention through guarantees, rather than direct loans or subsidies, also helps extend the reach of public policy to a wider range of SMEs by accessing firms that approach banks but may not approach public agencies or be aware of public schemes. For banks, the attraction is that the guarantee reduces some of the high risks of dealing with SMEs and entrepreneurs and enables them to build their experience and capacities in this area. The use of credit guarantees in the Russian Federation would therefore assist with a gradual withdrawal of the state from the banking business and from direct state lending and subsidies to SMEs by strengthening the offer of commercial credit.

In 2006, the federal SME support programme established credit guarantee funds in each region of the Russian Federation. In most cases, regions and municipalities provided 30% of the resources while the federal Ministry of Economic Development provided 70% (in certain regions, including Moscow and St. Petersburg, the financing ratio was 50/50). The funds provide partner banks with guarantees of up to 70% of the loan amount for periods of more than one year. The fixed annual fee for the issue of a guarantee is one-third of the Central Bank refinancing rate. The total resources in the regional funds were RUB 33 billion in 2013. At that time a cumulative 33 000 guarantees had been provided to authorised banks with an assumed credit risk of RUB 117 billion, enabling a total SME loan amount of over RUB 249 billion. Figure 6.8 illustrates the scale of capitalisation of the largest of the loan guarantee funds, showing the Moscow Loan Guarantee Fund as the largest (see Box 6.2). Subsequently, in July 2013, SME Bank established its own guarantee mechanism aimed at supporting lending to medium-sized enterprises.

Figure 6.8. **Scale of operations, Russian Federation loan guarantee programmes, 2013**



Note: Data at 1 January 2013.

Source: Moscow Loan Guarantee Fund (2013).

StatLink http://dx.doi.org/10.1787/888933272076

Box 6.2. **Moscow Loan Guarantee Fund**

The Moscow Loan Guarantee Fund demonstrates how credit guarantee schemes are able to lever government expenditures to help SMEs obtain bank loans and foster competition in the financial market for SMEs. It is the largest of the regional credit guarantee funds, with a capital of RUB 7.5 billion in 2013, and as such is able to exploit economies of scale. It co-operates with approximately 40 partner banks.

The Fund operates by sharing risk with the financial institution that makes the loan and the borrower. To access the guarantee, a borrower SME applies to one of the commercial banks with which the Fund is in partnership. If the bank is favourably disposed to granting the loan application but the borrower has insufficient collateral, the borrower and the bank apply for a guarantee to the Fund. If approved, a tripartite agreement (lender, borrower, guarantor) is signed, the fee for the guarantee is paid and the loan is approved. The maximum liability of the Fund is limited to 70% of the principal debt and interest amount, but not more than RUB 70 million.

Between 2006 and 2013 the Moscow Loan Guarantee Fund provided RUB 26 billion in loan guarantees, which enabled SMEs to obtain RUB 54 billion in bank loans. The majority of these loans were additional in the sense that they would not otherwise have been granted. It is estimated that an additional RUB 40.8 billion in lending was generated at a gross public cost of approximately RUB 1.3 billion, which was the cost of honouring defaults on the loans (including during the 2007-08 financial crisis period). This cost was offset to some extent by the fees paid for use of the scheme. The recipient SMEs were also able to grow, hire additional employees and add to the tax base as a result of their additional operations.

Source: Information supplied by Moscow Loan Guarantee Fund

A further major step was taken in 2014, with the establishment alongside the regional funds of the Federal Credit Guarantee Agency, with a registered capital of some RUB 37 billion. The main mission of this new national agency is to guarantee long-term SME investment loans by accredited banks, with a target of providing guarantees worth some RUB 170 billion supporting total SME loan amounts of some RUB 300 billion by 2016. This represents a doubling of the guaranteed loan amounts from the existing regional funds. In this endeavour, the agency will set up guarantee portfolios (composed of direct

guarantees, counter guarantees and syndicated guarantees) for credits from banks and other financial institutions to businesses with turnovers of less than some RUB 750 million. The guarantees are unsecured liabilities worth up to 70% of the loan amounts for terms of up to 15 years and 120 days (88 months) for eligible SME investment projects, including premises, plant and equipment and innovation projects associated with new products and markets. The Agency has been working with some 27 accredited partner banks, but plans to increase this number. It promises quick decision making for banks on the award of the guarantees (a targeted 10-day review period).

As well as increasing the volume of SME lending, the Federal Guarantee Agency aims to reduce interest rates on SME loans by agreements with banks on interest rates charged and to enable banks to start securitisation of SME loans to help build a secondary market. Further tasks will be support for leasing production equipment, providing capital to microfinance institutions, refinancing existing SME loans and providing capacity building and technical support for strengthening of the regional and municipal loan guarantee funds, including through developing and implementing common national standards and procedures for guarantee support and risk management.

In starting up the operations of the Federal Credit Guarantee Agency and strengthening the existing regional and municipal funds, it will be important to make good choices about the key parameters of the schemes. These parameters include (OECD, 2013):

- *Eligibility*. Loan guarantees are typically targeted to SMEs. Accordingly, most schemes limit the size of loan or guarantee available. Some programmes limit guarantees to particular industry sectors and set limits on the size of eligible borrower firms. Some schemes allow guarantees for loans to support working capital while others do not.
- *Per cent of loan guaranteed*. Guarantees typically range from 50 to 85 per cent of the outstanding loan balances, but the guarantee percentage varies widely across programmes.
- *Fees*. In some programmes borrowers pay a fee to the guarantor. Fees may be up front or over the courses of the loan or both.
- *Others*. Other parameters can include whether or not guarantees are re-insured; the extent to which the guarantor is involved in loan adjudication; and whether the programme is based on a pre-determined guarantee fund or whether the guarantor provides funding on an on-going basis.

Particular attention should be paid to how the parameters used by schemes in the Russian Federation influence the extent to which guaranteed loans are additional to loans that would otherwise have been made and the extent to which the schemes are financially sustainable without placing excessive burdens on state resources. A further consideration is the need to achieve efficiency and take advantage of economies of scale. While the larger credit guarantee programmes, e.g. in Moscow and St. Petersburg are perhaps able to take advantage of such efficiencies, this cannot be said of many of the smaller regional programmes. These smaller programmes might be better integrated into the national credit guarantee system or consolidated into a smaller number of regional programmes. Robust evaluations will be important in providing information to assist in the programme designs. In addition, it makes sense to learn from the experience of other countries. Box 6.3 reports, for example, on the experience of the Canada Small Business Financing Program (CSBFP).

Box 6.3. **Small Business Financing Programme, Canada**

The approach

The Canada Small Business Financing Programme (CSBFP) is a credit guarantee scheme that facilitates debt financing for higher risk SMEs, firms that would not normally receive financing. Since its launch in 1961, the programme has assisted more than 500 000 Canadian businesses to start, expand, modernise or improve.

To receive a guarantee, an SME first needs to seek financing from one of more than 1 500 eligible private sector commercial lenders. The prospective lender could reject the loan application or decide to finance the SME using its own conventional products. However, if the project appears too risky for a conventional loan but nonetheless appears to have fairly good chances of success, the lender could decide to make a loan backed by a CSBFP guarantee. To be eligible, the loan value must be smaller than USD 350 000 and go to an SME with annual revenues below USD 5 million. The loans are normally for acquiring real property and equipment and making leasehold improvements.

The CSBFP (through Industry Canada) is liable to pay up to 85% of eligible losses on defaulted loans registered under the programme. To help offset the cost of losses, it charges the lender an upfront fee of 2% of the value of the loan and an annual fee of 1.25% of the outstanding balance, which is remitted by the lender through the interest charged to the borrower. The programme caps the variable interest rate that lenders can charge SMEs at no more than 3% more than their prime rate (and caps fixed interest at the single-family mortgage rate plus 3%). These measures aim to ensure that while riskier loans are simply refused any financing and less risky loans are taken on directly by the banks without guarantee, intermediate investment projects which are riskier, often due to a lack of collateral, but appear viable, can go ahead with a guarantee. The CSBFP does not provide working capital financing.

Results

One of the primary objectives of the CSBF programme is to be additional ("incremental"), i.e. to finance loans that would not otherwise be available. It has been estimated that 75 per cent of the loans made would not otherwise have been provided (Riding et al., 2007).

A second primary objective of the programme is to achieve cost recovery over time, i.e. revenues from fees should offset the cost of claims for defaulted loans. The following table summarises the recent experience. The lending volume facilitated by the programme was approximately USD 1 billion per year at a loss rate of approximately 8 per cent. The gross government costs of the losses were to a large extent offset by the fees from borrowers. Overall, each dollar expended by government facilitated 12 dollars of private sector lending.

In addition, the programme aims to deliver social benefits that outweigh the costs, e.g. in terms of jobs created and additional taxes paid. Chandler (2012) has estimated that participation in the CSBFP in 2004 would have increased an enterprise's growth in salary, employment and revenues by 12, 12, and 7 percentage points, respectively, between 2004 and 2006. Furthermore, the CSBFP programme would have induced the incremental creation of approximately 5,000 new jobs during that period, comprising almost four per cent of all new jobs created in that period by SMEs.

Success factors

The achievement of substantial economic development benefits at low public cost reflects the leveraging of large volumes of additional private lending. The fact that it is private lenders themselves that must bring forward loan proposals to the programme helps achieve outreach to SMEs, while the need for SMEs to pay additional fees and for banks to take a share of the risk reduces the incentive to include non-additional loans.

Relevance to the Russian Federation

Credit guarantee programmes have been adopted by more than 60 nations. However, in many cases the programmes have either lacked sustainability or placed unacceptable financial burdens on the guarantors.

Box 6.3. **Small Business Financing Programme, Canada** *(cont.)*

OECD (2013) argues that the design of the programmes is paramount, with key parameters including the coverage ratio, term of the guarantee (i.e. length) and pricing. The CSBFP has been successful in developing criteria that have delivered a sustainable and effective programme for Canada.

Table 6.4 **Canada Small Business Financing Programme Activity, 1995-2011**

Year of disbursement	Loan Volume (USD million)	Number of loans	Claims Paid (USD million)	Number of claims	Losses (% of loan volumes)	Claims (% of loans)
1995-96	2 243	34 607	230	5 384	10.3	15.6
1996-97	2 010	30 855	185	4 372	9.2	14.2
1997-98	1 966	28 911	164	3 661	8.3	12.7
1998-99	1 607	22 445	142	2 936	8.8	13.1
1999-2000	1 343	17 614	115	2 367	8.6	13.4
2000-01	1 159	14 439	100	1 975	8.7	13.7
2001-02	898	11 008	65	1 268	7.3	11.5
2002-03	948	11 229	64	1 192	6.7	10.6
2003-04	996	11 040	76	1 369	7.7	12.4
2004-05	1 035	11 078	81	1 410	7.9	12.7
2005-06	1 081	10 719	103	1 520	9.5	14.2
2006-07	1 024	9 592	97	1 368	9.5	14.3
2007-08	987	8 929	95	1 223	9.7	13.7
2008-09*	896	7 751	57	717	6.4	9.3
2009-10*	950	7 510	39	467	4.1	6.2
2010-11*	1 009	7 405	17	193	1.6	2.6
Total	28 951	405 005	2 286	48 496	7.9	12.0

*Note that many of the loans disbursed in recent years remain outstanding and claims on such loans may yet be received.

StatLink http://dx.doi.org/10.1787/888933272343

Further information

www.ic.gc.ca/eic/site/csbfp-pfpec.nsf/eng/Home

Source: Riding et al. (2007); Chandler (2012); information supplied by Industry Canada.

Potential of credit bureaus

In advanced SME finance markets, banks, microfinance organisations and other investors can purchase credit assessments of loan applicants from one or more central credit bureaus that typically provide more than 95 per cent coverage. Credit assessment bureaus can provide lenders with valuable information about a prospective borrower's credit history and behaviour towards creditors, which facilitates the use of credit scoring methods to increase the effectiveness and efficiency of lending decisions. Box 6.4 gives the example of the use of the Beacon Score credit scoring by a microfinance institution. However, according to World Bank data, private sector credit bureau coverage in the Russian Federation is only 59 per cent. This suggests the need for government action to increase access to credit data to enable banks and other credit organisations to assess the riskiness of individual and business borrowers based on credit histories and other parameters.

Box 6.4. **The use of Beacon Score credit scoring methods**

The approach

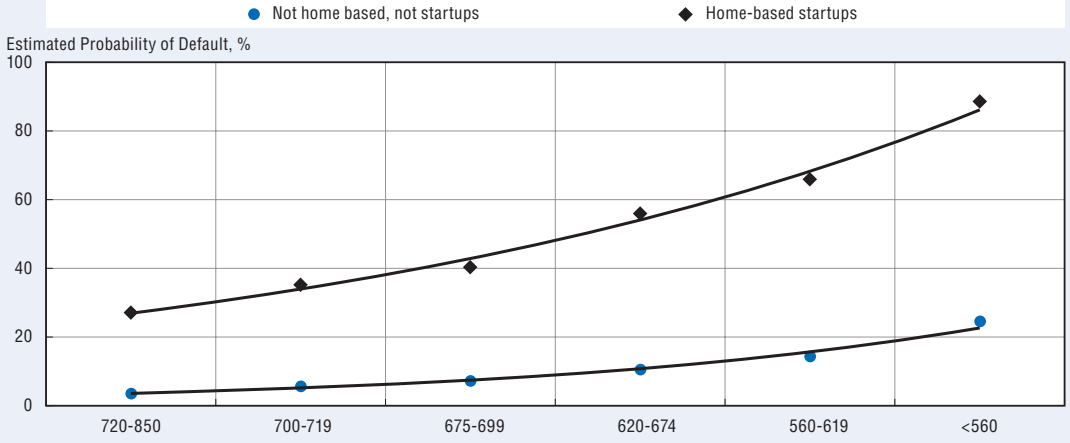
Beacon Scores are based on five criteria (approximate weightings in parentheses): past payment history (33%); amount of credit owing (33%); length of time credit established (12%); search for and acquisition of new credit (12%); types of credit established (10%). The following table illustrates how Beacon scores might be interpreted:

Beacon Score Range	Grade
720-850	Excellent
700-719	Very Good
675-699	Good
620-674	Fair
560-619	Bad
<560	Very Bad

The Alberta Women Entrepreneurs (AWE) programme uses Beacon Scores obtained from Equifax Canada, a private sector credit bureau, as an input into its decisions on the allocation of its USD 5 million loan fund. The fund provides term loans of up to USD 150 000 to eligible female residents who wish to start, expand or purchase a business. Loans have flexible repayment options and are repayable with terms of up to 5 years at a rate equal to three percentage points above the bank prime rate. Loan administration fees are 1% of the amount loaned to a maximum of USD 500.

Results

The graph below shows the relationship between Beacon Scores and actual patterns of loan defaults experienced by AWE. Higher Beacon Scores are associated with a lower probability of default. Thus the use of the scores has been important in increasing the sustainability of the programme. However, context is also important. For example, probabilities of default are higher for home based than non-home based firms and for younger than older firms.



Success factors

Taking into account Beacon Scores in lending decisions is rapid and cheap for AWE. However, the score is not the sole criterion used. In particular, in the case of AWE, a business advisory service has been coupled with the micro lending, which provides a useful means of discouraging the start-up of non-viable enterprises and increasing the chances of success of those businesses supported financially.

Box 6.4. **The use of Beacon Score credit scoring methods** *(cont.)*

Relevance to the Russian Federation

Simple credit scoring could increase the efficiency and viability of SME lending by banks and microfinance institutions in the Russian Federation on condition that credit information on individual borrowers is available. This can be promoted by encouraging state-supported credit bodies to share their data with a central credit information database or bureau.

Further information

www.awebusiness.com/pages/home/default.aspx

Source: Information from *www.beaconscore.ca* and Alberta Women Entrepreneurs initiative.

The fact that state-owned banks hold a majority of banking assets in the Russian Federation provides a unique opportunity to facilitate an expansion of credit bureau information. By requiring that state-related credit organisations (state-owned banks, MFIs and loan guarantee programmes) pool information with each other through an independent intermediary credit bureau organisation, a considerable store of credit histories could be created that all financial institutions could consult on a fee-paying basis. Over time, and by involving private sector banks, the initial database could be increased, allowing system-wide shared data on the credit histories of individuals and SME borrowers from which lending technologies such as credit scoring could be developed. In the longer term the repository could be devolved to one or more private sector credit bureaus.

Such an initiative would make all participants in the banking marketplace better off: lenders' risk assessments would be improved, allowing them to price to risk; borrowers would gain the ability to pay risk-appropriate interest rates rather than simply being denied credit. The cost of establishment of the repository should be relatively low and the bureau would eventually operate on a sustainable basis. Moreover, independent assessments of loan risk classifications may also enable banks to reduce their reserve requirements and more easily be in compliance with banking regulations. The establishment of credit bureaus has been accomplished in many other countries, and information providers such as D&B and Equifax are examples of private sector firms that operate as credit bureaus.[5] However, it is absolutely essential that credit bureau data must adhere to the highest legal, ethical and moral standards. To the extent that credit bureau data are not free from corruption the exercise would be worthless.

The public development bank: Vnesheconombank and SME Bank

Vnesheconombank

Some governments have created public sector financial institutions, including development banks, to provide financing for economic development. Several such institutions focus primarily on investments in infrastructure (for example, Spain's Instituto de Crédito Oficial), but they may also serve as institutional settings for SME and entrepreneurship finance. In the Russian Federation, the Vnesheconombank (VEB) development bank plays an important role in SME and entrepreneurship financing, largely through its SME Bank subsidiary, as well as supporting infrastructure investment, providing financing and insurance for Russian industrial exports and managing Russian state debts and pension funds and intervening as needed in the economy (as it did during the 2008-2009 debt crisis). Officially known as the State Corporation Bank for Development and Foreign Economic Affairs, the state is its sole shareholder and supports the bank directly by the state budget.

As far back as 1922, VEB was the only bank in the former Soviet Union entrusted with export-import and foreign currency transactions. VEB participated in the "London Club" (1997) and "Paris Club" (1999) restructuring discussions and was appointed in 2002 as the agent responsible for managing the Russian State Pension Fund (with RUB 740 billion in assets as of 2010). In 2008, VEB was mandated to provide anti-crisis assistance for the Russian economy, which included the bailout by acquisition of two Russian Federation commercial banks, Globexbank and Sviaz-bank. Acquired at a cost of RUB 213 billion Globexbank and Sviaz-bank currently operate as subsidiaries of VEB.[6] Profits from the operations of the two rescued institutions are used to repay the cost of the bailout.

Table 6.5 compares VEB with other development banks on key facets of its operation, although its total assets are relatively small. It has a strong record of performance compared with these banks. Its net margin exceeds that of its peer group and it has a return on equity of between 4.1 and 8.4 per cent over the period 2007-12.

Table 6.5. **Salient comparisons of public development banks**

	Russian Federation	China	Germany	Brazil	Japan
Ratings	Baa1/BBB/BBB	Aa3/AA-/A+	Aaa/AAA/AAA	Baa1/BBB-/BBB	AA3/AA-
State support	Implicit	Implicit	Guarantees all obligations	Implicit	Guarantees some obligations
Supervision	Government	State council	Ministry of Finance	Ministry of Economic Development	Ministry of Finance
Total assets (USD billion)	74.7	775.6	520.1	372.5	183.3
Capital adequacy ratio	13.9%	10.9%	17.6%	22.3%	20.4%

Source: Information provided by Vnesheconombank.

SME Bank

The support provided by VEB for SME and entrepreneurship financing is largely channelled through its SME Bank subsidiary. SME Bank, does not engage in direct lending to SMEs; rather, it provides indirect financing to 134 partner banks (mainly regional banks) and 141 non-bank organisations, which in turn make loans to qualifying SMEs. Essentially, SME Bank refinances loans advanced by the partner banks and other organisations by lending to partner banks on relatively attractive terms that then allows the partners to provide financing onwards to SMEs. To do so, SME Bank uses more than 20 credit products to provide capital for lending, leasing, factoring, credit cooperatives and microfinance companies. Table 6.6 illustrates the parameters of a sample of these credit products.

SME Bank has assisted 38 000 SMEs through these programmes. Furthermore, some 62% of the loans based on SME Bank programmes were granted for maturities of over 3 years, which is important given the virtual absence on long term lending available to SMEs in the Russian Federation. The average lending rate was 12.7% in 2013, but for innovation projects the average lending rate was 11.7%.

In July 2013, SME Bank established its own guarantee mechanism to support medium-sized enterprises. Guarantees are extended from the federal budget to VEB, which in turn extends guarantees to SME Bank, which extends guarantees to a pool of banks which provide financing for medium-sized enterprises. Guarantees will cover 50% of the loan amount, up to RUB 1 billion. Terms are for from 2 to 10 years.

Table 6.6. **Sample SME Bank credit products**

Product Name	Loans to partner banks			Partner bank loans to SMEs		
	Form	Term (years)	Rate (% p.a.)	Form	Term (years)	Rate (% p.a.)
Stimulus	Single issue	1-5 years	9.25%	Loan or LOC with limit	6 months to 5 years	14.25% (Maximum)
SMEs - idea[7]	LOC* with limit	< 7 years	6.75%	Loan or LOC with limit	2-7 years	12.25%
SMEs regional growth	LOC with limit	1-3 years	8.25%	Loan or LOC with limit	6 months to 3 years	Maximum margin of 5.5%
SMEs - manoeuvre	LOC with limit	< 7 years	8.00%	Loan or LOC with limit	2-7 years	Maximum margin of 4.5%
FIM	LOC with limit	< 5 years	8.25%	Loan or LOC with limit	1-5 years	< 12.25%
Refinance	Single issue	1-5 years	10.00%	Loan or LOC with limit	6 months to 5 years	Not pre-specified
Microfinance	LOC with limit, < RUB 30 million	1-3 years	9.75%	Loan or LOC with limit; < RUB 10 million	3 months to 3 years	19.5%
Leasing	LOC with limit< RUB 15 million	< 5 years	10.00%	Financial lease; > RUB 150 000; < RUB 150 million; < 80% of value of leased asset(s)	3-5 years	< 18.0%

Note: *LOC: Line of credit.

Source: Information provided by Vnesheconombank.

In addition, VEB has developed various agreements with international partner development banks. For example, VEB and KfW in Germany signed a Memorandum of Understanding in 2012 for the establishment of a National Entrepreneurship Support Fund with the support of the European Investment Fund. Initial funding is USD 300 million, but with a target of USD 900 million. The Fund plans to provide the following financial instruments:

- Direct long term loans to SMEs for 1-3 years denominated in RUB.
- Long term loans to commercial banks for financing of SMEs.
- Subordinated loans granted to banks with a value of RUB 50 million per bank.
- Mezzanine financing and direct investments in SMEs.

There are nonetheless some problems in finalising these agreements because of sanctions from some foreign countries. In addition, sanctions are affecting the refinancing of capital in VEB and SME Bank and the availability of state revenues for onward lending. In this context, even greater attention needs to be paid to getting the maximum impact from the public SME financing available from SME Bank by making an efficient selection of projects and product types and focusing on making domestic private markets work.

Overall, VEB and SME Bank are playing a critical role in helping address the demand for investment capital among SMEs and entrepreneurs. For example, there is evidence that the injection of financial support to SMEs through SME Bank was able to reduce the negative impact of the crisis in terms of access to credit, although it did not result in a statistically significant impact on employment growth in the SME sector (NISSE, 2010). However, even with their interventions a substantial SME finance gap remains. For example, the SME Bank programmes involve less than RUB 100 billion compared with an annual flow of lending to SMEs across the Russian Federation of more than RUB 6 500 billion, even if the market

share of SME Bank is higher in some areas: 12% of microfinancing, 3% of leasing and 5% of factoring. This suggests a need to expand the scale of VEB operations in a number of areas of SME and entrepreneurship financing support.

There is also a need to expand the scope of VEB and SME Bank activities in terms of introducing new products and services. In a recent review of 55 public financial institutions, (OECD 2015c) identifies 37 with financial products for SMEs and entrepreneurs. Table 6.7 summarises the SME and entrepreneurship products that they offered compared with those of VEB and SME Bank. It is evident that although VEB and SME Bank are involved in providing loans, loan guarantees and non-financial assistance such as advice and training to SMEs and financial institutions there are a number of other SME financing activities that they do not undertake that are offered by several other international public financial institutions, including new types of equity, hybrid debt-equity and securitisation products. Finnvera in Finland, described in Box 6.5, is an example of a development bank that is successfully supporting SME and entrepreneurship financing and has a number of features that could provide inspiration for the further development of VEB and SME Bank activities.

Table 6.7. **SME finance products offered by selected public financial institutions**

Institution	Direct				Indirect		
	Soft loans	Debt (loans)	Hybrid debt-equity (subordinated)	Equity	Loan Guarantees	Securitisation	Non-financial assistance (e.g. training)
EBRD	..	✓	..	✓	✓	..	✓
NIB	..	✓	..	..	✓	..	..
EIF	..	✓	..	✓	✓	✓	..
Australia, EFIC	..	✓	..	..	✓	..	..
Austria, AWS	✓	✓	..	✓	✓		✓
Belgium, Fonds Bruxellois de Garantie	..	✓	✓	✓	✓	..	..
Belgium, PMV Flanders	..	✓	✓	✓	✓	..	..
Belgium, SOLWFIN Wallonie	..	..	✓	✓	..	..	..
Brazil, BNDES	..	✓	..	✓	✓	✓	✓
Canada, BDC	..	✓	✓	✓	..	✓	✓
Chile, Banco Estado	..	✓	..	..	..	..	✓
Chile, Corfo	..	✓	..	..	..	..	✓
Colombia, Bancoldex	..	✓	..	✓	..	..	✓
Costa Rica, SBD	..	✓	..	..	✓	..	✓
Czech Republic, CMZRB	✓	✓	✓	..	✓	..	..
Denmark, Vaekstfonden	..	✓	..	✓	✓	..	✓
Estonia, Kredex	✓	✓	..		✓	..	..
Finland, Finnvera		✓	..	✓	✓	..	✓
Germany, KfW Mittelstandsbank	✓	✓	✓	✓	✓	..	✓
Greece, ETEAN	..	..	..	✓	✓	..	..
Hungary, MFB		✓			✓	..	..
Slovak Republic	..	✓	..	..	..	..	..
Hungary, Venture Finance Hungary	..	..	..	✓	..	..	..
Israel, SMB			..	..	✓	..	✓
Italy, MedioCredito Centrale	✓	..	..	..	✓	..	..
Korea, SBC	..	..	..	..	✓	..	✓

Table 6.7. **SME finance products offered by selected public financial institutions** *(cont.)*

Institution	Direct				Indirect		
	Soft loans	Debt (loans)	Hybrid debt-equity (subordinated)	Equity	Loan Guarantees	Securitisation	Non-financial assistance (e.g. training)
Mexico, NAFIN		✓	..	✓	✓	..	..
Netherlands, NL	✓	✓	✓	✓	✓	..	✓
Norway, Innovation Norway	✓	✓	..	✓	✓	..	✓
Peru, Cofide	..	✓	..	..	✓	..	✓
Russian Federation, VEB/ SME Bank	..	✓	..	..	✓	..	✓
Slovak Republic, SZRB	✓	✓	..	..	✓	..	..
Slovenia, SID	✓	✓	✓	✓	✓	..	✓
Spain, ICO	..	✓	..	✓	✓	✓	..
Sweden, ALMI	..	✓	..	✓	..	..	✓
Turkey, TKB	..	✓	..	✓	✓	..	..
United States, SBA	..	✓	..	✓	✓	..	..
Uruguay, BROU	..	✓	..	..	✓	..	✓

Source: OECD (2015c) The Role of Public Financial Institutions in Fostering SMEs Access to Finance. OECD Centre for Entrepreneurship, SMEs and Local Development, Paris.

Box 6.5. **SME and entrepreneurship financing by Finnvera Development Bank, Finland**

The approach

Finnvera is the public development bank of Finland, a state-owned enterprise that provides financial services to satisfy three mandates: to support the development of enterprises, especially SMEs; to promote exports and the internationalisation of enterprises; and to contribute to the achievement of the government's regional policy goals. It aims to offset shortcomings in the supply of financial services by taking higher risks than commercial lenders whilst sharing risks with private financial providers.

Finnvera operates a range of direct business loans programmes including micro loans, loans to women entrepreneurs, loans to support voluntary environmental investments by SMEs, contra-cyclical loans, and loans to support internationalisation. It also operates a variety of loan guarantee programmes. The standard programme offers guarantees of 80% of the credit for loans or bonds granted by banks, finance companies or insurance companies. Another programme guarantees 60% of a micro-loan of up to 85,000 EUR. Finnvera also provides counter-cyclical loan guarantees and acts as Finland's official export credit agency, offering guarantees to banks for export credits.

Veraventure, a Finnvera subsidiary, manages Seed Fund Vera, which makes direct equity investments in enterprises. A company can apply for venture capital financing from Veraventure online. It must be: (1) a small enterprise registered in Finland; (2) organised as a limited company; and, (3) in the process of establishment or at an early stage. The Board of Seed Fund Vera, based on a presentation by the management team, makes decisions as to the approval/rejection of applications. Veraventure also acts as a fund-of-funds by investing in Finnish regional venture capital funds organised as limited companies. Investments take the form of equity. Veraventure also administers a business angel network known as SijoittajaExtra (InvestorExtra) through which early-stage growth enterprises can apply for venture capital financing directly from business angels and through which individual investors can find investment opportunities in growing early-stage enterprises.

Box 6.5. **SME and entrepreneurship financing by Finnvera Development Bank, Finland** *(cont.)*

Results

Finnvera's activity in 2009 involved EUR 593 million in loans, EUR 474 million in guarantees, and EUR 127 million in export guarantees. It provided loans and loan guarantees to 3 457 start-ups and 1 246 growth enterprises and made equity investments in 116 companies. This was associated with the creation of 9 214 new jobs.

Success factors

The success of Finnvera is associated with good governance arrangements. These include regular evaluations of the cost effectiveness of programmes in achieving public investment and ongoing monitoring of capital adequacy and the transparent appointment of a Board of Directors from people nominated by the Ministry of Employment and Economy, the Ministry of Finance and the Ministry for Foreign Affairs.

Problems and responses

The global financial crisis led to problems for SMEs and entrepreneurs to obtain working and investment capital from commercial banks. Accordingly, in 2009, the Finnish Parliament agreed amended legislation on Finnvera to:

- Increase the Government's commitment to compensate Finnvera for credit and guarantee losses from EUR 2.6 to 4.2 billion for domestic financing and from EUR 7.9 to 12.5 billion for export financing.
- Increase the amounts of Finnvera loans and guarantees from EUR 210 million to 860 million and from EUR 10 million to 124 million for counter-cyclical loans and guarantees.
- Increase the shareholders' equity of Seed Fund Vera by EUR 22.5 million and that of Veraventure by EUR 7.5 million.
- Make a subordinated loan of EUR 50 million to keep the capital adequacy of Finnvera at a minimum of 12 percent. Another 30 million EUR was reserved for the same purpose in the State budget for 2010.

The existing skills, experience and infrastructure of Finnvera was critical in enabling the state to intervene rapidly through its public bank in mitigating the effects of the financial crisis on SMEs and entrepreneurs.

Relevance to the Russian Federation

Finnvera has a mandate that is much like that of VEB and SME Bank in the Russian Federation but has a wider range of SME and entrepreneurship financing initiatives. Loan guarantees, export credit and venture capital initiatives such as those operated by Finnvera could be a useful complement to the existing activities of VEB and SME Bank.

Further information

www.finnvera.fi/eng

Source: OECD (2015c) The Role of Public Financial Institutions in Fostering SMEs Access to Finance. OECD Centre for Entrepreneurship, SMEs and Local Development, OECD Publishing, Paris.

Conclusions and recommendations

The most important short to medium-term challenge for SME and entrepreneurship financing in the Russian Federation is to correct a situation in which the proportions of SMEs with access to a bank loan and the volumes of bank loans remain substantially below those in the OECD area and in ECA and Upper Middle Income countries generally, despite recent increases driven by public interventions. The weakness of bank lending in the Russian Federation has led to the emergence of a substantial private sector driven microfinance

market, and to some extent, a reliance of new firms and SMEs on government subsidies such as grants for equipment leasing for their investments. However, these palliatives are not sufficient. The financing amounts available through these means are of small scale, and the microfinance loans are short term and expensive, with interest rates often higher than 25 per cent annually. Increased coverage of bank lending among SMEs together with larger and longer term loans will be needed to cover the working capital needs for the growth and day-to-day operations of SMEs and to finance long-term asset expansion in new and growing firms.

In large part, the current situation can be attributed to a historical context that has left the banking sector largely without the resources of experience, expertise and technologies for SME and entrepreneurship lending. Where bank lenders are unable to assess the risk of potential SME borrowers and make informed decisions about which loans to make and which to reject they are driven to rely on credit rationing. The government can help correct this historic weakness by building the SME lending capacities of banks at the same time as their incentives to lend. One of the most important tools for this purpose is the use of loan guarantees offered to private sector banks and microfinance institutions. This provides both an immediate stimulus to lending and helps build the experience of banks and other financial institutions with SME lending in the longer term. There has recently been an upward trend in guaranteed loans in the Russian Federation stemming from the activities of regional and municipal loan guarantee funds, the introduction of loan guarantees for medium-sized enterprises by VEB and SME Bank and the creation in 2014 of a Federal Credit Guarantee Agency which should double the volumes of loan guarantees in the system by 2016. It will be important in strengthening the loan guarantee system to pay close attention to the design and operation of the national, regional and municipal schemes to secure high levels of additionality of loans and sustainability of loan guarantee schemes, which implies a need for the use of evaluation as well as provision of capacity building support for the local schemes.

A further potential government intervention that could be critical in raising the volume of lending by banks, microfinance institutions and others would involve expanding the availability and use of credit information on SME borrowers for lending decisions. One of the key problems that banks face in lending to SMEs is lack of information on the associated risks. In part, this reflects the fact that SMEs do not have to prepare standardised financial statements (which are not required by the tax system) and because there is not yet an effective credit bureau from which all banks can benefit. While the use of credit scoring is now almost universal in advanced countries as a way of assessing loan demands effectively and cheaply, it is rare in the Russian banking system. This information gap leads banks to be extremely conservative in their lending decisions. Together with a strengthening of the legal system with respect to investor protection, the government could increase lending by pooling credit information on firm and individual borrowers from state-linked credit programmes and sharing this information with other state entities and private banks through an independent intermediary organisation. This could enable banks and microfinance institutions to assess small business lending opportunities more efficiently using credit scoring, which would boost lending amounts and reduce interest rates. It could eventually lead to the establishment of one or more full-fledged credit bureaus drawing on both state and private sector lending information and supported by fees paid for the credit information supplied.

These efforts could be reinforced with a set of measures to build the capabilities of bank staff in SME and entrepreneurship financing and increase financial and business literacy among Russian Federation entrepreneurs. This calls for support of a major training programme in SME lending for bank staff that could be managed through the creation, perhaps through Vnesheconombank, of a centralised institute for banking education, one that includes SME lending as a key focus. The institute would be mandated to provide distance, online, and classroom educational programmes to bank staff and other financial services professionals, such as those involved in MFIs and those managing loan guarantee programmes. It would develop and provide educational materials related to SME banking and would be supported by the banking industry. One approach might be to affiliate such an institute with a university that also offers degrees in business education. At the same time, relatively low levels of financial and business literacy among Russian Federation entrepreneurs makes their businesses more susceptible to poor management decisions, which is a frequent reason for the failure of many SMEs and the risk perceived by prospective lenders. To address this, it will be important to expand efforts to provide entrepreneurship education in the formal education system and to offer business training, advice and counselling to existing SME managers and potential entrepreneurs.

Whilst banks should gradually take over the bulk of SME and entrepreneurship lending from the public and private microfinance sector in the Russian Federation, microfinance institutions will still have their role to play in providing lending for very small amounts. It is therefore important that existing weaknesses in the microfinance sector are addressed. In particular, measures should be envisaged to fill regional gaps in microfinance coverage and encourage some consolidation in the sector to increase the scale of individual institutions. In addition, supervisory changes should be made to assist borrowers to distinguish the very high interest rate lenders from other MFIs and reduce any abuses.

The supply of venture capital and private equity does not appear to be presenting a major problem for the development of high growth potential SMEs and entrepreneurship at this time. Rather the supply of seed and early-stage venture capital and private equity appears to be constrained by a lack of growth-oriented enterprises to invest in, which reflects weaknesses in upstream bank lending and a need to orient the innovation system more towards commercialisation of research. However, it is important to encourage more balance in the size distribution of Russian Federation venture capital funds by encouraging the emergence of a fewer larger funds. There is also scope to boost the emerging business angel financing sector with measures including support for the creation of business angel networks, tax incentives for angel investments and co-investment with angel investors by public organisations such as venture capital funds.

VEB and SME Bank are critical players in the development of a larger and more sophisticated financial market for SME and entrepreneurship financing in the Russian Federation. In particular they can help stimulate a shift in state financial support to SMEs and entrepreneurs from direct grants and loans towards leverage of private sector resources through expanded loan guarantees and new activities in the areas of venture capital and business angel investment. They also have a central role to play in efforts to provide staff in banks, MFIs, loan guarantee funds and other financial institutions with more extensive education in SME finance. They can also play a role in increasing financial literacy on the demand side of the financial market, in particular by helping raise investment readiness

in growth oriented SMEs. In these respects the public development bank could be a key player in the establishment of a new national institute for financial education. It could also be a major player in the development of a national credit information system. For these tasks, the roles of VEB and SME Bank should be interpreted more broadly than in the past in order to complement the supply of credit to the banking system for SME lending with other financial and non-financial products as found in the leading public financial institutions in the world.

The following key recommendations are therefore offered to improve SME and entrepreneurship financing in the Russian Federation:

Key policy recommendations on SME and entrepreneurship financing

- Expand bank lending to SMEs and entrepreneurs and increase the scale and terms of loans made by increasing the leverage of public investments (favouring loan guarantees over direct subsidies to SMEs or lines of credit to banks for onward lending), increasing credit history information in the SME lending market and building an inter-bank SME lending market by encouraging standardisation of loan contracts and implementing legislation to provide for securitisation.
- Promote the sustainability and additionality of the loan guarantee system by using evaluation evidence and information from international experience to set the appropriate design parameters for the national, regional and municipal credit guarantee funds as well as by providing capacity-building support to local funds and encouraging consolidation of smaller funds.
- Develop a national credit information system that enables banks, microfinance institutions and finance providers to assess the riskiness of SME borrowers based on their credit histories and other parameters. Require that all state-supported credit organisations contribute credit information to an intermediate credit information organisation and share the resulting database with private banks and financial institutions on a fee-paying basis.
- Fill outstanding gaps in the regional coverage of microfinance institutions, offer capacity-building support to microfinance institutions in SME lending and introduce new reporting and supervisory measures to help borrowers distinguish between payday lenders and responsible institutions.
- Channel public investments in venture capital towards expanding existing funds rather than creating new funds.
- Boost the business angel sector through measures such as strengthening legal protection for minority shareholders, recognising business angel investment in regulations, supporting the creation of business angel networks, offering tax incentives for angel investments, providing public co-financing for projects with angel investors and offering awareness, training and mentoring support in angel investment to potential angels and high growth enterprises.
- Augment the scale of the SME lending interventions of the public development bank, VEB and its SME Bank subsidiary in the short to medium-term, particularly in encouraging longer-term and larger loans to start-ups and growth-oriented SMEs.
- Expand the remit of the activities of VEB and SME Bank to enable them to introduce new financial products in the area of equity, hybrid debt-equity and securitisation instruments, and new non-financial products, including hosting a national institute for financial education (offering distance, online, and classroom-learning programmes to financial services professionals, such as those involved in banks, credit guarantee programmes, microfinance institutions and venture capital funds), and supporting the development of a national credit information system by advancing the availability of credit rating tools, technologies and data.
- Design all measures to improve the financing system for SMEs and entrepreneurship so as to avoid the possibility of systemic corruption.

Notes

1. For example, the Consultative Group to Assist the Poor reports that "promotional booklets found in post offices in several major Russian cities were advertising microloans in the amounts starting from USD 100 that, if taken for one week, would cost 2772% *per annum* (and a "special offer for low-income pensioners" – at 2598%)." *www.cgap.org/blog/interest-rates-microloans-russia-how-much-too-much;* accessed March 22, 2013).
2. It is important to distinguish between "private equity" and "venture capital". Private equity typically comprises investments in traditional later-stage and established businesses and is seldom of interest to growing SMEs. Venture capital, classically, is investment in early-stage, high-risk ventures with growth potential.
3. Data in this section were extracted from Russian Venture Capital Association (2013). Because data from this source were based on a survey of Russian Federation Venture Capital firms, to which not all firms replied, these data arguably understate private equity and venture capital activity.
4. A few examples of national government run programmes are those of the United States Small Business Administration, the Canada Small Business Financing Program and the United Kingdom Enterprise Finance Guarantee. Finnvera in Finland and BPI in France are examples of schemes run by public development banks.
5. Interfax and D&B established a joint venture in 2008 to operate in Russia and the CIS countries, providing access to the D&B global business database and analytical services for credit risk assessment. However, domestic credit history data from within the Russian Federation needs to be expanded substantially.
6. In addition to Globexbank and Sviaz-bank, VEB also operates subsidiaries Roseximbank (0.39% of total VEB assets), VEB Leasing (6.46% of total VEB assets), VEB Capital (0.34% of total VEB assets), and SME Bank (3.66% of total VEB assets). Two additional subsidiaries, Belvnesheconombank (1.64% of total VEB assets) and Prominvestbank (5.77% of total VEB assets) operate in Belarus and Ukraine, respectively. Recently, EXIAR, the Russian Federation export credit agency began operation with VEB as the sole shareholder.
7. Loans advanced under the terms of the "idea" and "manoeuvre" programmes are targeted to the financing of SMEs for the implementation of innovative projects (idea) and modernization (manoeuvre); "regional growth" loans are targeted to SMEs in regions in which demand for credit is low.

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OECD Studies on SME and Entrepreneurship
Russian Federation

Chapter 7

The Local Dimension of SME and Entrepreneurship Policy in the Russian Federation

This chapter identifies strong spatial variations in SME and entrepreneurship performance across the regions of the Russian Federation together with differences in the scope and nature of constraints in regional business environments. Some regional and municipal governments are active in improving their regulatory conditions for SMEs and entrepreneurship, but the progress is highly uneven across the country. Federal government ministries and agencies also operate some locally-differentiated actions such as in cluster and financing support. However, regional and municipal governments are not as active in SME and entrepreneurship promotion as they could be, reflecting constraints in their budgets and professional capacities for strategy making. This gap needs to be addressed if government objectives for growing the SME economy and achieving more balanced spatial development are to be met. The co-funding arrangements of the federal SME support programmes are critical in helping to secure local interventions and could increase participation further with greater flexibility and dialogue in design and implementation. The federal government also has a role to play in building the strategy-making capacities of regional and municipal governments.

Spatial variations in SME and entrepreneurship activity

Large and growing regional disparities

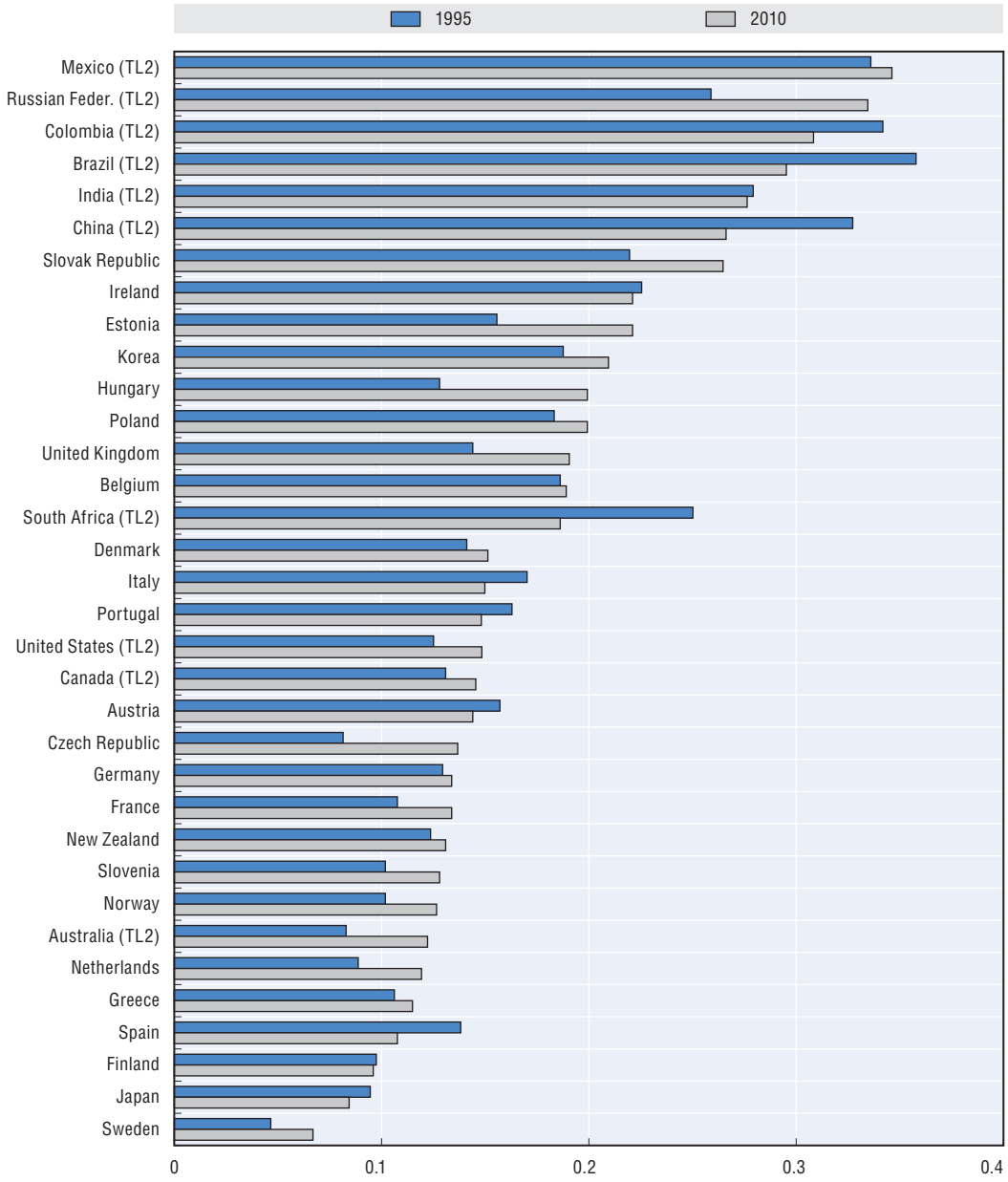
The Russian Federation is a large and varied country in which regional GDP per capita disparities exceed those of most OECD countries and emerging economies and where the regional divide is worsening (Figure 7.1). The disparities affect conditions for the development of SMEs and entrepreneurship in different regions through their impact on factors such as entrepreneurial motivations, potential markets and availability of financing. They are also themselves a reflection of differences in entrepreneurship and SME performance. The main centres with relatively good economic performance include Moscow city and region, Saint Petersburg, the Khanty-Mansiysk Autonomous District, and the Sverdlovsk and Krasnoyarsk regions. Income per capita is highest in Moscow at RUB 730 000 (USD 25 000), more than double the national average (World Bank 2012a). On the other hand, many regions have very low population densities and income per capita, including the North Caucasus, Far East and Urals. Unemployment rates are also very uneven; the unemployment rate in the Moscow region standing at only 3.3% in 2010 compared to 16.9% – twice the national average – in the Caucasus (Farra *et al*. 2013).

Whereas national policy in the Soviet period aimed to achieve a degree of balanced regional development and national growth poles were distributed across the Soviet territory, since the early 1990s the development of regions has become more closely tied to their capabilities in generating private sector business activity. The shift in approach is reflected in a sharp increase in disparities following the demise of the Soviet Union in 1990-92 (Zubarevich 2008) and further increases during shocks such as the financial crisis of 1998 and the global financial crisis of 2008 (Chepurenko *et al*. 2011). The capability of regions to support SMEs and new enterprises will be critical in helping them compete in an increasingly market-oriented and open economy, particularly with the Russian Federation's accession to the World Trade Organisation (World Bank, 2012b; Rutherford and Tarr, 2010).

Lack of SMEs in rural regions

Figure 7.2 shows the substantial differences that exist across the regions of the Russian Federation in numbers of SMEs compared with population size. Whereas the number of SMEs per 10 000 inhabitants was above 400 in St. Petersburg in 2012 and regions including Kalingrad, Yaroslav, Novosibirsk and Moscow had rates of more than 200, more than 20 territories had rates of less than 100 SMEs per 10 000 population. All regions need to increase their SME numbers as part of the national effort to grow the SME economy, but the challenge is particularly important in the regions where the density of SMEs is very low if these economies are to share in and contribute to national growth.

Figure 7.1. **Gini index of GDP per capita across regions in selected countries, 1995 and 2010**



Notes: The Gini index is a measure of inequality among all regions of a given country. It takes on values between 0 and 1, with zero interpreted as no disparity. It assigns equal weight to each region regardless of its size; therefore differences in the values of the index among countries may be partially due to differences in the average size of regions in the country (with smaller regions generally being associated with greater disparities). TL2 corresponds to OECD territorial level 2, which corresponds to large regions. TL3 corresponds to the small OECD territorial level 3 regions.

Source: OECD (2013), Gini index of inequality of GDP per capita across TL3 regions, 1995 and 2010, in OECD Regions at a Glance 2013, OECD Publishing, Paris. DOI: *http://dx.doi.org/10.1787/reg_glance-2013-graph66-en*.

StatLink *http://dx.doi.org/10.1787/888933272087*

There is no clear relationship between the regional density of SMEs and peripherality from economic centres, measured for example by distance from Moscow. However, higher SME densities tend to be found in more urbanised regions while low SME densities are particularly prevalent in rural regions (Figure 7.3). There is also a weak positive correlation between SME density and regional GDP per head (Figure 7.4).

Figure 7.2. **Regional variation in number of SMEs per 10 000 population, Russian Federation**

Note: Figures are missing for the Republic of Ingushetia.

Source: Figures are calculated from Rosstat (2013), SMEs in Russia 2013.

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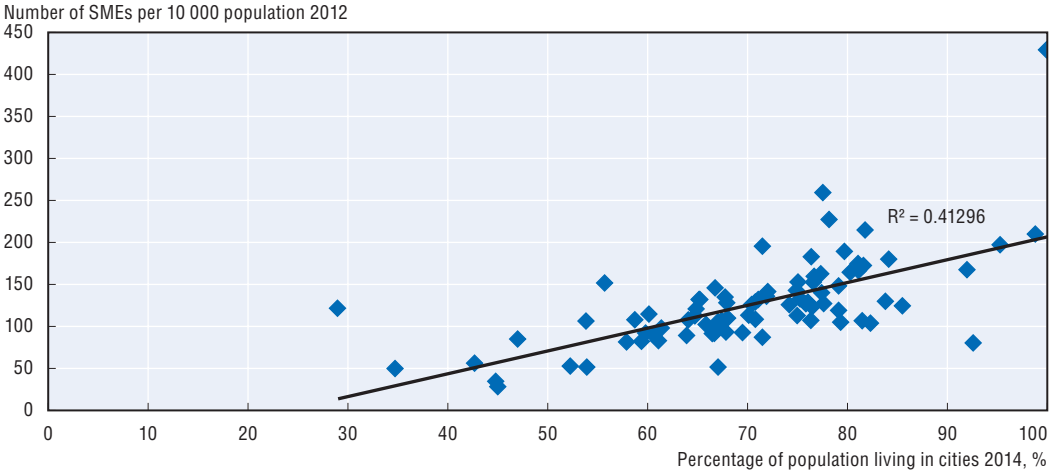
Figure 7.3. **Relationship between regional SME density and population density, Russian Federation, 2012**



Note: Figures are missing for the Republic of Ingushetia.

Source: Rosstat. Figures for SME Density are calculated from Rosstat (2013), SMEs in Russia 2013.

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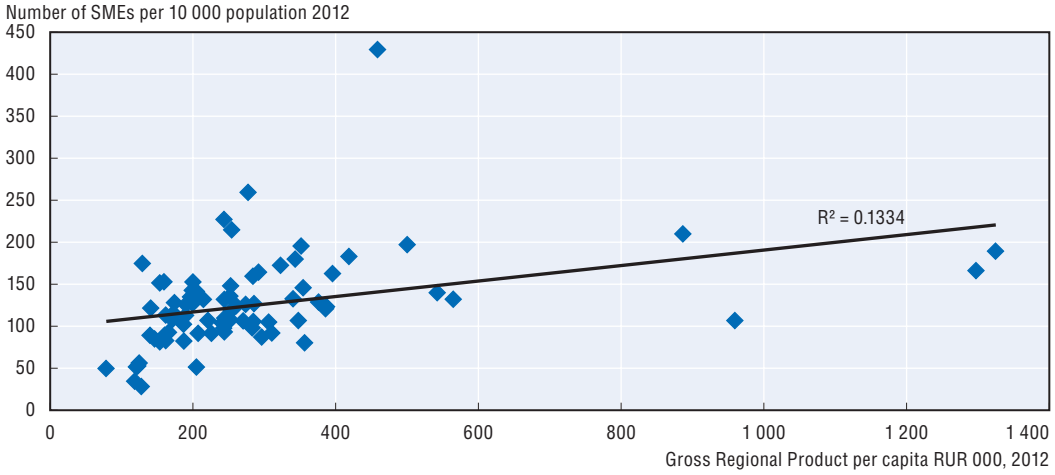
Low business start-up rates in rural regions

These patterns are being exacerbated by a concentration of the recent growth in SME numbers in the larger urban centres (Naumova and Vatolin, 2011), a trend which is confirmed by the data in Figure 7.5, which show that the proportion of people involved in early stage entrepreneurial activity was lower in settlements with less than 100 000 inhabitants than

Figure 7.4. **Relationship between SME density and Gross Regional Product per capita**



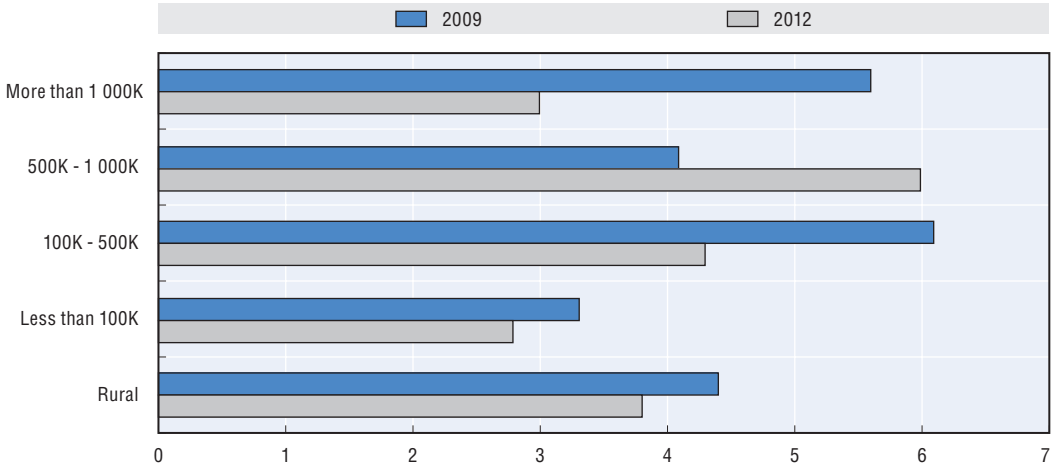
Note: Figures are missing for the Republic of Ingushetia. Figures for the Khanty-Mansiysky Autonomous Area, the Nenetsky Autonomous Area and the Yamalo-Nenetsky Autonomous Area are included in larger territories.

Source: Rosstat. Figures for SME Density are calculated from Rosstat (2013), SMEs in Russia 2013.

StatLink http://dx.doi.org/10.1787/888933272110

Figure 7.5. **Early stage entrepreneurial activity by population size of settlement, 2009 and 2012**

Percentage of adult population involved in early stage entrepreneurial activity



Note: Early stage entrepreneurial activity refers to people who took active steps to open a new business in the previous year or who are owners of new businesses that have been active for less than three and half years.

Source: Verkhovskaia, O. R., and M. V. Dorokhina (2013), National Report Global Entrepreneurship Monitor 2012 Russia, Graduate School of Management, St. Petersburg State University..

StatLink http://dx.doi.org/10.1787/888933272126

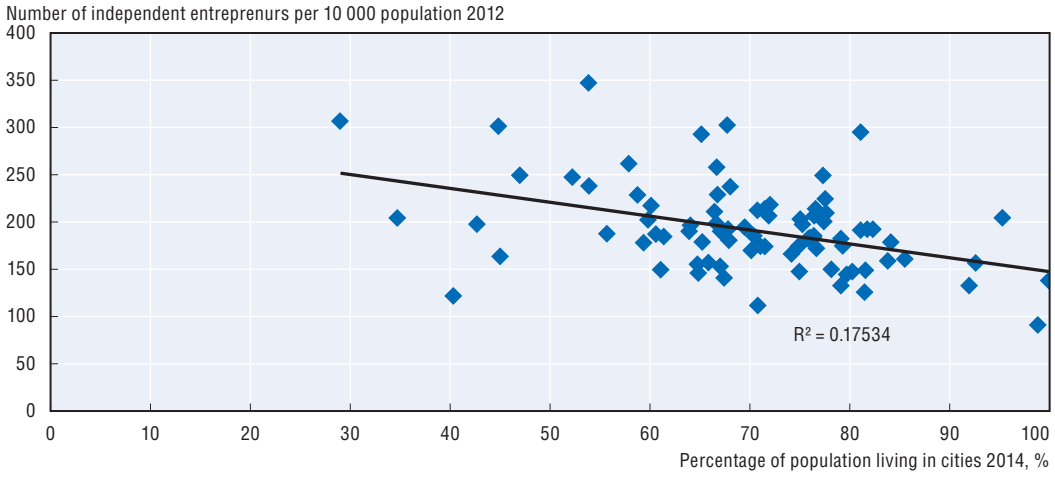
in larger settlements, both in 2009 and 2011 (Verkhovskaia and Dorokhina, 2012). There are also differences in the types of people involved in business creation in urban and rural areas. Early stage entrepreneurs in rural areas are more likely to be male (57% of all early stage entrepreneurs in settlements with less than 100 000 population compared with 47% in cities with more than 1 million inhabitants) and to have low education levels (30% in settlements of less than 100 000 populations compared with 10% in cities with more

than 1 million inhabitants) (Verkhovskaia and Dorokhina, 2012). In the two largest urban centres, Moscow and Saint Petersburg, two-thirds of early stage entrepreneurs have higher educational qualifications, reflecting the geographical concentration of higher education institutions in these urban agglomerations.

High self-employment rates in rural regions

The reverse side of this picture is that people are more likely to be self-employed in rural regions (Figure 7.6). This appears to be related to a lack of alternative employment opportunities. On the other hand, there is no strong link between regional self-employment rates and peripherality or regional GDP per head.

Figure 7.6. **Relationship between self-employment and population density, Russian Federation**



Note: Covers individual entrepreneurship entities which conducted business operations in 2012.

Source: Rosstat. Figures for Self-employment Density are calculated from Rosstat (2013), SMEs in Russia 2013.

StatLink http://dx.doi.org/10.1787/888933272138

Spatial variations in the business environment

Factors in the business environment that support or hinder SME and entrepreneurship development vary significantly across the regions of the Russian Federation. Some light is thrown on these issues by the 2012 World Bank Enterprise Survey, which shows the extent to which businesses surveyed in 37 regions identified major constraints to their operations in the areas of access to finance, skilled workforce, infrastructure, business regulations and taxes, and rule of law. Although there were some important similarities across the regions, in particular tax rates were always the most frequently cited major constraint while infrastructure and regulations were generally seen as less problematic, there were also some significant variations.

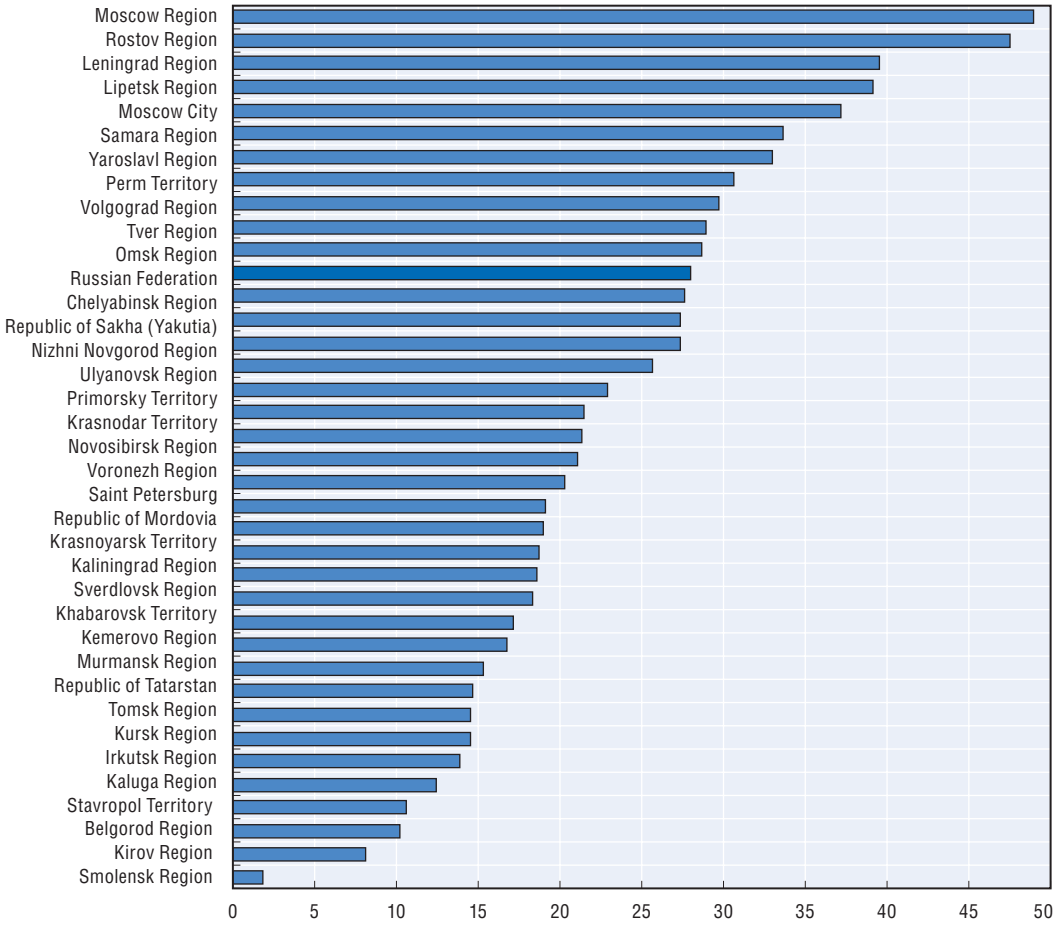
Access to finance

The extent to which access to finance is a major constraint for SMEs and entrepreneurs appears to vary substantially between regions (Figure 7.7). Whereas nearly one-half of enterprises in Moscow Region and Rostov identified access to finance as a major constraint, the corresponding figures in Kirov and Smolensk were less than one in ten. There are three types of regions in which access to finance appears to be a relatively widespread major constraint: major urban centres and their surroundings (e.g. Moscow Region, Moscow City, St Petersburg and Leningrad Region); heavily industrialised regions dominated by a

few large-scale industries (e.g. Lipetsk, Perm, Omsk, Samara, Tver, Volgograd); and more peripheral and rural regions such as Rostov.

Figure 7.7. **Perceived ease of access to finance, selected regions, Russian Federation, 2012**

Percentage of surveyed business owners/managers reporting access to finance as a major constraint



Source: World Bank Enterprise Surveys, Russia 2012 *http://www.enterprisesurveys.org/data/exploreeconomies/2012/russia.*

StatLink *http://dx.doi.org/10.1787/888933272148*

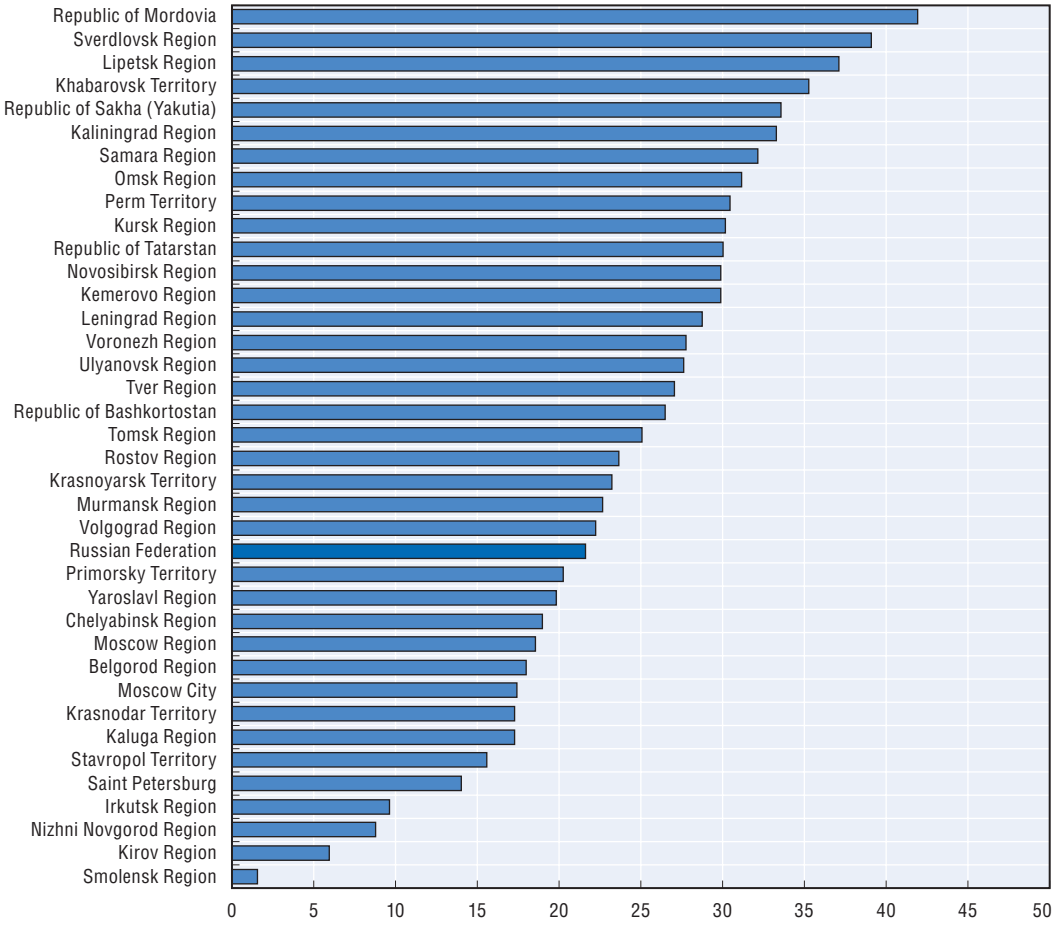
There are also important differences across regions in the extent to which surveyed enterprises actually use external financing (Figure 7.8). The degree of access to bank finance is significantly related to the propensity of firms to report access to finance as a major constraint, but the relationship is not one-to-one, reflecting the fact that enterprises can take various compensating actions to reduce their reliance on bank lending such as drawing on internal finance sources.

Workforce skills

There are also significant spatial variations across the Russian Federation in proportions of enterprises reporting lack of workforce skills to be a major constraint (Figure 7.9). Regions in which relatively large proportions of businesses identified the problem included large urban centres and their surrounding regions such as St. Petersburg and Moscow City, regions with a heavy industry (e.g. Chelyabinsk and Kemerovo) or high technology focus (e.g. Novosibirsk), and peripheral and/or predominantly agricultural regions (e.g. Kirov,

Krasnodar, Rostov). There were also important regional differences in the proportions of enterprises offering formal training to their workers. As shown in Figure 7.10, only 15% of surveyed businesses in Smolensk offered formal training to their employees, as compared with 62% in Tatarstan.

Figure 7.8. **Percentage of firms with a bank loan or line of credit, selected regions, Russian Federation, 2012**



Source: World Bank Enterprise Surveys, Russia 2012 *http://www.enterprisesurveys.org/data/exploreeconomies/2012/russia.*
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Infrastructure constraints

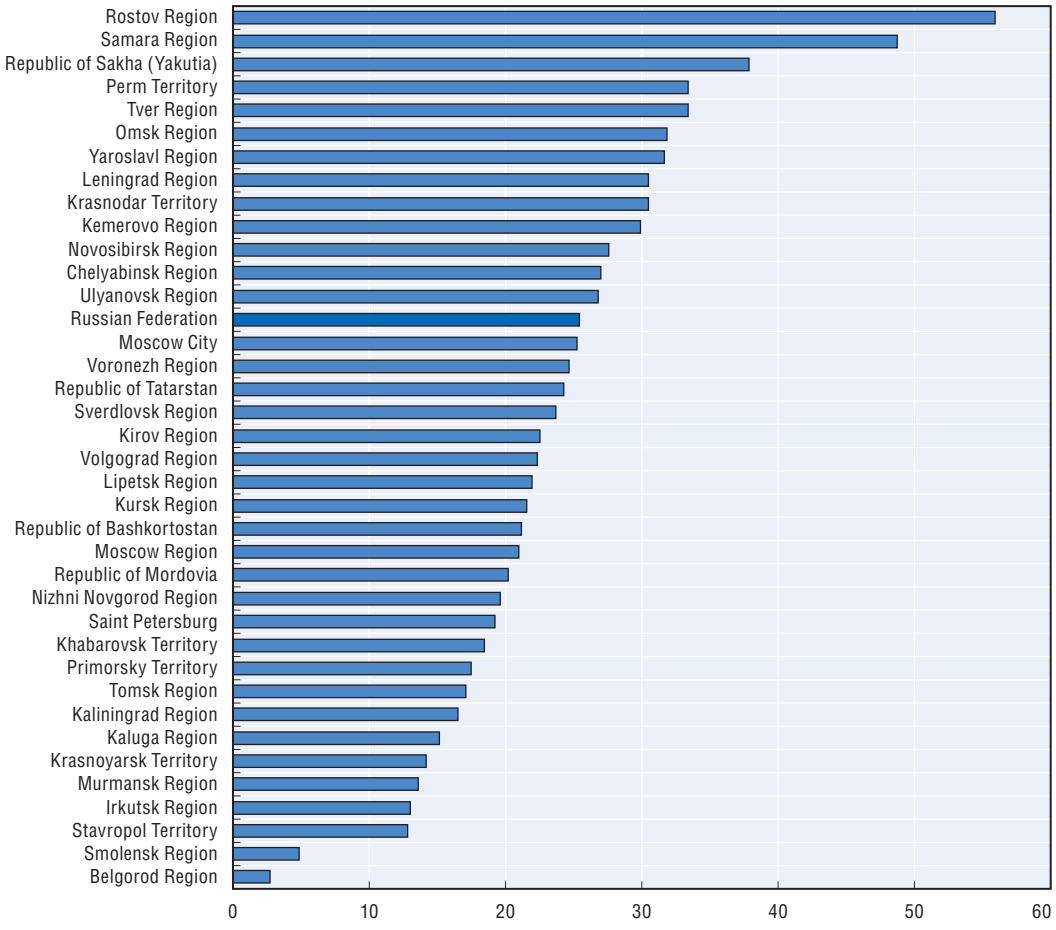
As shown in Table 7.1, gaps in electricity and transportation infrastructure tend to affect greater proportions of enterprises in sparsely populated or peripheral regions, such as the Republic of Sakha in the Far East, Rostov and Stavropol in the far south west and Chelyabinsk in the Ural mountains. This is experienced in various ways, such as electrical outages or the need to own a generator.

Regulations and taxes

Differences in the degree to which tax rates were seen to be a major constraint to business operation are shown in Table 7.2. Whereas tax rates were considered to be a major constraint by more than two-thirds of business owners and managers in Chelyabinsk, Moscow Region, Primorsky, Saint Petersburg, Samara, Stavropol, and

Figure 7.9. **Perceptions of ease of access to workforce skills, selected regions, Russian Federation, 2012**

Percentage of surveyed business owners/managers reporting an inadequately educated workforce as a major constraint



Source: World Bank Enterprise Surveys, Russia 2012 *http://www.enterprisesurveys.org/data/exploreeconomies/2012/russia.*

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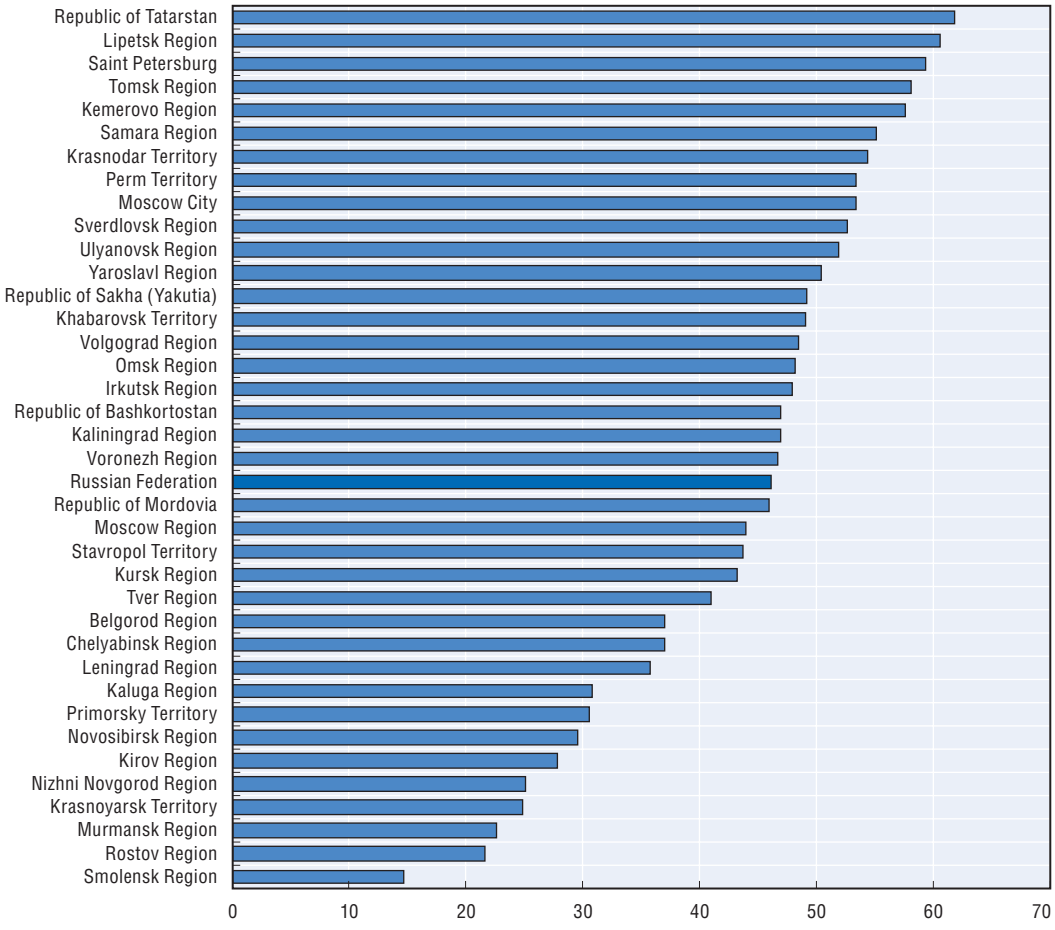
Tomsk, the corresponding proportions were less than one-third in Belgorod and Smolensk. In general, the regulatory framework is perceived to be less of a problem than other business environment conditions in most Russian regions. However, Table 7.2 identifies some exceptions: more than one-quarter of surveyed firms identified major constraints with respect to tax administration in Chelyabinsk, Rostov and Samara, with respect to business licensing and permits in Leningrad, Sakha and Rostov, with respect to customs and trade regulations in Kaliningrad (reflecting its enclave status between two EU Member States), Moscow City and the Republic of Sakha (Yakutia), and with labour regulations in Rostov.

Further light is thrown on these issues by the 2012 Doing Business report on the Russian Federation (World Bank, 2012a), which ranks 30 cities on the ease of doing business in four areas of local business jurisdiction and regulation (Table 7.3). This shows that it is not the largest cities such as Moscow, Novosibirsk or St. Petersburg which have established the simplest regulatory environment for businesses, but smaller cities such as Ulyanovsk, Saransk and Vladikavkaz where collaboration between local support agencies and municipalities may be easier to achieve.

Figure 7.10. **Percentage of firms offering formal training, selected regions, Russian Federation, 2012**



Source: World Bank Enterprise Surveys, Russia 2012 *http://www.enterprisesurveys.org/data/exploreeconomies/2012/russia.*
StatLink *http://dx.doi.org/10.1787/888933272175*

Table 7.1. **Perceptions of infrastructure constraints, selected regions, 2012**
Percentage of surveyed business owners/managers reporting selected infrastructure as a major constraint

	Electricity	Transportation
Russian Federation average	23.1	19.0
Belgorod Region	6.3	2.5
Chelyabinsk Region	37.2	25.1
Irkutsk Region	13.9	14.9
Kaliningrad Region	22.7	16.8
Kaluga Region	16.4	20.2
Kemerovo Region	14.0	15.2
Khabarovsk Territory	32.8	27.7
Kirov Region	23.2	15.6
Krasnodar Territory	24.9	24.5
Krasnoyarsk Territory	23.2	15.5
Kursk Region	23.4	17.7
Leningrad Region	30.4	39.0
Lipetsk Region	39.0	23.4
Moscow City	23.5	19.6
Moscow Region	16.8	25.7

Table 7.1. **Perceptions of infrastructure constraints, selected regions, 2012** *(cont.)*

	Electricity	Transportation
Murmansk Region	19.0	16.4
Nizhni Novgorod Region	10.8	13.3
Novosibirsk Region	14.0	8.2
Omsk Region	25.7	24.4
Perm Territory	30.4	25.6
Primorsky Territory	17.8	13.4
Republic of Bashkortostan	7.7	5.3
Republic of Mordovia	21.6	13.6
Republic of Sakha (Yakutia)	42.1	39.5
Republic of Tatarstan	28.7	17.3
Rostov Region	54.4	42.6
Saint Petersburg	20.1	9.9
Samara Region	24.3	24.6
Smolensk Region	1.7	0.0
Stavropol Territory	38.0	3.9
Sverdlovsk Region	25.4	28.0
Tomsk Region	9.6	12.3
Tver Region	20.6	16.9
Ulyanovsk Region	25.1	22.8
Volgograd Region	18.2	15.6
Voronezh Region	34.6	29.0
Yaroslavl Region	21.3	20.7

Source: World Bank Enterprise Surveys, Russia 2012 *http://www.enterprisesurveys.org/data/exploreeconomies/2012/russia.*
StatLink *http://dx.doi.org/10.1787/888933272355*

Table 7.2. **Perceptions of constraints in business regulations and taxes, selected regions, 2012**

Percentage of surveyed business owners/managers reporting selected regulations or taxes as a major constraint

	Tax rates	Tax administration	Business licensing and permits	Customs and trade regulations	Labour regulations
Russian Federation average	59.1	14.2	15.6	16.0	6.0
Belgorod Region	28.4	2.8	0.3	2.9	2.2
Chelyabinsk Region	69.5	30.0	8.1	15.1	1.3
Irkutsk Region	39.4	5.4	9.3	1.3	5.9
Kaliningrad Region	36.9	10.2	16.1	29.7	4.1
Kaluga Region	66.3	10.9	19.2	7.9	10.2
Kemerovo Region	62.4	16.5	8.7	6.0	7.3
Khabarovsk Territory	58.0	6.0	20.3	18.6	5.5
Kirov Region	46.2	16.9	5.7	0.5	7.6
Krasnodar Territory	47.5	20.7	14.8	14.2	9.3
Krasnoyarsk Territory	60.8	5.2	18.4	5.5	0.6
Kursk Region	57.7	16.7	16.8	10.2	0.7
Leningrad Region	64.3	7.8	30.1	18.5	2.2
Lipetsk Region	57.3	19.7	16.8	2.4	4.4
Moscow City	55.5	16.5	15.5	31.4	4.6
Moscow Region	74.3	11.2	9.8	21.5	5.5
Murmansk Region	43.8	12.9	16.9	6.8	2.9
Nizhni Novgorod Region	63.1	10.6	16.0	6.3	4.1
Novosibirsk Region	66.5	5.7	5.5	6.4	6.1
Omsk Region	62.4	8.1	14.4	3.0	3.4
Perm Territory	49.8	7.8	17.6	14.7	4.7
Primorsky Territory	73.3	9.4	21.6	21.3	2.8
Republic of Bashkortostan	56.9	5.9	9.0	5.6	3.1

Table 7.2. **Perceptions of constraints in business regulations and taxes, selected regions, 2012** *(cont.)*

	Tax rates	Tax administration	Business licensing and permits	Customs and trade regulations	Labour regulations
Republic of Mordovia	54.8	6.2	11.1	6.2	2.1
Republic of Sakha (Yakutia)	56.3	9.0	30.4	13.5	7.4
Republic of Tatarstan	59.2	15.3	15.8	7.7	3.6
Rostov Region	61.9	49.3	38.6	20.3	40.3
Saint Petersburg	69.2	5.9	23.5	11.0	5.4
Samara Region	74.0	26.6	22.5	33.3	5.7
Smolensk Region	12.7	0.0	6.4	0.0	0.0
Stavropol Territory	72.4	6.3	4.5	4.9	0.4
Sverdlovsk Region	62.2	13.2	18.5	17.7	1.2
Tomsk Region	67.2	17.5	13.6	9.2	4.8
Tver Region	52.2	19.8	23.3	5.5	0.6
Ulyanovsk Region	63.4	9.9	18.2	18.9	4.5
Volgograd Region	45.4	12.3	17.4	5.0	5.1
Voronezh Region	54.0	9.5	12.2	7.5	10.6
Yaroslavl Region	65.2	7.4	14.0	5.8	2.4

Source: World Bank Enterprise Surveys, Russia 2012 *http://www.enterprisesurveys.org/data/exploreeconomies/2012/russia.*

StatLink *http://dx.doi.org/10.1787/888933272364*

Table 7.3. **Ease of doing business in selected Russian Federation cities, 2012**

City	Region	Aggregate Rank	Starting a business	Construction permits	Getting electricity	Registering property
Ulyanovsk	Ulyanovsk Oblast	1	3	4	5	8
Saransk	Republic of Mordovia	2	20	8	1	8
Vladikavkaz	Republic of North Ossetia-Alania	3	27	11	2	2
Rostov-on-Don	Rostov Oblast	4	26	15	3	4
Kazan	Republic of Tatarstan	5	4	14	17	4
Kaluga	Kaluga Oblast	6	17	9	15	1
Stavropol	Stavropol Kray	7	4	2	9	19
Yaroslavl	Yaroslavl Oblast	8	7	17	6	16
Surgut	Khanty-Mansiisk Autonomous Okrug-Yugra	9	30	1	19	8
Irkutsk	Irkutsk Oblast	10	8	6	10	18
Petrozavodsk	Republic of Karelia	11	6	16	21	8
Kirov	Kirov Oblast	12	13	5	4	20
Omsk	Omsk Oblast	13	19	20	13	4
Vyborg	Leningrad Oblast	14	10	23	12	8
Vladivostok	Primorsky Kray	15	18	22	23	3
Volgograd	Volgograd Oblast	16	2	27	26	4
Voronezh	Voronezh Oblast	17	15	28	16	8
Tver	Tver Oblast	18	21	25	14	8
Kaliningrad	Kaliningrad Oblast	19	11	3	22	22
Tomsk	Tomsk Oblast	20	15	6	10	25
Samara	Samara Oblast	21	22	24	28	8
St. Petersburg	St. Petersburg	22	1	9	24	27
Khabarovsk	Khabarovsk Kray	23	24	29	8	17
Yekaterinburg	Serdlovsk Oblast	24	29	13	19	20
Perm	Perm Kray	25	13	12	18	27
Murmansk	Murmansk Oblast	26	12	19	27	23
Kemerovo	Kemerovo Oblast	27	28	21	7	29
Yakutsk	Republic of Sakha-Yakutia	28	8	26	25	30
Novosibirsk	Novosibirsk Oblast	29	23	18	29	24
Moscow	Moscow	30	25	30	30	26

Source: World Bank (2012), *www.doingbusiness.org/reports/subnational-reports/russia.*

StatLink *http://dx.doi.org/10.1787/888933272370*

Rule of law

Table 7.4 illustrates some pronounced regional differences in perceptions of the rule of law across the Russian Federation. In particular, the proportion reporting corruption as a major constraint was relatively high in Leningrad, Moscow City, Omsk, Rostov, Saint Petersburg, Samara, and Volgograd. In addition, more than one-quarter of business owners and managers reported major constraints with respect to the court system in Rostov Region, with respect to crime, theft and disorder in Leningrad, Rostov and Tver and with respect to informality in Belgorod, Chelyabinsk, Primorsky, and Samara.

Table 7.4. **Perceptions of business constraints in rule of law, selected regions, 2012**

Percentage of surveyed business owners/managers reporting selected aspects of rule of law as a major constraint

	Corruption	Courts system	Crime, theft and disorder	Informality
Russian Federation	33.1	7.4	12.4	14.2
Belgorod Region	17.6	0.0	2.6	30.2
Chelyabinsk Region	26.4	6.9	21.5	32.3
Irkutsk Region	10.8	6.3	14.9	12.1
Kaliningrad Region	27.4	6.5	10.1	8.4
Kaluga Region	26.9	11.8	9.0	7.9
Kemerovo Region	27.8	12.6	9.5	12.7
Khabarovsk Territory	18.7	7.0	10.5	8.6
Kirov Region	10.6	5.9	12.4	2.2
Krasnodar Territory	24.0	6.6	7.7	22.6
Krasnoyarsk Territory	18.0	2.1	4.0	14.2
Kursk Region	28.6	4.2	13.0	9.9
Leningrad Region	40.7	11.1	26.4	6.9
Lipetsk Region	22.4	12.5	19.5	9.9
Moscow City	45.4	6.6	11.8	10.2
Moscow Region	30.9	4.9	15.0	17.1
Murmansk Region	17.7	6.2	13.9	19.5
Nizhni Novgorod Region	22.4	3.2	2.6	17.8
Novosibirsk Region	26.3	2.6	5.9	2.9
Omsk Region	37.8	3.5	14.6	15.2
Perm Territory	24.1	7.2	18.2	16.5
Primorsky Territory	23.0	11.4	9.7	34.4
Republic of Bashkortostan	19.9	4.4	8.5	10.3
Republic of Mordovia	15.2	2.6	5.5	10.1
Republic of Sakha (Yakutia)	18.1	8.4	18.5	16.4
Republic of Tatarstan	23.6	7.4	15.2	15.0
Rostov Region	52.8	38.5	37.5	17.2
Saint Petersburg	51.0	4.4	6.9	18.6
Samara Region	39.0	11.3	23.5	26.6
Smolensk Region	0.0	4.4	0.0	0.0
Stavropol Territory	23.2	0.7	4.7	3.5
Sverdlovsk Region	25.7	4.3	15.4	14.4
Tomsk Region	23.1	6.0	7.4	13.1
Tver Region	30.9	7.2	25.4	23.1
Ulyanovsk Region	26.3	7.5	6.5	23.3
Volgograd Region	33.8	5.0	4.2	10.0
Voronezh Region	20.6	10.0	10.3	11.1
Yaroslavl Region	27.1	10.1	13.8	20.2

Source: World Bank Enterprise Surveys, Russia 2012 *http://www.enterprisesurveys.org/data/exploreeconomies/2012/russia.*

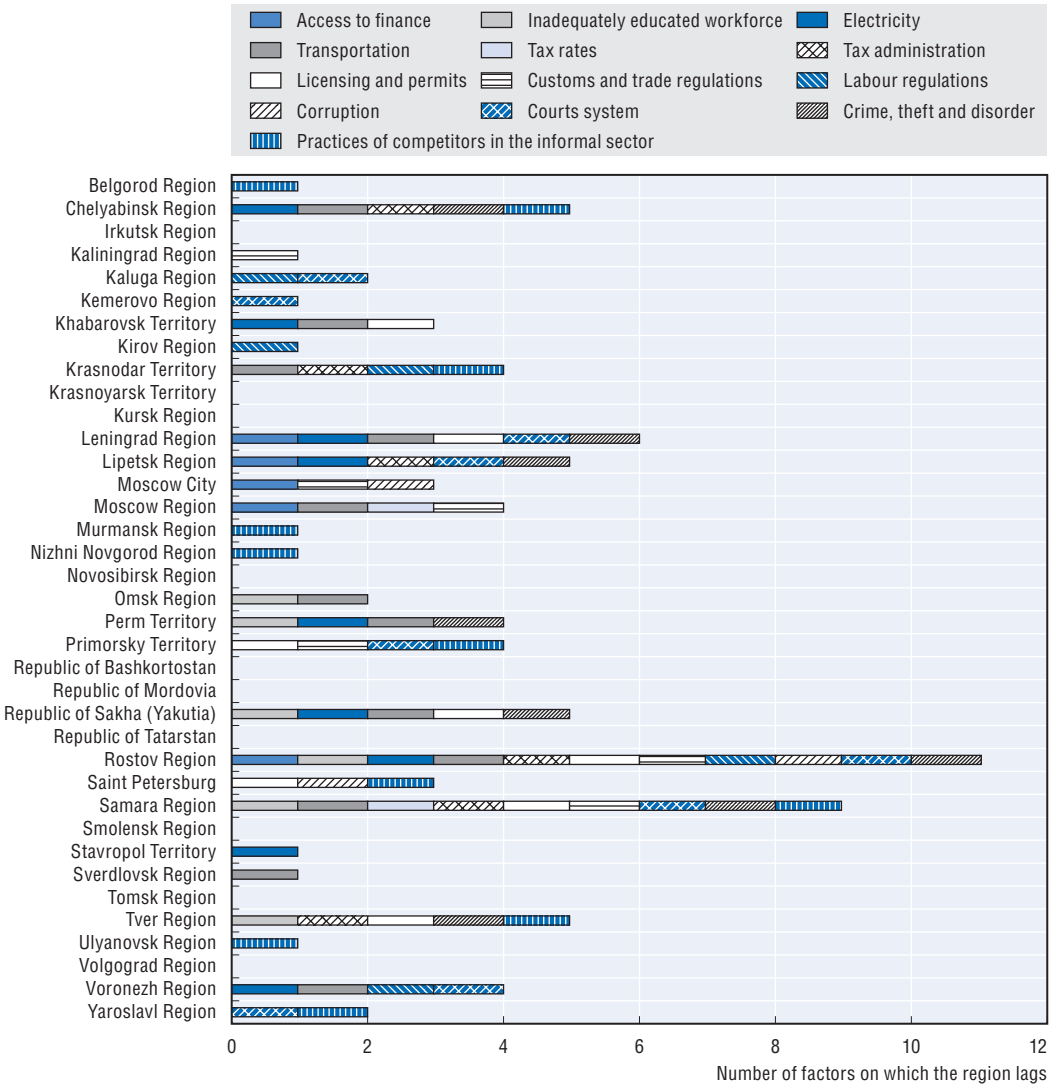
StatLink *http://dx.doi.org/10.1787/888933272381*

Differences in the scope of business environment deficiencies

Figure 7.11 shows the number of categories of business environment conditions for which the percentage of surveyed enterprises in the World Bank Enterprise Survey identifying a major constraint was at least 25% above the Russian Federation average. This illustrates two points. First, there are certain regions, in which businesses report major constraints on several business environment conditions, such as Rostov, Samara, Leningrad, Chelyabinsk, Lipetz and Tver. Second, the specific business environment conditions that present particular problems vary significantly across regions.

Figure 7.11. **Regions lagging behind in framework conditions, selected regions, Russian Federation**

2012



Note: Regions are classified as lagging behind where the percentage of firms identifying the specific framework condition as a major problem is more than 25% above the national average.

Source: Calculated from World Bank Enterprise Surveys, Russia 2012 *http://www.enterprisesurveys.org/data/exploreeconomies/2012/russia*.

StatLink http://dx.doi.org/10.1787/888933272188

Local regulations and rule of law

Local regulations

One of the priorities for strengthening SME and entrepreneurship activity in the Russian Federation involves reducing the burden of business regulations and increasing understanding and application of the rule of law. While much can be done at federal level, regions and municipalities have their own levels of administration and legal competences. In the area of business taxation, the regional influence is mainly related to the way in which federal regulations are implemented and enforced. However, regions and municipalities have stronger influence in other domains. Thus Article 72 of the federal constitution gives joint jurisdiction to the federal and regional levels on regulatory matters related to the possession, use and disposal of land and natural resources and delimitation of state property and full authority to the regions for regulations outside of these areas. Similarly, Article 130 gives limited devolution of powers to municipalities on issues of local importance, including use and disposal of municipal property. It is therefore important that regulations are simple and transparent at local as well as national level in order to remove burdens on business development and minimise the spread of corruption.

A number of regions and municipalities in the Russian Federation have taken steps to improve their regulatory frameworks; often in cases where there has been a political lead from a "reform champion" such as a governor, deputy governor, minister or mayor (World Bank 2012a: 5). For example, various regional and municipal authorities within the Russian Federation have sought to reduce the administrative costs of start-up of formal businesses. Steps that have been taken include reducing the fees which banks, notaries and seal makers can charge businesses to complete start-up requirements and the use of new tax legislation introduced in December 2014 that allows regional authorities to give new entrepreneurs a "tax holiday" (effectively a zero rate of tax), which will also indirectly assist in reducing the cost of start-up. Chelyabinsk Region was the first to enact this legislation.

Another area of improvement involves simplification of local regulations. For example, Saratov Chamber of Commerce in association with the Centre for International Private Enterprise (CIPE) has developed a system for analysing regulatory procedures in order to identify areas of lack of clarity and transparency that give rise to opportunities for corruption. The process has been used to work on improving a diverse set of regulations in various regions, for example leasing forests (Perm Region), licensing education activity (Kirov Region), privatisation of municipal assets (city of Novorossiisk), operation of lotteries (Smolensk Region) and granting construction permits (Khabarovsk Region) (CIPE, 2010). Typical regulatory improvements that have resulted from this exercise include specifying maximum times to be taken for procedural steps, making more information available to businesses, and using independent sources of advice on valuations and technical issues.

Simplification has also been occurring through the introduction of single windows for business interaction with regional and municipal governments, through which all basic services to businesses are delivered from the same office. For example, a single window decree in Krasnodar Region regarding land transactions resulted in the time taken to review documents being reduced from 6-24 months to 2-6 months, even though the procedures remained the same. In Khabarovsk, a single-window procedure for small

business registration reduced the time for registration procedures from 30 to 7-15 days. In addition, a number of regional and municipal administrations have been proactive in disseminating information on the federal government's on-line business registration platform and helping entrepreneurs to make use of it.

Another positive development has been the introduction across the country of regional business ombudsmen, who can advocate for businesses as a countervailing power against arbitrary decisions at a regional and municipal level (CIPE, 2008). This should provide a significant focus for change and transparency in regulations and rule of law at local level.

These types of approaches could usefully be extended to other regions and other areas of regulation. The federal government should maintain the momentum by supporting the inter-regional exchange of information and experience in local regulatory improvements. A declaration of best practice in implementation of local regulation would also be helpful. Box 7.1 gives an example used at federal level in Canada, which could be adapted to the regional and local level.

Local public procurement

There is increasing international recognition that public procurement can be used as a policy lever for SME and entrepreneurship promotion at the same time as achieving value for money in the supply of goods and services to the public sector, as long as satisfactory changes are made to public procurement systems in order to reduce barriers to the participation of new and small firms, such as high fixed cost administrative burdens, lack of transparency, large contract sizes and a bias towards selection of established large firm suppliers.

In the Russian Federation these issues are being addressed by a federal law of April 2013, which introduced new requirements for regional and municipal governments in procurement contracts. As a result, SMEs and entrepreneurs are likely to benefit from new methods for identifying potential suppliers, including tenders with qualified participation, two-stage tenders, calls for proposals and the relocation of public auctions to an electronic platform. They should also benefit from the allocation of a minimum quota for SMEs in regional and municipal government procurement. In particular, under the new legislative framework, the price offered by a bidder will no longer necessarily be the most important criterion in the assessment of tenders and selection of the successful bidder. This opens up the possibility for proactive regional and municipal governments to stimulate economic development by specifying additional selection criteria designed to favour SME and entrepreneurship development.

However, more needs to be done to ensure that procurement law is implemented transparently and effectively at regional and municipal level. An analysis of procurement activities in 2012 by the National Association of Procurement Institutions showed a significant number of distortions in public announcements of tenders, designed to hide information (NAPI et al, 2013), while a meeting of the regional business ombudsmen in December 2014 identified problems relating to the fact that the procurement law is interpreted and implemented differently in each region.[1] Further standardisation of procedures and training of officials would help to promote best practice public procurement methods at regional and municipal levels. In addition, actions may need to be taken to

build the capacities of local SMEs and entrepreneurs to consider and win public sector contracts, such as improvement of skills, business strategies and physical capital as well as sharing good practice information among successful contractors.

Box 7.1. **Directive on Regulatory Management, Canada**

The approach

The Canadian government has produced a Directive on Regulatory Management at federal level, which lays out principles of good regulation and a set of procedures that must be adhered to by all federal departments and agencies. The aim is to ensure that new and existing regulations not only protect the public interest but are also efficient and effective, based on evidence, and promote a fair and competitive market economy. The Directive includes an undertaking to monitor and control the administrative burden, create accessible understandable and responsive legislation, and ensure timeliness, policy coherence and minimal duplication. The Directive applies to all aspects of regulation including both planning and implementation.

Specific provisions include:

- A commitment to Regulatory Impact Analysis, including consultation with stakeholders, setting clear objectives and outcomes, analysing the costs and benefits, cooperation with provincial and territorial governments, and planning for implementation.
- Introduction of regulatory management including a "one for one" rule (any increase in the administrative burden should be compensated by removing other regulation); applying a "small business lens" to new regulations; and forward planning – all departments and agencies should provide advance public notice of regulatory changes, at least on an annual basis.
- Clear roles and responsibilities for different federal institutions.

Results

The Directive provides a clear structure for the development of new regulations by federal departments and agencies. This is expected to reduce the burden of regulations on SME and entrepreneurship development. It also forms a framework for good practice among the Canadian provinces and territories even where it is not binding on their activities.

Success factors

The framework includes a checklist for officials and institutions on what needs to be considered in developing new regulations, emphasising the need to keep the administrative burden as low as possible while achieving policy objectives.

Problems and responses

The framework focuses on those elements of regulation that are under federal government control and are not binding on local regulations. However, regulatory organisations at local level are encouraged to consult the principles of good practice that the Directive sets out.

Relevance for the Russian Federation

A federal directive of this nature in the Russian Federation could set out principles for regulation to be applied at regional and municipal levels. This would reassure SMEs that their voice is heard, that the regulatory burden is kept limited, that regulation is applied in a uniform manner, and that there is adequate notice of new regulations.

Further information

The full text of the Directive is at *http://www.tbs-sct.gc.ca/rtrap-parfa/cdrm-dcgr/cdrm-dcgr01-eng.asp*.

Source: Information from government of Canada.

Local tailoring of SME and entrepreneurship programmes

The institutional role of regional and municipal governments

The important spatial differences within the Russian Federation in the level and nature of SME and entrepreneurship activity and the constraints posed by the business environment signal the need for a locally-differentiated component within state SME and entrepreneurship programmes. The purpose of such locally-differentiated actions is to address certain locally-specific bottlenecks, stimulate the most appropriate kinds of SME and entrepreneurship activity given local capabilities (e.g. encourage upgrading from necessity to opportunity entrepreneurship and increase the productivity of SMEs in weaker regions while promoting innovation and supplier chain connections in stronger regions), and respond to local sector specialisations. Two main approaches to local tailoring can be employed. First, federal government and federal agencies such as the public development bank can design and implement locally-differentiated programmes that vary in their targets and approaches across the country or that are limited to certain places. Second, regional and municipal governments can design and implement their own local programmes, on their sole initiative or in conjunction with the federal authorities, given the powers and responsibilities assigned to them by the federal SME Act of 2007 and the Russian Federation constitution (economic development is neither a federally-reserved nor a shared competence, hence providing the local level with autonomy to act).

Both of these models are to be found in the Russian Federation, and are described below for a range of programme intervention areas together with their limitations and potential steps forward. Overall, neither approach is yet strongly developed. At federal level, there are a few examples of locally-specific initiatives, in particular the federal government's innovative clusters policy and access to finance programmes operated by the public development bank, VEB. However, the number of policy areas involved is limited. At sub-national level, regional and municipal governments commonly design and implement their own programme actions in conjunction with the federal SME support programme. However, there is uneven provision of SME programmes and support services across the country and less than full participation by regional authorities in the federal SME support programme.

Key areas of local programme tailoring

Finance programmes

To date there has been only limited tailoring to differing local conditions of access to financing initiatives for SMEs and entrepreneurs. The majority of regional government intervention has involved the offer of state guarantees for SME lending to regional banks and regional offices of national banks with the aim of increasing lending amounts and reducing the interest rates charged. Alongside this, most of the rest of the financial infrastructure created by regional governments has been focused on the regional co-financing of financial initiatives designed by federal government in which federal guidelines for financial products are tight, allowing regional governments little flexibility to adapt the programmes to specific regional needs. One such example concerns microcredits. Although many regions offer microcredits as part of the programme portfolio of their regional funds, they are restricted by federal rules as regards the upper level of what constitutes a microcredit, which is set to RUB 1 million by federal law.

At the same time, public development banks are starting to play an important role in adapting public SME and entrepreneurship financing measures to regional conditions in two ways. First, they are working to increase the scale of external finance supply in regions with the largest financing gap. For example, Vnesheconombank (VEB) is working with non-financial organisations to offer services to SMEs and entrepreneurs in regions where banks have relatively limited reach. Similarly, Sberbank (which has majority public ownership) is one of the few banks to have opened offices for SME lending in weaker regions. Second, they are helping to adapt the mix of the public financing offer to the needs of different regions. In this respect, VEB has established framework agreements for collaborative SME and entrepreneurship financing initiatives with fifty regional governments using shared information about regional conditions and priorities to identify appropriate financing projects and partners for each region. It has developed a programme with Novosibirsk region, for example, to finance small businesses in science and technology activities, as prioritised by the regional strategy and has established joint programmes with several agricultural regions to finance new farmers and diversify farm activities into tourism, trade and services activities. Another positive development in a few regions has been the establishment of regional public banks in a way that is integrated with their overall SME and entrepreneurship development strategies (see Box 7.2).

Box 7.2. **ELITA bank, Kaluga region, Russian Federation**

ELITA Bank is a regional public bank set up by the government of Kaluga region, which has been offering banking services for more than 20 years. Its priority target groups are SMEs. The bank has developed a portfolio of special credit products and offers preferential conditions to small businesses. Credits are offered for terms of up to 5 years. The bank cooperates with the Regional Fund for Entrepreneurship Support, in particular the regional loan guarantee fund, and is a partner of the national SME Bank. ELITA Bank illustrates a method through which regional governments can improve financial services within their regions.

Source: Information supplied by regional government of Kaluga.

One of the aims of these initiatives is to develop more sophisticated financial markets including a wider range of financing instruments in those regions with the most developed and differentiated SME bases, particularly in terms of the volume of innovative enterprises. For example, Sberbank has introduced one-stop business support agencies to provide financial education for SME managers and entrepreneurs in the more developed regions of Tula and Kaluga to increase the sophistication of finance demand. Similarly, public initiatives to stimulate venture capital and business angel financing are concentrated in 22 dynamic regional economies, often linked to innovation infrastructure such as technoparks. In Kaluga, for example, in 2011, the government supported innovative entrepreneurs to establish the Kaluga Regional Association of Business Angels.

Despite these promising initiatives, regionally-differentiated finance programmes remain too rare. At the federal level, the government could encourage more regionally-tailored initiatives by increasing the degree to which financial programmes that are co-funded by federal budgets allow for regional variation. For example, the federal law on microcredits could be reviewed to allow regional variations in the value of micro credits that can be offered per firm. This could be based, for example, on the relative development of the credit structure in regions, with micro credit of larger amounts being permitted

where banks are not yet able to fill the gap for larger amounts. At regional level, there may be scope to develop additional financial products for nascent and start-up enterprises in collaboration with public development banks and commercial banks, which will be the main financing partner for new firms in the longer run. Regional governments could also expand their efforts to foster the development of equity capital for innovative businesses in regions where a strong innovative SME sector is emerging, including through the support of venture capital initiatives (see the example of a regional fund in Germany in Box 7.3) and the support of regional networks of business angels.

Box 7.3. **Siegerlandfonds: a regional venture capital fund, Germany**

The approach

The Siegerland venture capital fund was set up in 1983 by the public savings bank located in the Siegerland regions in the state of North Rhine Westphalia and is the oldest regional venture capital fund in Germany. It aims to contribute to longer term and successful development of SMEs in the Siegerland region as well as offering financial and advisory support to start-ups. It offers three product lines:

- **S-BETEILIGUNG** focuses on equity capital for existing small businesses and start-ups, offering seed, start-up and growth financing and funding for business succession. The fund invests between EUR 200 000 and 850 000 for between 5 to 10 years, as a shareholder and/or in the form of a dormant partnership.
- **S-KAPITAL** provides equity capital for growth in medium-sized companies with good credit rating. Investments are in the form of participatory rights capital of between EUR 250 000 and 850 000 for 7 to 10 years.
- **S-CHANCENKAPITALPLUS** offers equity capital as a dormant partnership for amounts between EUR 50 000 and 200 000 for up to 7 years to smaller firms combined with a loan or leasing financing from the savings bank.

Results

Since its creation the fund has invested in the equity of over 150 companies in the region.

Success factors

The fund has developed a focused investment approach, concentrating on three products that provide risk capital for critical stages during enterprise development (business start-up, business succession, and restructuring during crisis). It also complements the provision of equity capital with management support and coaching for the companies it invests in.

Problems and responses

The fund experiences high company failure rates given the risky nature of the projects it invests in. It has therefore developed a diversified portfolio of investments in terms of the mix of sectors and enterprise sizes.

Relevance to the Russian Federation

Regional venture capital funds are an important part of the financial infrastructure in regions with significant numbers of start-ups and growth-oriented SMEs that find it difficult to access national equity funds. The number of regions offering venture capital funding should grow in the Russian Federation as the SME sector strengthens.

Further information

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Source: Information supplied by Siegerlandfonds.

Innovation programmes

The infrastructure for support of innovative SMEs and start-ups is relatively uniform across regions. All regions have a mix of technoparks, incubators, technology transfer centers, prototyping and design centers and engineering centres created in line with federal programmes. Some regions have adapted elements of this infrastructure to the needs of local enterprises, for example by the involvement of private businesses in the development of incubators and prototyping centres, as in the case of Kaluga. In addition, the consultancy services provided to local businesses as part of the service offer of the innovation centres is an important means of tailoring support to the needs of regional enterprises.

However, there is more scope to develop innovation support actions that are more targeted to the particular innovation needs of local enterprises and that aim to support the development of regional economies towards emerging competitive strengths. Some of the science and technology park infrastructure can be made more effective in stimulating local knowledge transfers between universities, research organisations and local SMEs by increasing the emphasis on support to academic spin-out enterprises and other innovative businesses in terms of networking, coaching and innovation collaboration relative to company-specific subsidies and premises (see Box 7.4). In addition, it is important to provide sector-specific innovation services for strong regional clusters. Such innovation support should not be confined to technology-oriented innovation but should also be able to support incremental and non-technological innovation in non-science based sectors.

Box 7.4. **Jönköping Science Park, Sweden**

The approach

Jönköping Science Park was established by the municipalities of Jönköping and Habo and Jönköping University in order to support the creation and growth of businesses exploiting university research. Its actions are financed by the two municipalities and the university and by bids to national innovation programmes and the European Union Structural Funds. The science park offers the following innovation services:

- **Business Lab** provides free coaching support to students and employees from Jönköping University wishing to start a business. Recent graduates with experience of business are employed as coaches and can be supplemented on a case-by-case basis by senior coaches.
- The **Business Incubator**, with 15 places, supports growth-oriented businesses with a personal business developer during a period of two to three years. Its services include over 400 hours of business coaching and access to specialist advice in law, economics, banking and insurance, technology and marketing. Office space in the incubator is free of charge for the first three months, after which market rents are applied.
- The **Business Growth** section hosts around 80 firms, including R&D units of large firms and companies that provide services to other firms on the Science Park. A "co-working space" has recently been created to encourage innovation collaboration. The space can be booked on a daily basis and favours exchanges, networking and synergies between young entrepreneurs, typically in creative professions.
- The Science Park has built up a **Financing Web Portal** that provides an overview of funding opportunities available in the region. Funding sources are classified according to business development stages (idea, start, development, growth).

Box 7.4. **Jönköping Science Park, Sweden** *(cont.)*

- **The Jönköping Business Development Investment Fund** is jointly owned by Jönköping Science Park, Jönköping University, the Sixth AP Fund and several private investors. It focuses on early-stage investments in high-potential businesses with innovative products and services or with international potential, usually as the first external investors.
- **Research commercialisation service**. The Science Park started a new service in 2011 to offer University staff and students the means to utilise and commercialise their research results, for example through finding new channels to disseminate research results to society, matching students and researchers to companies, and supporting the creation of a start-up based on research results.

Results

The Science Park currently hosts approximately 100 businesses. Since its establishment in 2002 it has contributed to the creation of almost 1 000 start-ups.

Success factors

Features of the Jönköping Science Park that have contributed to its success in supporting local entrepreneurship and innovation are:

- Strong links to the University, reinforced by co-investment and co-ownership.
- Targeted support that differentiates between graduate entrepreneurs and growth-oriented businesses.
- An integrated support package combining infrastructure services (hatchery, incubator) with financial and non-financial services and growth mentoring.
- Low costs of mentoring and other support for student entrepreneurship.
- A very good understanding of the needs of academic entrepreneurs and continuous initiatives to improve existing services.

Problems and responses

The high share of international students and employees at Jönköping University sometimes prevents academic start-ups from progressing towards growth when students and/or employees return to their home countries. The Science Park helps address this problem by facilitating the acquisition of promising start-ups by larger Swedish or international companies.

Relevance to the Russian Federation

This is an example of a Science Park developed by regional stakeholders that provides a range of coaching, mentoring, financing and networking services as well as physical space for the development of graduate enterprises and high growth potential firms. These types of services and objectives should be emphasised strongly in the further development of science and technology parks in the Russian Federation.

Further information

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Source: Jönköping Science Park and Sjölundh, T. and Wahlbin, C. (2008) "Entrepreneurial students: The case of students starting up companies in parallel with their studies at Jönköping University", Sweden. *Industry & Higher Education*, 22(6), 441-452

Labour market and skills programmes

SME and entrepreneurship development is held back by a limited supply of skilled labour in many regions of the Russian Federation. Lack of skills is often connected to a poor image of vocational training among enterprises and people as well as to loss of more skilled workers due to outmigration from poorer regions. In response, regional

governments have started to implement skills development programmes that focus on training of SME workforces in collaboration with employers. They often work with regional industry councils, chaired by regional ministries with representatives of regional educational establishments and regional companies of different sizes, to define appropriate local training initiatives. On the other hand, more can be done to adapt training in higher education institutions to the needs of regional SMEs. In particular, graduate internships in SMEs are under-emphasised by regional government training initiatives. Furthermore, regional governments have not done enough to adapt business education in higher education institutions to the requirements of SME and entrepreneurship development. The case of the introduction of entrepreneurship education in curriculum of the Novosibirsk Technical University demonstrates the potential to increase the relevance of business training to regional economies (Box 7.5).

Box 7.5. **Entrepreneurship education in Novosibirsk Technical University**

Since 2004, Novosibirsk Technical University offers its own educational programme for students and young scientists wishing to start their own businesses based on the conclusion that the federal standard business education did not fit the needs of their students and employees. It developed a tailored educational offer focused for example on commercialisation of research results and internationalising a technical business venture. In their master theses, interdisciplinary project teams consisting of designers and engineers undertake tasks such as planning their own business and publicly defend their idea in front of a jury of local business and technical specialists.

Source: Information from Novosibirsk Technical University.

Cluster programmes

Regional clusters have been supported since 2012 by a federal innovative clusters programme favouring regions with a strong science base (Kutsenko and Meissner, 2013). For example the federal programme has been used to develop a medical technologies cluster in Akademgorodok in Novosibirsk and a biotech and pharmaceutical cluster in Obninsk in Kaluga. The latter included the establishment of a biotechnology and pharmaceuticals training centre in February 2012 with the involvement of key employers and plans to locate a branch of Moscow State University in Kaluga to undertake science and education related to the needs of local firms. The weakness of these cluster initiatives, however, is that they are restricted to R&D-driven innovations. Businesses that can participate directly must hold a patent, have applied for one or have implemented other measures to protect their intellectual property. They are required to submit information related to the volume of their innovative products or services, and they have to undergo a technical audit and an expert evaluation after which they obtain the status of "innovative business". This approach risks excluding many innovative SMEs from cluster support since even in technology-driven sectors SMEs often do not possess in-house R&D. It also limits the scope of the policy to develop non-science based clusters.

Some regions are also developing clusters as part of their inward foreign direct investment strategies, as in Kaluga with its emerging automotive cluster that includes Magna and Volkswagen as anchor firms for local supplier development. In principle, such supplier development strategies offer a good basis to build on regional strengths. However,

regional supply chain development initiatives do not yet seem to follow a comprehensive and systematic approach. Rather, the linkages that have been created have been ad-hoc, in that they respond to certain inward investment projects but are not spread across the whole SME development system and do not involve all major inward investors. Furthermore, the scope for developing training programmes for clusters has been under-emphasised relative to innovation support. Box 7.6 provides an international example of how such training initiatives could be promoted in regional clusters.

Box 7.6. **A training programme for the medical instruments cluster of Tuttlingen, Germany**

The approach

Tuttlingen is a rural district in the south west of Germany that hosts a long-established SME-based medical engineering cluster accounting for some 75% of Germany's surgical instrument industry. The cluster includes approximately 300 final producers of medical instruments, 200 subcontractors, and 80 trade enterprises. The cluster has a highly-skilled workforce with specific mechanical skills and tacit knowledge built up over many years.

To retain the cluster's lead in the face of increasing international competition, local public actors and enterprises have co-operated to build the offer of technical training aimed at cluster firms. Two major initiatives were taken. First, in 2003 the municipality helped finance the establishment of the International Business School Tuttlingen, which offers a specialist MBA programme on Medical Devices and Healthcare Management for engineers, scientists and medical doctors. Second, in 2009 the regional government of Baden-Württemberg and the city and district governments of Tuttlingen financed the establishment of a new campus of the University of Applied Sciences of Pforzheim in the town of Tuttlingen offering bachelor studies in medical technologies focused on surgical instrument making. The buildings required an investment of EUR 11 million. The university campus is also supported financially by more than 100 local enterprises. These enterprises also contribute to course selection and design, have a say in the recruitment of new professors and contribute to teaching by participating as lecturers.

Results

This initiative led to two new local facilities for vocational and tertiary education aimed at a specialist cluster workforce.

Success factors

The partnerships created between regional and municipal governments, private sector companies and higher and vocational education institutions have been the basis for the development of this new training infrastructure.

Problems and responses

The financial sustainability of this model could become an obstacle in the longer run. To help secure funding, the municipality of Tuttlingen set up an association together with private companies that supports the new applied sciences campus with EUR 2.5 million annually for up to ten years.

Relevance to the Russian Federation

This initiative illustrates how training projects can be developed for a cluster by adapting the activities of existing vocational and tertiary education institutions with support of local government authorities and cluster enterprises.

Further information

www.hfu-campus-tuttlingen.de/campus/tuttlinger-hochschulmodell/

Source: Information from municipality of Tuttlingen.

Rural development

Many regions also emphasise support for entrepreneurship and small business development in rural areas. The focus lies, however, on self-employment, small family breeding farms and cooperatives, and/or on agri-tourism, all of which reflect federal priorities. As of today, there appears to be little emphasis on a comprehensive and genuinely tailored regional approach to fostering SMEs in rural areas.

Development of mono-industry cities

Mono-industry cities are dominated by a single large employer or a handful of large employers as a legacy of the centrally-planned economy and are often in substantial decline given ongoing economic restructuring. There are currently some 150 mono-industry cities, constituting approximately 14% of the Russian Federation's cities and 11% of its urban population. They are structured in a core-periphery pattern, centred on the industrial core of the Russian Federation in the Urals Federal District (Zubarevich 2011). Mono-industry cities offer poor conditions for economic recovery through SME and entrepreneurship development, such as lack of appropriate skills and infrastructure and a large distance from consumer markets. The predicament of the mono-industry cities worsened markedly in the wake of the global financial crisis in 2009, generating wage arrears, accelerating job layoffs, increasing unemployment, intensifying fiscal stress, and triggering protests and unrest (Deutsche Bank Research, 2009). In response, the federal government and the relevant municipal authorities introduced a twin strategy of redirecting a portion of natural resource revenues generated within mono-industry cities to supporting public consumption and maintaining traditional sources of employment (Commander *et al*. 2011) and supporting new business formation by investment in retraining and small business premises (Zubarevich 2011). However, to date there has been insufficient emphasis in these packages on building entrepreneurial skills and role models given a prevailing lack of entrepreneurial culture.

Budget constraints

In seeking to boost the locally-differentiated element of SME and entrepreneurship policy and ensure that there is at least a basic level of programme support and business support services infrastructure in every region and municipality it is important that regional and municipal government authorities have budgets available for local SME and entrepreneurship programmes. However, only three taxes (on property, gaming and transport) go directly to regions and only land taxes go to municipalities. All other taxes either go directly to the federal budget or are shared between the federal, regional, and municipal levels according to proportions stipulated in the Budget Code (OECD, 2008). Furthermore, federal law dictates floors, ceilings and exemptions for these taxes, and it is not in the remit of the regional authorities to change rates, for example to increase these taxes in order to fund economic development actions. The situation has worsened since Local Self-Governance reforms in 2005 that reduced the fiscal capacity of regional administrations while leaving their statutory responsibilities intact (Chepurenko, 2011; Deutsche Bank Research, 2009). A further consequence is that some local political leaders may lack motivation to push hard for SME and entrepreneurship development programmes because they will capture only a small proportion of the additional tax revenues generated and end up under-funded relative to the scale of the tasks required.

This leaves the sub-national authorities largely dependent on federal transfers to develop SME and entrepreneurship policy actions; regional authorities relying heavily on fiscal transfers from federal government and municipalities relying in turn on transfers from the regional authorities. While there are some unconditional block transfers from federal to regional authorities, which aim to reduce the gaps in fiscal capacity between the richest and poorest regions, and represent just under one-third of the value of federal-regional transfers (World Bank 2011), the majority of the transfers are conditional, i.e. they can only be used for specific programmes on the basis of co-funding arrangements. These co-funding arrangements include a redistributive mechanism in allocating additional funds to regions with low levels of entrepreneurship and SME activity and limited regional budgets (Box 7.7). This is a kind of place-based positive discrimination toward supporting lagging regions that could help them catch-up with the best performing regions over the longer term and promotes the kinds of more balanced development sought in the Russian Federation (Barca *et al*., 2012). It contrasts with a strategy of concentrating available support in the best performing regions that already have favourable conditions for SMEs and entrepreneurship.

Box 7.7. **Redistributive allocation of federal co-financing**

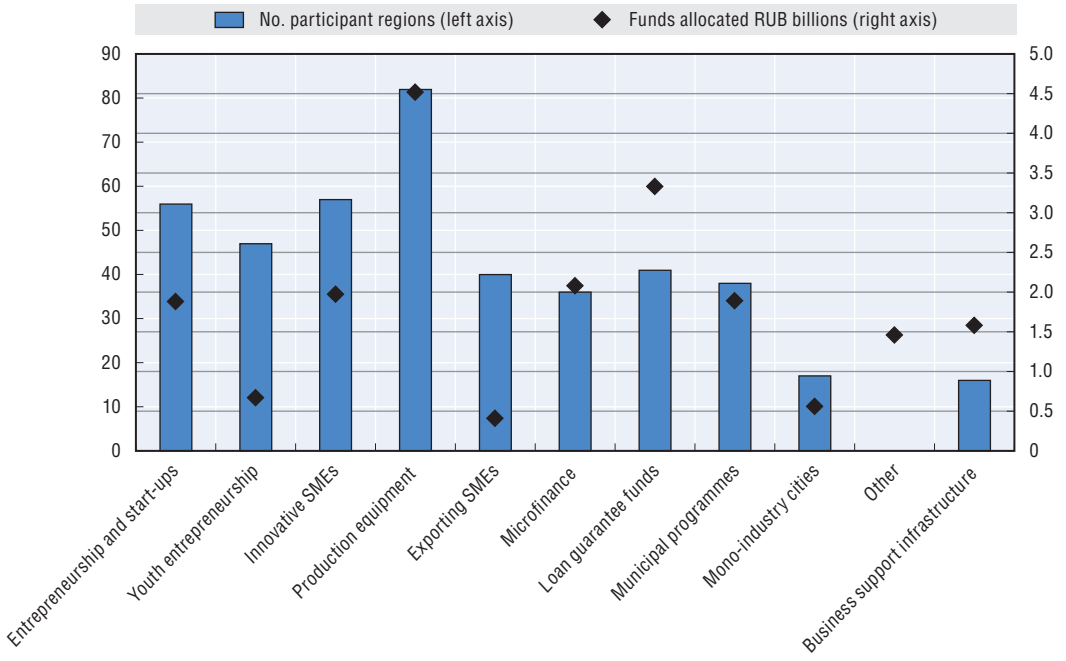
A co-financing allocation model is used in SME and entrepreneurship policy in the Russian Federation, which enables the relative proportion of budget contributions to SME and entrepreneurship programmes made by the federal and regional levels to vary according to the level of prosperity and need of the regions, for example in terms of the number of active entrepreneurs and SMEs operating in each region and the relative levels of regional budget contributions. For Moscow and St. Petersburg the ratio is 50:50 between the federal and regional contributions. However, weaker regions with strong SME development needs can obtain up to 80% funding from the federal level. For example, the Chukotka Autonomous Area receives higher levels of federal co-financing for its entrepreneurship education programme in order to respond to very low current numbers of entrepreneurs and SMEs.

Source: Information supplied by Ministry of Economic Development, Russian Federation

Given the importance of federal co-financing to the development of SME and entrepreneurship policy actions at local level, it is important that regional and municipal authorities participate fully in the co-funded programmes and that these programmes are adequately funded. However, changes will be needed to ensure that this is the case. In the area of SMEs and entrepreneurship, the key co-funded programme is the federal SME support programme. However, as shown in Figure 7.12, although collectively all regions participated in at least some components of the federal SME support fund in 2012, many regions do not put forward bids to participate in certain programme components, leaving gaps in support across the country. In particular, only 16 regions participated in the business support infrastructure component of the federal SME support programme. Similarly, less than one-half of all regions participated in the SME exporting, microfinance, loan guarantee and municipal programme components. This compares to 82 regions that participated in co-financing of the "leasing development and production modernisation" component and more than 50 regions that delivered the "support for innovative companies", entrepreneurship and start-ups and youth entrepreneurship components. One of the factors behind the low participation of regions in certain federal SME support programme components is that the rules and guidelines for regional participation in federal SME support programmes can be quite rigid and do not allow regions to adapt programme support to their own requirements.

Figure 7.12. **Regional participation in federal SME fund programme components**

2012



Note: "Other" is not specified in the information supplied but includes support for activities to promote entrepreneurship and to develop a system of personnel training, retraining and advance training for the small business sector (training vouchers, compensation for training/ retraining costs, and organisation of training events).

Source: Information provided by the Russian Federation Ministry of Economic Development.

StatLink http://dx.doi.org/10.1787/888933272196

An important action to support the development of local SME and entrepreneurship programmes in the Russian Federation will be to increase the flexibility of the federal SME support programme to meet local needs and the level of co-ordination between federal and local authorities in the development of the programme. In parallel, it is important to encourage each regional and municipal administration to allocate appropriate funding to SME and entrepreneurship programmes in each financial year so that they have the necessary co-funding for participation in federal schemes and can develop some actions of their own independently. In this respect, consideration should be given to a greater degree of fiscal decentralisation and the question of whether more business tax revenues should be retained at municipal and regional levels. This would act as an incentive for the sub-national authorities to promote SME and entrepreneurship activity, both through improving their business regulations and through developing their own SME and entrepreneurship programme measures and participating in those of the federal government. It would also give them an initial budgetary basis to develop SME and entrepreneurship programmes that could be expanded as their success in generating new tax revenues grows.

Constraints in strategy making capacities and processes

As well as available budgets, a strong local dimension to SME and entrepreneurship policy depends on having regional and municipal governments with the professional capacities and ongoing practices required to design and implement SME and entrepreneurship programmes that respond to the particular problems and opportunities in their areas.

To some extent the necessary arrangements are in place. The preparation and use of regional economic development strategies by the regional government administrations is foreseen by the federal SME Act of 2007, which also specifies that the process of regional strategy development should include consultation with business, civic and government stakeholders.

There are several examples of regions that have utilised the available autonomy and developed effective regional strategies in this manner. The Novosibirsk regional administration, for example, has designed and developed a special purpose SME development programme, which was allocated RUB 190 million from regional budget funds and a further RUB 470 million from the federal budget in 2011 (PwC, 2012). A core focus of this strategy has been commercialisation of results from the region's science base through investment in a network of technoparks to support the start-up of new businesses with close connections with universities and research institutes and the provision of localised business support facilities such as business incubators for local target sectors including instrumentation, information technology, biotechnology and nanotechnology for new materials. Kaluga region is another to have developed a tailored strategy for SME and entrepreneurship development focused on mobilising its particular local economic potential. In this case, the region has chosen to focus on building up its lead clusters by encouraging innovative entrepreneurship, supported by the creation of a regional Agency for Innovation Development, attracting foreign direct investments in the key sectors, such as the automotive industry and biopharmaceuticals, and stimulating linkages with local and regional firms.

However, the quality of regional economic development strategies, and the degree to which they identify and respond to key local conditions, varies significantly across the Russian Federation. Without strategies, the priority and direction of the regional administration's aspirations and intentions for SME and entrepreneurship development cannot be communicated and shared with business owners and SME managers. Similarly the degree of stakeholder consultation varies significantly. And in most cases, regional strategies are developed without arrangements for robust monitoring and evaluation of regional SME and entrepreneurship trends and problems and the impact of programme actions undertaken. All the regions and municipalities of the Russian Federation should be encouraged to develop regional economic development strategies as a guide to their SME and entrepreneurship actions, including appropriate consultations with local stakeholders (see Box 7.8) and the use of local monitoring and evaluation evidence.

With respect to monitoring and evaluation, strong emphasis should be placed on securing independence and objectivity and using modern approaches for distinguishing appropriate indicators for programme inputs, activities, outputs, outcomes and impacts. The appropriateness of monitoring and evaluation indicators is critical; otherwise the incentive and performance management structures for policy initiatives and institutions will be skewed. The effectiveness of the prototyping centre in Novosibirsk, for example, was measured on the number of new jobs it created whereas its main focus is productivity improvement, potentially reducing direct jobs. Stronger evaluation is especially important at the current time, given the relatively early and expansive stage of development of the policy support system at the regional and municipal levels. Reflection upon evaluation evidence will help inform regional and municipal policy makers about whether the

appropriate mix of programmes is being developed for their areas and whether the programmes are being well implemented.

Box 7.8. **Stakeholder engagement in regional strategy development**

Good practice policy increasingly recognises the importance of involving stakeholders in each stage of the policymaking cycle: from identification of the problem, through analysis, option appraisal, design, development, delivery, evaluation and feeding back into policy improvement. Stakeholder engagement enables more detailed and in-depth understanding of the policy area, gathers knowledge and insight from a wider field, and enrols actors into supporting the policy. In the Russian Federation, regional and municipal administrations have been experimenting with flexible stakeholder engagement models capable of incorporating particular mixes of regional and municipal actors in the policymaking process. Examples include Regional Industrial Committees or Councils that have been established to ensure that the voices of entrepreneurs and SMEs as well as other stakeholders such as business associations, universities and civic groups are heard in the policy development deliberations of regional and municipal administrations. Typically this input spans a range of issues including business education, regulations, tax, training and transport. In Kaluga, for example, the Chamber of Commerce is active in supporting particular groups such as women managers, owner entrepreneurs, entrepreneurs in specific sectors and young people to meet and input into policy representation activities. Opening up the policymaking process at the regional and municipal levels in this way has delivered benefits for effective policymaking and such experiences are worth consideration in other regions with more closed policymaking approaches.

Source: Information from Kaluga regional government and chamber of commerce.

The European Union's new approach to regional innovation strategies – based on the idea of 'Smart Specialisation' – warrants attention as a means of promoting the tailoring of policy approaches to particular regional and local contexts in the Russian Federation through a clear and structured process of strategy development (Box 7.9).

One of the constraints to developing appropriate regional and municipal strategies at the current juncture is a lack of professional capacities to design and implement appropriate regional and local economic development strategies (Chepurenko, 2011; Smallbone and Welter, 2012). The federal Ministry of Economic Development could therefore assist regional and municipal administrations to get started in developing appropriate strategies by identifying different types of regions with particular kinds of needs and possibilities, for example divided around the categories of 'very weak', 'weak', 'medium-developed' and 'highly-developed' areas, together with the proposal of appropriate modules of policy support around which regional and municipal administrations could adapt their approaches to their own conditions. Such an effort is not meant to replace regional evidence gathering and stakeholder consultation but can complement and support it, particularly in the short term as strategy development needs are identified and capacities increase. In parallel, the federal government could sponsor national capacity-building activities for regions and municipalities in strategy making, such as training and good practice experience exchanges in policy design, development, implementation and evaluation.

Box 7.9. **Smart Specialisation Strategies, European Union**

The approach

Smart Specialisation Strategies aim to promote entrepreneurship and innovation by creating a mechanism that increases the focus of public and private investments in research and innovation on regional competitive advantages, including actions that will support regional transition to new sectors.

The process of developing a Smart Specialisation Strategy in a region involves six basic steps:

1. Analysis of the regional context and potential for innovation (involving differentiation based on how to transform existing economic and technological specialisations into new activities that can be exploited by SMEs and new ventures).
2. Establishment of a sound and inclusive governance structure for the strategy (involving different national and regional policy organisations as well as regional universities and enterprises).
3. Production of a shared vision about the future of the region (identifying possible paths for economic renewal and transformation of the region and communicating these paths to stakeholders).
4. Selection of a limited number of priorities for regional development (making choices reflecting the existence of key assets and capabilities within and across sectors, the diversification potential of these sectors or cross-sectors, their critical mass, and their international position).
5. Establishment of suitable policy mixes (through a multi-annual action plan including action lines and projects, target groups, responsible actors and delivery mechanisms, targets, timelines and funding mechanisms).
6. Integration of monitoring and evaluation mechanisms to assess the appropriateness and impact of the strategy (including context indicators benchmarked against other regions and strategy output and results indicators).

The development of Smart Specialisation Strategies at national or regional levels has been introduced as a condition for obtaining European Union regional innovation funding from the European Structural Investment Fund and Horizon 2020 research fund during the 2014-2020 programming period. Training, guidance materials and capacity building support is offered by the European Commission to regional actors to help them develop appropriate strategies.

Results

Smart Specialisation Strategies aim to increase the impact of regional innovation policies by focusing public investments where policy can make the most difference to economic development in each region and co-ordinating the activities of different stakeholders to increase positive synergies. The results will become apparent as the programming period advances. However, the introduction of a 'conditionality' establishing a strategy for drawing down funding together with provision of guidance on how to prepare such strategies has led to the development of more and better quality regional development strategies.

Success factors

A number of key factors are likely to play a critical role in the success of regions in developing and implementing Smart Specialisation Strategies:

- Regional actors need strong familiarity with the purpose of the approach and how to undertake each component, including methods of diagnosis of regional potential and involving regional stakeholders, methods of identifying and setting priorities and methods of linking regional strategies with national and sectoral policies.
- The sector development priorities of different regions should be distinct and closely linked to genuine regional competitive advantages, rather than all focused on a desire to develop the same fashionable sectors (information technologies, life sciences, nanotechnology, logistics, green energy etc.).
- There should be clear linkages between stated priorities, programme interventions and budgetary allocations.

Box 7.9. **Smart Specialisation Strategies, European Union** *(cont.)*

- Regional monitoring and evaluation need to be well developed in order to support the assessment and prioritisation of policy.

Problems and responses

Some technologically advanced regions see little value-added in developing a strategy while others lack the capacity to do so. This implies the need for capacity building in strategy development, especially in regions with little experience of developing strategy and innovation policy.

Relevance for the Russian Federation

Increased tailoring of SME and entrepreneurship programmes to regional contexts will increase the impact of federal and regional SME policy spending in the Russian Federation. The Smart Specialisation Strategy approach provides a method of analysing regional opportunities and combining the efforts of different national, regional and local stakeholders in creating regionally-specific action plans to guide programme intervention. It is an approach that emphasises the importance of innovation and entrepreneurship applied to all types of regions, not just regions with strong high-tech and R&D assets.

Further information

European Commission Smart Specialisation Platform: *http://s3platform.jrc.ec.europa.eu/home*.

Source: European Commission Smart Specialisation Platform.

A further important challenge is to develop stronger political leadership in support of SME and entrepreneurship activities from the governors and deputy governors of regional administrations and the mayors of cities. Where political leaders have given SME and entrepreneurship policy a priority strategic position and direction, this has positively shaped the initiatives and efforts of their functional ministries, departments and agencies as well as framing the activities of regional and local businesses, associations and civic actors. In some regions, such as Novosibirsk, the economic development minister and ministry provide the lead and are responsible for strategy and co-ordination of support mechanisms. This type of economic development leadership should be encouraged in other regions and cities. It can also be effective to establish new ministries for economic development at the regional level with briefs to co-ordinate and integrate SME and entrepreneurship development activities across existing ministries (Box 7.10).

Box 7.10. **Innovation in ministerial organisation in Kaluga region**

There is a tendency for government administrative structures to promote ministry-focused or 'silo' approaches that hamper the development of cross-ministry strategies for SME and entrepreneurship development. To address this problem, the regional government in Kaluga established a ministry with a deliberately cross-cutting focus to work across and with specific functional ministries. The Ministry of Information Society and Innovation has a brief to focus upon innovation and the information society, and to drive its integration across the existing functional ministries. The aim of this institutional innovation is to integrate and co-ordinate activities, ensuring that innovation is given support and priority, and that the programmes and policies of specific ministries are complementary and supportive. The Ministry of Information Society and Innovation has a specific role in leading and driving entrepreneurship and SME policy at the regional and municipal levels.

Source: Information from Kaluga regional government.

Policy co-ordination between federal and local levels

The existence of significant local actions in SME and entrepreneurship policy implies the need for appropriate arrangements to co-ordinate federal and local actions so as to ensure that policies at the different levels of government pull in the same direction. There are two pillars in federal-local SME and entrepreneurship policy co-ordination in the Russian Federation. The first pillar is the 2007 federal SME Act, which identifies the forms of support to be offered at the regional and municipal levels, without specifying their funding sources. The second pillar is the co-funding of regional and municipal actions through the federal SME support programme, which allows regional and municipal governments to choose which of the federally-supported programme components to get involved in and how to shape them to their local contexts and the federal government to choose which regional and municipal actions to fund from those proposed to it.

A strong steer can be given to the actions undertaken in the regions by the priorities that the federal government gives for the use of the federal SME support programme. In order to secure programme actions in its priority areas, the Ministry of Economic Development issues an annual order listing the measures that will be supported under the federal SME support programme. It defines these measures based on its priorities, past absorption of programmes and suggestions from the regional and municipal authorities that co-fund the actions. Federal priorities for 2010-2012, for example, were focused upon the innovation sector, modernisation of manufacturing and credit guarantee and micro-financing programmes. Regional authorities that develop actions in these areas have a greater likelihood of securing funding because of the greater resources available and the greater match with federal government selection criteria. The technoparks in Novosibirsk, for example, successfully secured support for activities by matching with the federal priority to support information technology cluster initiatives in the regions. This also affects the resources available to municipal authorities, which have to work with and through the regional administrations and cannot bid directly to the federal government.

Policy dialogue across the different levels of government is critical to ensuring effective operation of the co-funding system. To facilitate the dialogue, the federal Ministry of Economic Development and makes an annual presentation to regional and municipal governments on the upcoming programme and how they can participate. Some regional administrations have cultivated additional relationships with federal government, for example meeting to exchange opinions, feed in their views on upcoming programme development, and gain insight into federal policymaking and priority setting in order to increase their bidding success. As the federal ministry expands its range of programmes annually, it is open to influence from the regions and municipalities on which types of activities to support and this type of dialogue can be very important in ensuring that it is able to support regions and municipalities effectively. For example, the federal government decided to roll out advance payments for leasing agreements to all regions following a successful regional programme in Tatarstan.

However, some regional authorities, especially those beyond the main urban centres, currently consider that federal SME and entrepreneurship policy priorities, both within and beyond the federal SME support programme, are identified without sufficient dialogue with them in order to ensure that co-funding mechanisms can respond to the particular needs of their regions. More in-depth dialogue with a wider range of regional and municipal authorities should be therefore be encouraged to help build the responsiveness of federal programmes to regional conditions and increase the ability of the regions to make use of co-

funding possibilities. In addition to the proactive efforts of certain regional and municipal authorities in opening up a dialogue on SME and entrepreneurship development with federal government, a strengthening of formal arrangements for federal-local dialogue is recommended. In particular, it would be worthwhile to revitalise the Inter-regional Economic Associations (IEAs) that existed earlier in the 2000s to support interaction between the federal, regional and municipal authorities and to provide a channel for feedback on the shaping of federal policy initiatives.

Conclusions and recommendations

It is important to build a strong local dimension to SME and entrepreneurship policy in the Russian Federation in order to respond to large spatial variations in the scale and nature of SME and entrepreneurship activity and the conditions that affect it and ensure that there is at least a basic set of programme interventions and business development services provision in each region and municipality. The density of SMEs and the rate of business creations are both higher in more prosperous and urban regions than in poorer and more rural locations, which suggests the need for remedial actions to address the problems of the lagging regions if national objectives are to be met for growing the SME economy and generating a more balanced pattern of regional development and potential. In addition, there are significant differences in the sector structures of different regions and municipalities, their environments for innovation and the nature of the entrepreneurship and SME activity that can be encouraged as well as in the scope and nature of the business environment constraints that SMEs and entrepreneurs face, calling for a differentiation of policy actions according to regional and local priorities.

Federal government can help respond to local differences and increase the scale of local SME and entrepreneurship support by implementing locally-distinct interventions via federal ministries and agencies. Some such initiatives are in place, including the innovative clusters programme of the federal Ministry of Economic Development and the partnerships that the public development bank, VEB, has developed with banks and other partners in specific regions aimed at developing SME finance interventions that are appropriate to the nature of the finance markets and SME and entrepreneurship activity in place locally. However, more can be done to encourage local differentiation and tailoring of federal policies, including by expanding the nature of the clusters programmes to cover non-science based sectors and actions for skills development as well as innovation and introducing other locally-focused programmes.

At the same time, the participation of regional and municipal governments will be critical to SME and entrepreneurship support, given their economic development powers and their local knowledge of SME needs. Regions and municipalities are already tasked by the 2007 federal SME Act with preparing regional economic development strategies in consultation with local stakeholders and there are many examples of strong regional strategies that respond to local opportunities, such as those of Kaluga and Novosibirsk. Regions and municipalities also have significant local regulatory responsibilities, and leading regions and cities such as Chelyabinsk. Saratov, Perm, Kirov, Novorossiisk, Smolensk, and Krasnodar are already engaged in important measures to reduce business registration costs, simplify local regulations, and open up public procurement to SMEs and entrepreneurs. However, many regions and municipalities are lacking key programme interventions and business development services infrastructure, good practices in local regulatory simplification have not been taken up in all places, and many regions are

working with economic development strategies that are not based on adequate analysis of local conditions.

The federal government can support regional and municipal authorities in introducing appropriate SME and entrepreneurship policies and programmes. In this effort, it needs to focus on addressing two key constraints experienced at the local level. The first concerns budgets. Municipalities and regional governments in the Russian Federation have constrained resources for SME and entrepreneurship actions because of limited fiscal decentralisation and local tax revenues and tend to rely mainly on co-funding of SME and entrepreneurship policy actions by federal government. A major budget for the core federal SME programme is therefore essential. In addition, regions and municipalities could be encouraged to participate more fully in the various components of the federal SME support programme through greater flexibility of its co-funding rules and greater dialogue in its design in order to increase the scope to adapt the programme to local needs, for example in terms of target groups, specific services offered, and the scale of spending on different types of initiative. Adjustments to business tax distribution arrangements could also encourage more involvement in SME and entrepreneurship policy by the regional and local authorities. Secondly, federal government can support stronger evidence-based strategy making at regional government level with training of local officials, good practice exchanges, developing model strategy templates for different types of region and encouraging the creation of economic development ministries at regional and local levels. The federal government can also develop mechanisms such as good practice exchanges to promote the roll out of regulatory changes at local level to better support SMEs and entrepreneurship.

The following key recommendations are offered to federal government to strengthen the local dimension of SME and entrepreneurship policy in the Russian Federation:

Key policy recommendations for federal government on the local dimension of SME and entrepreneurship policy

- Encourage all regional and municipal authorities to adopt good practice approaches in regulatory improvement and the use of public procurement for SME and entrepreneurship promotion, including through the creation of a national platform for experience sharing.
- Re-examine arrangements for the distribution of business taxation revenues with a view to increasing the incentives for regional and municipal governments to implement SME and entrepreneurship actions and increase the resources they put into this task.
- Strengthen the local differentiation and tailoring of selected programmes of federal ministries and agencies, including supporting more region-specific financing services through the public development bank, *Vnesheconombank*, such as venture capital and business angel initiatives in regions where strong innovative SME sectors are emerging, and expanding the federal clusters programme to cover non-science based sectors and include activities for skills development as well as innovation.
- Increase the participation of regional and municipal governments in the federal SME support programme by increasing federal-local dialogue in the design of programme components and increasing flexibility in the rules and management of the programme to better meet local priorities.
- Support regional and municipal authorities to develop their professional capacities for designing and implementing locally-distinct, evidence-based policies and programmes for SME and entrepreneurship promotion. Provide guidelines, training and forums for good practice exchange in strategy making, propose appropriate modules of policy support that can be implemented in different types of regions, and encourage the creation of new dedicated economic development ministries and offices in regional and municipal governments.

Note

1. Information from the website of the Federal Ombudsman *http://ombudsmanbiz.ru/*

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KEY ISSUES AND POLICIES

The Russian Federation has a target of increasing the share of small and medium enterprises to 50% of GDP and employment by 2020. Substantial policy efforts are being made, for example, to increase competition, reduce regulatory and administrative burdens, support the access of SMEs and start-ups to finance, and upgrade the productive capacities of small business. This report identifies the major future priorities. They include increasing transparency in business transactions, fostering an entrepreneurial culture, increasing SME workforce and management skills, developing supply chains, increasing the numbers and quality of business incubators and other business development service centres, and enlarging the financial and non-financial products of Vnesheconombank, the public development bank.

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