



OPPORTUNITIES AND CHALLENGES FACED BY SMALL AND MEDIUM ENTERPRISES IN UZBEKISTAN

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Abstract

Small and medium enterprises (SMEs) are a pillar of economic development in most national economies - both more and less developed. Enterprises of this type, being more flexible than large entities, are better able to use the opportunities created by the environment. Nevertheless, in the course of their activity, they also face numerous challenges. Thus, the purpose of the presented research is to identify the opportunities created and existing challenges in the development of SMEs in Uzbekistan in recent years. According to the opinion of 384 respondents (CAWI), the most important opportunities created by the government involved tax benefits and subsidies, preferences for export products and tax incentives for those creating new jobs. At the same time, the most important challenges were poor infrastructure, lack of skilled specialists, problems with the credit allocation system and high-interest rates.

SZANSE I WYZWANIA DLA MAŁYCH I ŚREDNICH PRZEDSIĘBIORSTW W UZBEKISTANIE

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Słowa kluczowe: małe i średnie przedsiębiorstwo, rozwój, polityka wsparcia.

Abstrakt

Małe i średnie przedsiębiorstwa (MŚP) są podstawą rozwoju gospodarczego większości gospodarek krajowych - zarówno tych bardziej, jak i mniej rozwiniętych. Przedsiębiorstwa tego typu, będąc bardziej elastycznymi niż duże podmioty, coraz lepiej wykorzystują możliwości jakie stwarza otoczenie. W toku swojej działalności często napotykają jednak na wiele zagrożeń. Celem badań przedstawionych w artykule była identyfikacja szans i wyzwań przed jakimi stoją obecnie małe i średnie przedsiębiorstwa w Uzbekistanie. Według opinii 384 respondentów najważniejszymi szansami stworzonymi przez rząd były ulgi podatkowe i dotacje, a także preferencje dla produktów eksportowych oraz zachęty podatkowe dla tworzących nowe miejsca pracy. Jednocześnie najważniejszymi wyzwaniami rozwojowymi była słaba infrastruktura, brak wykwalifikowanych specjalistów, problemy z systemem alokacji kredytów oraz wysokie stopy procentowe.

Introduction

Small and medium enterprises (SMEs) have numerous benefits to their owners and the economy (Brodziński *et al.*, 2020, p. 107). These entities play an important role in Uzbekistan economic growth and the current role of SMEs is highly growing. That is why the rapid development of SMEs is a key element in ensuring the sustainable growth of any country's economy and a priority of ongoing economic reforms. The development of SMEs leads to the creation of new jobs. SMEs are not only an important source of job creation in countries, they can also become a source of innovation and increased productivity (Hansjörg & Zeynep Mualla, 2018, p. 2). At the same time, SMEs face numerous challenges to their development which, in individual regions, leads to restrictions on their functioning (and sometimes to collapse), which also affects the negative development of the entire economy (Glinkowska, 2019, p. 101-112).

The latest statistical data show that in Uzbekistan, the share of employment by SMEs was 73.8% of the total employed population (State Committee of the Republic of Uzbekistan on Statistics, 2020, Q4, p. 1). The success

of an entrepreneur depends on several social-economic, political and technological environmental factors (Firdouse, 2014, p. 89-94).

In recent years, Uzbekistan has been paying great attention to the development of SMEs. Many decisions and decrees have been made in the last three years. For example, the position of Business Ombudsman was introduced, the Prime Minister's Representative in all provinces to assist entrepreneurs, the State Fund for Entrepreneurship Development (200 billion, 50 million Uzbekistani som, which is equivalent to approx. USD 20,000,000) and the Agency for Entrepreneurship Development were established (Uzbekistan National News Agency, 2019). However, many problems in Uzbekistan hinder the development of SMEs, one of them is the poor development of the market infrastructure and a lack of specialists in the field of SMEs (OECD, 2017, p. 1-45).

Although many researchers have conducted research on SMEs in Uzbekistan, little attention has been paid to topics related to SMEs' opportunities and challenges. According to many scientists (Jimmy & Pauric, 1999, p. 5; Madalina, 2013, p. 205; Kubičková *et al.*, 2017, p. 1987; Gherghina *et al.*, 2020, p. 2), small enterprises are an important part of the world economy. For this reason, many researchers have conducted research on the practices and activities of these enterprises. Although the Uzbekistan government is creating opportunities for SMEs, there are still many challenges, which have not been precisely identified. Therefore, the authors focus on filling this gap and the purpose of the presented research is to identify the opportunities created and the existing challenges in the development of SMEs in Uzbekistan in recent years. Moreover, the practical contribution of this article is not only limited to the identification of opportunities and challenges, but it also includes a comparison between these two factors.

Small and medium enterprises in Uzbekistan

The Resolution of the Cabinet of Ministers of the Republic of Uzbekistan "On measures of transition to the international system, classification of types of economic activity" has indicated the differences between micro and small enterprises. Micro-enterprises consist of 1-5 people, 1-10 people, and 1-20 people, small enterprises consist of 5-25, 11-50 and 21-250 people. For example, micro-enterprises in manufacturing (food production) consist of 1-20 people, and small enterprises in manufacturing (food production) consist of around 21-250 people. Micro enterprises in transportation and storage consist of 1-10 people, and small enterprises in transportation and storage consist of 11-25 people. There is no normative data to determine medium-sized enterprises. According to the information given by the World Bank, the sizes of SMEs in Uzbekistan are: a) small enterprises have 5-19 employees, b) medium enterprises have 20-99 employees, and c) large enterprises have 100+ employees. SMEs in Uzbekistan are not defined based on clear criteria that are consistent with

international practice. In international practices, SMEs should also include annual turnover and characteristics of the industry along with the number of employees (Tadjibaeva, 2019, p. 2). The result of the above studies show that micro-firms contain 1-20 people, small enterprises contain 21-100 people and medium-sized enterprises contain 101-250 people.

At present, the number of SMEs in Uzbekistan is 334,800 (without agricultural farms) and the number increased by 56.73% in 2020 Q2 compared to 2014. The number of SMEs is based on the type of economic activities in the following sectors: 28,800 in agriculture, forestry and fisheries; 70,000 in industry; 36,000 in construction; 100,600 in trade; 15,200 in transportation and storage; 25,500 in housing and food; 7,600 in information and communication; 6,400 in health and social services; and 44,700 in other specialties (State Committee of the Republic of Uzbekistan on Statistics, 2020, Q2). In Q1 2020, 23.3 thousand new SMEs were newly created (without agricultural farms), which is 23.4% less than the same period in 2019 (State Committee of the Republic of Uzbekistan on Statistics, 2020, Q1, p. 182).

Literature review

SME development is highly related to a favourable investment atmosphere, public consumption levels and geographical locations (Eravia *et al.*, 2015, p. 96). Some researchers (Scott *et al.*, 2017, p. 1-32) have identified a number of opportunities to support SMEs. These include training and business development support, innovative financing to address the financial problems of at-risk SMEs, as well as the allocation of targeted fiscal packages and others. As major consumers of goods and services, governments have an opportunity to support SMEs directly through their purchasing policies (Loader, 2005, p. 17). Technological advances and the development of e-commerce have opened up vast opportunities for SMEs as well as offering new foreign markets. However, restrictions on the financing of SMEs, tight profit margins and difficulties in innovation hinder the development of SMEs (Luo *et al.*, 2019, p. 2999).

Many researchers have investigated in detail the opportunities created for SMEs in their country. For example (regarding the Asian continent), according to Rahadi (2016, p. 51) opportunities for SMEs in Indonesia are indicated by market potential, creativity, export opportunities and the availability of local knowledge about the market. That study indicated that the main strength of Indonesian SMEs was in their creativity, i.e. the production of unique and new products leading to an advantage in a competitive environment in the market. This would be effective for SMEs in increasing the annual assets and sales growth when government diagnostic and support services are combined with government loan financing (Soonae *et al.*, 2020, p. 213-238).

SMEs are a key pillar in the development of the Asian economy since they cover more than 96% of all Asian businesses. However, there are many challenges for the growth of SMEs on this continent. The lack of a database, underdeveloped sales channels, the problem of asymmetric information between suppliers and demanders of funds and high-interest rates on bank loans lead to the slow growth of SMEs (Yoshino & Taghizadeh-Hesary, 2016, p. 17; 2018, p. 15). Wang (2016, p. 167-176) has identified five obstacles for SME managers. Among them, “access to finance” is the greatest barrier. That study analysed the impact of internal and external factors on the access to finance for SMEs and found that the most serious constraints for SMEs in need of external funding were high-interest rates, complex application procedures and high collateral requirements. According to Petković *et al.* (2016, p. 45), obstacles in the successful development of SMEs are due to the difficulties in the collection of receivables from debtors, high tax rates, and the difficulty in obtaining loans from banks. The results of a study by Aliyev (2019, p. 36), have shown that bank loans are beneficial for SME enterprises, however, the low level of financial literacy of entrepreneurs and high tax rates limit SME financing opportunities. Challenges related to financial factors have been observed by many researchers. Mainly, the lack of access to finance is seen as one of the important factors hindering SME innovation. Of course, there are other factors as well. For example, Yadollahi Farsi and Taghi Toghraee (2014, p. 1-15) have identified several challenges which are exploratory factors. Some of these include:

- lack of management skills: as a result of this, entrepreneurs may not be prepared for changes in the business environment and innovative developments;
- lack of credit: due to the lack of access to credit, entrepreneurs may have a lack of free choice, i.e. they are forced to buy old, obsolete equipment instead of using innovative technologies;
- regulatory environment: the activities of SMEs are affected by unexpected government policies, as well as corruption.

Factors hindering the development of SMEs are the lack of skilled human resources, high interest rates (Eravia *et al.*, 2015, p. 96), unsatisfactory food hygiene, a lack of sustainability practice (Noor Hasnan *et al.*, 2014, p. 328-336), a low level of management skills for continuous improvement, a lack of motivation for employees (Maarof & Mahmud, 2016, p. 522-531), a high cost of raw materials and a high initial cost of investment (Musa & Chinniah, 2016, p. 254). The external financing provision for SMEs is also still low (Eniola & Entebang, 2015, p. 334-342). The challenges for SMEs in developing countries consist of limited access to long-term and affordable finance and a lack of institutions for the developmentally skilled class of entrepreneurs and workers (Hansjörg & Zeynep, 2018, p. 34). The observed challenges for SMEs in India are the procurement of funds, infrastructure development, government policy and raw material procurement (Agarwal *et al.*, 2019, p. 33). In Malaysia, there are five major barriers for SMEs. These include financial issues, human resource

problems, marketing strategies, facilities, appliances, layout and problems with suppliers (Azwa Ambad *et al.*, 2020, p. 13).

Research methodology

Since the study focuses on SMEs, especially in developing countries, the research is based on the SMEs in Uzbekistan as the population of interest. Due to a limitation on collecting information from the entire population, a sample size was selected. However, for this research, convenience sampling was chosen as it was believed to be the most effective. In identifying the sample size for this thesis, a formula by Cochran (1977) was used. Using this formula (for a confidence level of 0.95, and a maximum error of 0.05), a minimum sample size of 384 subjects was obtained.

The data collected was from both primary and secondary sources. The primary data set that was gathered in this study was inspected several times so that there would be no errors when it came time to analyse it in the system. The data that had been collected for the content analysis was processed by the use of descriptive writing, in addition to making use of tables and statistical information when necessary.

A questionnaire was used as a survey instrument to generate primary data. The questionnaires were distributed through the Auditor firm (Amulet-Audit Auditing Company LLC in Tashkent was established on March 23, 2008, and currently employs about 10 auditing specialists). The created questionnaire was entered into Google Forms and a link was sent to the auditing firm via email and telegram. The questionnaires were sent out by the Auditor to the respondents (who were the managers of SMEs). The auditors also monitored the return of the questionnaires and reminded managers to submit them (in order to obtain the required number of returns). The questionnaires were collected between October-December 2020. In order to check the reliability of the questionnaire, the Cronbach's alpha coefficient was used (mean = 0.8). The questionnaire consists of two sections. The first section contained eight questions that were meant to collect general information about SMEs that included their activities, number of workers, workers' salary scale, workers' education level and so on. The second section contained two questions which included opportunities and challenges for SMEs. At the same time, the opportunities in the study were limited to those that were created by the public policy conducted in relation to this sector of the enterprise (through financial and non-financial support).

The following section addresses the statistical tests that were conducted. Some of the tests included descriptive statistics, frequencies and cross-tabulation. The results were then illustrated in pictures that were created following the coding of the researcher.

Results

A total of 384 SMEs were sampled, of which 74 SMEs (19.2%) employed 1-10 workers, 185 SMEs (48.2%) employed 11-50 workers, 81 SMEs (21.1%) employed 51-100 workers and 44 SMEs (11.5%) employed 101-250 workers. The majority of the respondents belonged to the service (54.4%), manufacturing (23.4%) and construction (13.3%) industries; while other enterprises constituted 8.9%.

The survey results show that the number of workers employed by beginning entrepreneurs was mainly 1-10 (76.6%) and 11-50 (18%). A considerable number of entrepreneurs who started a business with 1-10 employees developed to employ from 11 to 50 people (Tab. 1).

Table 1

Size of the enterprises according to number of employees

Specification	Number of employees when start a business							
	service	manufac- turing	trading	agricul- ture	textile	construc- tion	education	total
1-10	158	78	12	6	10	24	6	294
11-50	51	12	0	0	0	6	0	69
51-100	0	0	0	0	0	21	0	21
101-250	0	0	0	0	0		0	0
The number of employees at present								
1-10	48	7	4	0	0	9	6	74
11-50	116	61	0	2	2	4	0	185
51-100	34	17	6	4	5	15	0	81
101-250	11	5	2	0	3	23	0	44

Sources: own study.

Most of the workers received a salary between USD 200-500. In some services (construction and manufacturing enterprises) employees received salaries between USD 500-1,000. Wage levels by sector of the economy are presented in the Table 2.

Table 2

The level of employees' wages

Specification	Salary amount in USD							
	service	manufac- turing	trading	agricul- ture	textile	construc- tion	education	total
Less than 200-300	63	19	0	6	0	7	6	101
Between 300-500	138	30	9	0	10	15	0	202
Between 500-1,000	8	41	3	0	0	29	0	81

Sources: own study.

Forty-seven percent of employees of SMEs were bachelor's degree holders (180), 38.3% were diploma (college) holders (147), 12% were master's degree holders (46) and 2.9% were Ph.D. holders (11) (Tab. 3).

Table 3

Employees' level of education

Specification	Number of employees by level of education							
	service	manu- facturing	trading	agricul- ture	textile	construc- tion	education	total
Diploma (College)	67	32	0	5	8	35	0	147
Degree (Bachelor)	118	37	12	1	2	10	0	180
Masters	17	21	0	0	0	6	2	46
PhD	7	0	0	0	0	0	4	11

Sources: own study.

39.6% (152) of SMEs are expected to increase the number of employees to 1-10 in three years, while 29.4% (113) of SMEs are expected to increase the number of employees to above 11-50 in three years. 13.3% (51) of SMEs are anticipated to increase the number of employees to above 51-100 in three years and 17.7% (68) of SMEs are not expected to increase the number of employees in three years (Tab. 4).

Table 4

Future employment plans

Specification	Number of employees to which it is planned to increase employment							
	service	manufac- turing	trading	agricul- ture	textile	construc- tion	education	total
Unexpected	49	6	9	0	2	0	2	68
Expected until 1-10	133	12	1	6	0	0	0	152
Expected until 11-50	27	33	2	0	8	39	4	113
Expected until 51-100	0	39	0	0	0	12	0	51
Total								384

Sources: own study.

It should be noted that those entrepreneurs who do not plan to increase employment have two options (keep employment at the same level or reduce it). None of the surveyed entrepreneurs intended to increase employment by more than 100 people.

Overcoming the challenges for SMEs depends on the opportunities and support that the government has created for SMEs (OECD, 2018, p. 1-4). Figure 1 shows the opportunities created by the government in the development of SMEs. Most of the enterprises (181, i.e. 47.1%) received tax benefits and subsidies from the government, of which 33.8% were service enterprises, 5.9% were manufacturing enterprises and 7.4% were construction enterprises. Sixty-two SMEs (16.2%) were granted preferences by the government for product export, of which 5.9% of SMEs were service enterprises, 4.4% of SMEs were manufacturing enterprises and 2.9% of SMEs were textile enterprises. Fifty-six SMEs (14.7%) were offered tax incentives by the government to create new jobs, of which 5.9% of SMEs were service enterprises, 5.9% of SMEs were manufacturing enterprises and 2.9% of SMEs were construction enterprises (Fig. 1).

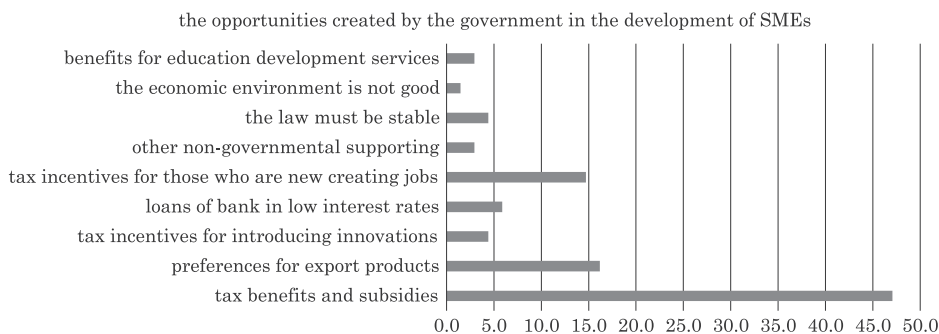


Fig. 1. Frequency analysis of respondents by opportunities created by the government in the development of SMEs

Sources: own study.

All of these opportunities in Uzbekistan belong to financial support given to SMEs by the government.

The main challenges of Uzbek SMEs consist of a lack of skills, poor infrastructure, financial difficulties and legal issues. In SMEs, challenges related to expertise such as lack of entrepreneurial skills (10.3%), weakness of financial management (10.3%) and lack of strategic planning (4.4%) can be seen. Financial challenges for SMEs were observed, such as higher tax rates (4.4%), problems related to the credit allocation system (8.8%) and only certain groups could use tax and customs benefits (10.3%). Legal challenges for SMEs were related to legal uncertainty, which was confirmed by 13.2% of respondents. The main obstacle to the development of SMEs in Uzbekistan is the poor development of market infrastructure and other infrastructure. These challenges were observed in 30.9% of SMEs (Fig. 2).

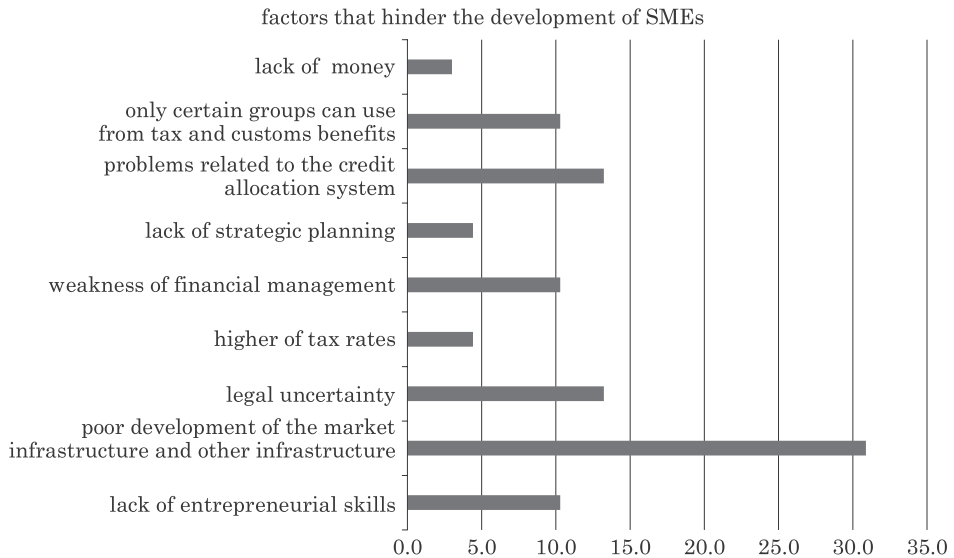


Fig. 2. Frequency analysis of respondents by factors that hinder the development of SMEs
Sources: own study.

The cause of the failure of most entrepreneurs in Uzbekistan is a lack of entrepreneurial experience, poor financial management, over-investment in fixed assets and lack of marketing experience, among others (Saidova, 2018, p. 138-142).

Discussion

According to the Statistics, in 2020 Q2 the average monthly nominal accrued wages in Uzbek SMEs amounted to USD 250. This increased by 26.5% compared to the corresponding period of 2019. The higher the level of knowledge of employees and their motivation to work, the higher the quality of the work performed. The level of education has a positive impact on the profitability of the business (Chiliya & Roberts-Lombard, 2012, p. 468). The study found that most SMEs have bachelor and diploma (college) degrees. This shows that the level of education of employees working in SMEs in Uzbekistan is high and medium. It is recommended to increase the level of education of medium-level workers.

In recent years, the government of Uzbekistan has created many opportunities for the development of SMEs. The survey was conducted during the coronavirus pandemic period and the results show that the government has been providing more financial support to SMEs. The measures to provide legal protection and financial support to business entities have also been strengthened. A decree

by the President of the Republic of Uzbekistan “On further measures to support the population and businesses during the coronavirus pandemic” was adopted. The decree reflects the opportunities for business entities such as reducing the tax burden through tax exemptions, write-offs of fines and penalties, tax deferrals and other measures to support entrepreneurs.

The survey results indicate the following four factors influence the failure of SMEs in Uzbekistan.

Poor infrastructure: The findings have shown that one of the biggest challenges for SMEs in Uzbekistan is the weakness of market infrastructure and other infrastructure. The studies of other researchers in explaining these problems more clearly were included. The results of research conducted by the Central Bank showed an increase in some factors that prevented the more efficient use of production capacity. For example, in 2020, when compared to 2019, problems related to the electricity and natural gas supply had increased by 3 percent. The Central Bank study highlighted the problems of power supply and natural gas infrastructure in Uzbekistan (Central Bank, 2020). There are also challenges associated with logistics, market and road infrastructure in Uzbekistan. One of the obstacles to creating a competitive logistics sector is that the de-monopolization of a number of enterprises and the liberalization of foreign trade policy is very slow (Akbaraliev *et al.*, 2019a, p. 5). The challenges of market infrastructure in Uzbekistan include insurance companies, audit firms, trading houses, consulting centres, business centres and so on.

Lack of skills: The lack of entrepreneurial skills, weakness of financial management and a lack of strategic planning negatively affect SME development in Uzbekistan. This lack of skills depends on several influencing factors, such as low level educational systems, a lack of HRM, illegal expenditures, etc. For example, the violation of budgetary discipline and other illegal expenditures (a total of 81.7 billion Uzbekistani som, which is equivalent to approx. USD 8,019,802) were identified by the Department of State Financial Control of the Ministry of Finance and its territorial departments in the first half of 2020. Nine billion Uzbekistani som (equivalent to approx. USD 891,089) were detected as being illegal expenditures belonging to the Ministry of Public Education and 6.9 billion Uzbekistani som (equivalent to approx. USD 683,168) belonging to the system of the Ministry of Education. Such illegal activities inevitably affect the development of the education system.

Legal uncertainty: The adoption or amendment of many laws in recent years has led to a misunderstanding of the law among some entrepreneurs. For example, changes in the tax system has led to misunderstandings concerning certain types of taxes for entrepreneurs, which can be seen as a number of problems among entrepreneurs in calculating value-added tax. The findings have indicated that there are legal uncertainty challenges for SMEs in Uzbekistan. The first reason for such legal uncertainties is the low level of experience and skills of entrepreneurs. Because such shortcomings can lead to a poor understanding

of normative documents, there is often a failure to use the opportunities provided by the government. Secondly, the existence of normative documents that focused on single operations that differ from each other or the absence of normative documents leads to legal uncertainties. But there is no clear evidence as to whether such problems exist. Therefore, it is necessary to conduct an in-depth analysis and compare the normative documents related to SMEs.

Financial problems: Some SMEs are facing financial difficulties that depend on the credit allocation system and higher tax rates. High-interest rates and excessive bureaucracy reduce the opportunities for entrepreneurs to access loans. Entrepreneurs try to utilize their own funds more than loans and this decreases the quality level of products and services. High tax rates can lead to tax avoidance by entrepreneurs (it creates a shadow economy) or bankruptcy due to an inability to pay taxes.

Nearly 78% of enterprises that participated in the survey were given various tax benefits by the government. Notwithstanding, about 88% of these enterprises faced challenges involving poor infrastructure, lack of skills, legal uncertainties and financial problems.

Conclusions

The development of SMEs is critical to supporting economic growth in Uzbekistan. This paper analysed the opportunities and challenges faced by SMEs in Uzbekistan. In recent years, Uzbekistan has created many opportunities for the development of SMEs. This is evidenced by the fact that the number of SMEs and their share in GDP is growing from year-to-year. The results show that the government has been providing entrepreneurs tax benefits and subsidies, preferences for export products and tax incentives for those who are creating new jobs.

In addition to the opportunity to grow, as with any existing business, SMEs also face several challenges, such as poor infrastructure, lack of skilled specialists, problems with the credit allocation system, high-interest rates, and others. Uzbekistan should analyse these challenges and investigate every single factor and cause (Akbaraliev *et al.*, 2019b, p. 5). This would involve many specific approaches, including analysing major obstacles affecting the improvement of infrastructure and the educational system, attracting investors to the private sector, the simplification of the credit system, the reduction of interest rates and, finally, a reduction of the power of monopolies in certain business sectors.

As with any study, some limitations must be acknowledged. First, it was planned to conduct the survey in each region, but the limited scope of the opportunity and difficulties of reaching respondents made the entire research work challenging. Secondly, we studied the opinions of respondents (entrepreneurs,

managers), which may be subjective. Of course, the respondents know their own enterprises very well, but it would be advisable to supplement future research with objective financial indicators.

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