

**EXPLORING POSSIBILITIES FOR SUSTAINABLE DEVELOPMENT IN SMALL AND MEDIUM-SIZED ENTERPRISES IN THE NORTH-EASTERN REGION (NER)***Darina PAVLOVA*<sup>1</sup>*Sibel AHMEDOVA*<sup>2</sup>

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**ABSTRACT**

*The paper focuses on the key issues facing small and medium-sized enterprises in the North-Eastern planning region, their position (standing) and importance, their funding advantages and disadvantages, the impact of the external environment, the interconnectedness between business and entrepreneurship. The aim is, on the basis of research and analysis of the economic situation in NER, to outline the main factors and possibilities that should be considered in ensuring sustainable economic growth in the SME sector. For the purposes of this study, therefore, a detailed survey was carried out among SMEs in the region. Accordingly, much of the information for the paper comes from the official statistics and reports from different enterprises in the North-Eastern region (NER). Presented are also guidelines for a more effective SME activity that would facilitate their survival and effectively promote the achievement of economic sustainability.*

**KEYWORDS:** *small and medium-sized enterprises, competitiveness, sustainable development.*

**JEL CLASSIFICATION:** *011,012,04, R11.*

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**1. INTRODUCTION**

As a full member of the EU, Bulgaria recognizes the necessity of encouraging the creation of an environment that is conducive to the development of small and medium-sized enterprises (SMEs), enhancing their competitiveness, strengthening and expanding the presence of Bulgarian enterprises in the European and global markets as well.

Some of the complex issues in modern economy are the enhancement of competitiveness and achievement of sustainable economic development of diverse countries, regions, sectors of economy or individual business organisations. Small and medium-sized enterprises (SMEs), however, are of paramount importance for solving this problem.

SMEs are becoming an increasingly important factor in contemporary society, by providing employment opportunities and playing a crucial role in ensuring stronger local and regional economies.

And this is exactly what determines the purpose of the present study: through research and analysis of the SME situation in NER to get a better basis for drawing proper conclusions and making relevant proposals for enhancing SME competitiveness and achieving sustainable development of the region.

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## 2. FEATURES OF NER

The North-Eastern region comprises the northern part of the Bulgarian Black Sea coast, part of the eastern slopes of Stara Planina, part of Ludogoriето and Dobrudzha. The region consists of four districts: Varna, Dobrich, Shoumen and Targovishte and 35 municipalities. It covers 13, 05% of the territory and 13, 1% of the country's population and with its area of about 14 487 km is referred to as the smallest region in the country. In the overall assessment of the levels of vulnerability of the EU regions to development challenges, 2020 - globalisation, climate change (global warming), demographic changes and energy dependency, the North-Eastern region is ranked sixth among the European regions with the highest level of vulnerability to all four challenges. Its general vulnerability index is 82 out of 100 (possible points) (National Statistical Institute, 2014a, 2015).

Analysis of the economic situation in the North-Eastern region proves, however, it is in a comparatively good level. The region ranks fourth among the country's level 2 regions as regards primary indicators for measuring the level of economic development. Located within its territory are 13.8 % of the enterprises from the country's non-financial sector, accounting for 11.7% of the total number of persons employed, having 12.6 % of the tangible fixed assets at its disposal and realizing 10.8% of the revenues gained from the activities of the non-financial sector enterprises in the country.

The region is estimated to have great economic potential for business development and for increase in foreign investments – strategic geographical location, well-developed transport infrastructure and agreeable natural conditions.

The data analysis shows that the NER's total value of the produced gross domestic product (GDP) at current prices for 2014 amounts to BGN 10 198 million. Its contribution to the national gross domestic product ranks it third after the South-Western and South-Eastern regions. Actually, the proportion contributed by NER and the other regions taken together is approximately comparable to that contributed by the South-Western region /48.3%/ (National Statistical Institute, 2015).

In the distribution of GDP by regions at NUTS 3 level (districts) for 2014, it has become evident that Varna district makes up the largest share– 81.8 % of the total for the North-Eastern regional GDP, with Targovishte district –constituting the smallest one (12,1 %). The regions of Dobrich and Shoumen have similar values of 19.0 % and 18.2 % respectively.

The average value of the GDP per capita for 2014 in Varna district (10270 leva/person) exceeds the average value of the region's or country indicator (7468 leva/person). The other districts – Dobrich with BGN 6730, Targovishte with BGN 6179 and Shoumen with BGN 6141, are at levels substantially below those for the country or region. The inner-regional differences as to the percentage of the GDP within the region are considerably strong – Varna district holds 61.6%, whereas Targovishte - 9.1%.

The North-Eastern region has 12 % contribution to the country's gross value added. The reported value of the gross value added for 2014, BGN 7 496 thousand, ranks the North-Eastern region fourth after SWR, SCR, and SER.

### 2.1. Position of SMEs in NER's economy

Over the last two years in NER there have been 49 853 well-functioning entities actively participating in the economic life across all sectors, out of which 46 138 are micro, 3090 small, 536 medium and 90 large enterprises. Micro enterprises hold the largest relative share of 92,5%, followed by the small and medium with 6,2% and 1,1% respectively. Large enterprises in NER represent a tiny share of 0,2% (National Statistical Institute, 2013, 2014a, 2015). 243728 people are employed in the economic sector, with the net revenues from the sales being BGN 20246597 thousand. The level of entrepreneurial activity in the region is 51,3%, with an average for the country of 48,9% (National Statistical Institute, 2014b).

By districts it is estimated that the largest group of economic entities is in Varna -31389 or 62,2% of all in the region, and the smallest one - in Targovishte district - 7,3%.

In the North-eastern region, the service sector accounts for 62.90% of the region's gross value added, the industry – 29.79 %, and agriculture – 7,29 %. The region's economy comprises agriculture and forestry 8%, industry 31% and service sector 61%.

Service sector is the most attractive arena for the small and medium-sized enterprises. SMEs produce 73.7% of the value added in the service sector average for the country. NER reports an increase beyond these levels after 2010. And yet, no substantial shifts in these shares by regions have been observed recently. The difference between maximum and minimum indicator value in percentage points has increased from 22% to 24%. SMEs produce around 45% of the value added in the industry sector average for the country.

Comparative analysis of the data by regions shows that SME value added share in NER's industry has risen from 40.40% to 47.20%. SMEs provide roughly 97% of the value added in the agricultural sector average for the country.

The structure of economy within and across localities shows that the share of agricultural enterprises is the largest in Dobrich-19%, followed closely by Targovishte with 15%, Shoumen 14% and Varna with only 3% (National Statistical Institute, 2014a).

37% of the enterprises in the town of Targovishte operate within the sphere of industry followed by the other regional towns: Shoumen - 32%, Varna - 31% and Dobrich - 27%. In the sphere of services the greatest share goes to the enterprises in Varna-66%, Dobrich with 55%, Shoumen with 54% and Targovishte with 48%.

The branch structure of industrial enterprises is varied, with manufacturing gaining a competitive lead over the production of chemical products and agro- food (and beverage) industry, whereas the production in the textile, footwear, clothing and knitwear industries corresponds to only 2,5% of the industrial output. With a share of 22.9% it appears that production and distribution of electricity and thermal power has become the main economic driver of the region. The region is leading in terms of electricity produced from renewable energy sources /RES/.

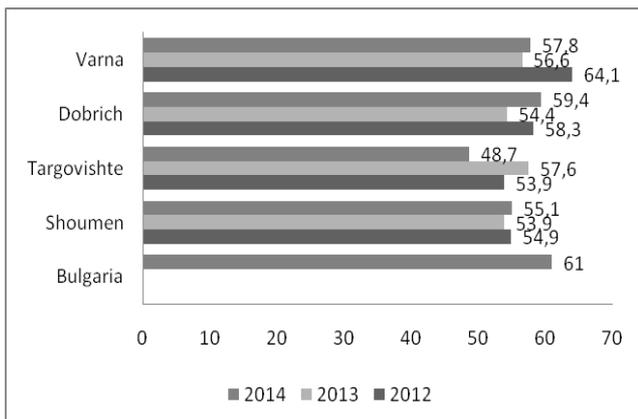
Considering the facts above, it should be noted that profitability of non-financial sector enterprises exceeds the average for the country, and that, thus far, is not directly linked to—fast pace of technological renewal and implementation of innovations in the industry sector enterprises, it is, rather, related to achieving greater profitability in industrial branches such as agriculture, transport services, hotel industry and catering industry or restaurantship.

## **2.2. Employment in NER's SMEs**

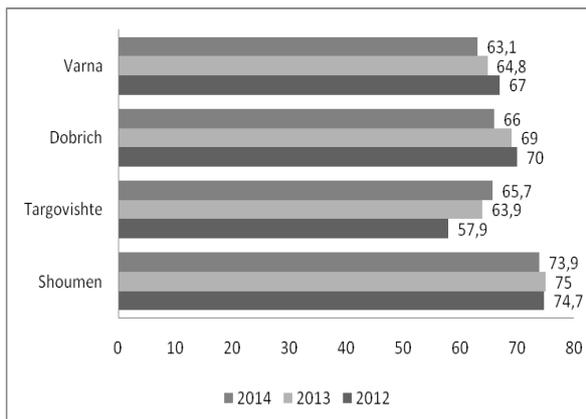
In recent years SMEs provide approximately three-fourths of the employment in the non-financial sector, and their share has risen from 74.5% of the total number of people employed in all non-financial enterprises in 2008 to 75.4% in 2013.

The values of the rate of economic activity of the population in Bulgaria are significantly behind the EU average -27. NER level of economic activity /66,1%/ is around 10% lower than the European average, but is close to the average value for Bulgaria. Among the level 2 regions, for 2013, NER ranks second after SWR with a value of /71.6%/ coming the closest possible to the European average of 28. The change in the rate of economic activity of the population over the period 2007 - 2010 to 15 completed years and over, identified in NER is a downward trend in the share from 67.9% in 2008, to its lowest value of 66.1% in 2011, which is even lower than the value in 2009, despite the slight increase with 0.2 % in 2010.

In 2014 the unemployment rate in the country goes down with 1.5 percentage points as compared to the previous year reaching 11.4%. Long-term unemployed persons (for one year or over) are 60.5% of all unemployed. The portion of the unemployed in NER in 2014 represents 12,6% of the total number of the economically active population in the region.



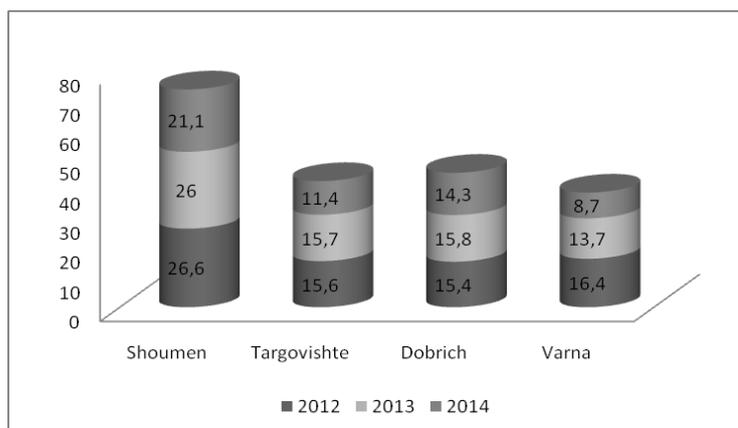
**Figure. 1 Economic activity rate**



**Figure. 2 Economic activity rate 15-64 years.**

Source: Data adapted from National Statistical Institute (NSI), 2014

Over the period 2012 to 2014 observed is a substantial shift in the unemployment rate across the different districts in the region. In 2012 in all four districts under study the rate of unemployment is high as a result of the ongoing consequences from the global financial and economic crisis. In 2012 Shoumen is the town with the largest relative share of unemployed persons accounting for 26,6%, followed by Varna with 16,4%, Targovishte with 5,6% and Dobrich with 15,4%. In 2014 the town with the lowest rate of unemployment is Varna - 8,7%, followed by Targovishte with 11,4%, Dobrich with 14,3% and Shoumen with 21,1%.(figure.3)



**Figure. 3 Unemployment rate of different districts in NER (%)**

Source: Data adapted from National Statistical Institute (NSI), 2014

NER has experienced considerable changes in direct foreign investments (DFI) over the last years and in 2010 the region’s share in the total volume of attracted foreign investments (funds) for the country becomes 9,51%. The region ranks third in the country in 2010 by the size of the accumulated direct foreign investments (National Statistical Institute, 2015).

Despite the downward trend in DFI at a national level, leading districts in attracting investments are Varna – with the largest share of € 3105 and Targovishte – €1560 in 2012. The 2012s have seen a marked decline in the size of DFI in Dobrich reaching €1398, with the lowest one being in Shoumen - €590 of DFI.

Over the period 2012 to 2014 the tangible fixed assets (TFA) in the real sector in North-eastern region are quite variable. Varna and Dobrich are the districts experiencing considerable decline, which is, nevertheless, part of a nationwide trend. Observed in Targovishte and Shoumen is the inverse of the relationship. This should primarily be seen in the light of expansion or creation of new enterprises, and improved product marketing in the industry sectors and agriculture as well

(2013, 2014a, 2015).

**Table 1. Direct foreign investments euro/ person (on accrual basis)**

№	town	2012	2013	2014
1	Varna	1500599,7	1471179,2	1424057,7
2	Dobrich	233539,4	261811,9	299945,1
3	Targovishte	193503,9	186336,8	208880,9
4	Shoumen	91091,6	105668,7	108596

*Source:* Data adapted from National Statistical Institute (2013, 2014a, 2015)

**Table 2 Investments in TFS in NERP BGN/person**

№	town	2012	2013	2014
1	Varna	1091098	1012292	1129690
2	Dobrich	373192	328709	380718
3	Targovishte	156440	258311	319230
4	Shoumen	192565	256016	237943

*Source:* Data adapted from National Statistical Institute (NSI) (2014a)

### 2.3. Economic sustainability of SMEs in NER

A study into the main factors relevant to SME sustainable development was conducted through a survey among 30 enterprises from different sectors in NER's SMEs. The purpose was to make generalized assessments of the possibilities of the business environment to ensure conditions conducive for the development of SMEs in NER. The analysis covered a three- year-period from 2012 to 2014.

Within the scope of the conducted survey for the purposes of the present analysis, 48% of the entrepreneurs are with higher education, one third with secondary specialized, 18% with secondary and less than 1% — with primary education. On the basis of these considerations, it can be summarised that entrepreneurs with higher education are predominant among the industrial entrepreneurs (65%), while in trade they tend to be significantly underrepresented (39%).

Medium-sized enterprises have the greatest share of entrepreneurs with higher education (83%), followed by the small (63%), while in micro enterprises their share reaches 40%. The entrepreneurs with higher education are most prevalent in 35, 36-44 and 45-54 age groups. The age structure of the entrepreneurs is 20% up to 30 years, 50% from 30 to 50 years, 30% from 50 to 70 years.

The analysis shows that the educational level of the employed persons in the surveyed enterprises is as follows: 30% with primary education, 45% - secondary and 25% - higher (tertiary) education. A large part of the employed persons with secondary education are in the sphere of trade, services and industry, while those with primary education are employed primarily in the sphere of construction.

On the basis of the above information it can be said that 30% of the surveyed enterprises operate in the sphere of industry, 60% in the sphere of trade and services and 10% in other sectors.

Nearly 65% of the enterprises are export-oriented and have established foreign trade and international relations with countries such as Russia, Ukraine, the Netherlands, Romania, Greece, Turkey, etc. SMEs in NER have been exporting to Romania mostly fertilizers, and to Greece and Turkey timber materials and panels. A considerable part of the enterprises exporting goods and services to Russia and Ukraine have been badly affected by the conflict between the two countries. The enterprises undertaking export activities to these two countries face a decline in about 90%.

An increasingly important factor in the development of the local SMEs is the economic growth in countries such as China, Malaysia and Indonesia. More and more local companies switch to purchasing raw and other materials from China because of their low cost and the possibilities for higher profit margins. On the other hand, the poor quality of the raw materials greatly affects the

quality of the products. All this results in an increase in transportation costs and the number of complaints (warranty claims).

Another trend that became observable among surveyed enterprises is the reduction in the number of employed persons after 2009. 34,5% of the enterprises reduce the number of employed by 3 to 50 persons. The decrease is reported to be substantial among micro and small-sized enterprises, whereas with medium-sized this rate is 5,6%.

Analysis of the revenues from SME economic activities over the period 2009 to 2012 shows a downturn with the sharpest decline in 2009-2010 as a rebound from the effects of the economic crisis. It becomes evident that micro enterprises have failed to adapt to the changing environment and have difficulties in overcoming the impact of the economic crisis. In general, it is observed that the revenues from their business activities cannot cover their operating expenses (costs) and contribute to profit. With small and medium-sized enterprises there is only one activity generating losses - with small enterprises it is the hotel industry and catering industry or restauranturship, while with the medium ones - mining and quarrying industries.

In the North-eastern region the rise in revenues by 9,8% in the last two years is mainly due to increased returns by the large-sized enterprises. Changes in operating costs are comparable to the changes in revenues.

In NER - 65,5% of SMEs rely too heavily on bank finance, or funding sources from investment and other financial institutions, 57,9% on budgetary programmes, EU funds and other foreign financial assistance and 5% on (enterprise) owner's personal funds, loans from their relatives or friends. This explains why a high percentage of the enterprises, around 98,6%, identify access to financing as difficult or insufficient (European Commission, 2013).

On the basis of evaluation of the financial resources, intended to promote innovative activities, it can be said that 45% of the enterprises allocate funds for purchasing tangible fixed assets, 25% for training and human resources development, and 10% lack the appropriate funding. Half of the enterprises recruit highly qualified labour force for the purposes of innovation, research and development, 32% develop new product ideas and implement these ideas into practice, 13% create and maintain innovative infrastructure within the enterprise itself, and only 0,5% are engaged in innovation short- or medium-term activities in close collaboration with scientific and academic organisations.

The key indicators for economic sustainability, within a business context, as determined by the entrepreneurs, are the financial, market, manufacturing, technical and technological, and investment sustainability. Financial sustainability has been assessed on the basis of generalizing indicators such as liquidity, solvency, profitability and others. All surveyed enterprises have identified it as an indicator of paramount importance.

Market sustainability is assessed on the basis of a generalized assessment of change in sales volume, market share, stocks and others. 80% of surveyed enterprises have ranked this indicator with a high degree of importance and 15% with a moderate one.

As key factors of external environment suggested can be the following findings:

- ✓ 70% of the surveyed enterprises indicate the suppliers and their pricing policy;
- ✓ 73,9% of the enterprises single out the provision of materials at exactly the right time for their effective utilization;
- ✓ 95% of SMEs point out the level of the interest rates on bank loans;
- ✓ 85% availability of suitably qualified labour resources;
- ✓ 55% changes in normative acts or regulations;
- ✓ 79,7% consumer behaviour;
- ✓ 79,8% competitors' strategies and planned actions;
- ✓ 95% conflict between Russia and Ukraine;
- ✓ 96,8% China's economic development.

Among the surveyed SMEs in NER only 4,5% have risk assessment and crisis early warning systems. Basic measures the enterprises employ to withstand both risks and crisis situations are:

- ✓ development of products and services on a low-cost base;
- ✓ cost reduction;
- ✓ reduction in employment levels and consolidation of activities;
- ✓ marketing strategies - advertising, promotions, discounts, bonuses for loyal customers (diligent bill-payers), etc.

### 3. CONCLUSIONS

On the basis of the above analysis, we can formulate the following key conclusions and major proposals:

- a) SME development is of great importance for the district economy and for the achievement of sustainable economic growth through mobilization of their own potential and innovations, improvement of the quality of life, (availability of) employment and income (growth);
- b) SMEs enable the achievement of higher levels of employment, growth and productivity in NER;
- c) The main issues faced by SMEs are: difficulties in accessing financial resources, lack of highly qualified manpower, changes in normative acts or regulations, etc. For that purpose it is necessary for SMEs to be directed, during the new programming period, to a more efficient use of funding opportunities available through different EU funds and programmes;
- d) NER has the potential for further development of the basic industries (grounded in its underlying structure) – chemical industry, transport engineering, mineral product manufacturing industry, as well as agricultural and food industry on the basis of well-developed agricultural sector. SMEs should explore their appropriate niche, making use of the distinct advantages of the region;
- e) Creation and development of clusters, that might give rise to a future territorial and productional integration and involvement of smaller localities as elements of an economically effective and dynamically developing industrial activity.

It can be concluded that despite all the problems and negative trends in the development of regional economy, SMEs are still able to perform their full function and account for the considerable share of NER's GDP. Creating a SME - friendly environment and their encouragement (incentivizing) turns out to be of crucial importance for the provision of NER sustainable development. Hence, it is our strong belief that small and medium-sized enterprises play an important role in providing novel insights into the rapid and stable recovery of the national economy.

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