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SMALL AND MEDIUM SIZED ENTEPRISES DURING THE COVID-19 PANDEMIC CRISIS – PROBLEMS AND CHALLENGES

Abstract: Small and medium enterprises are the backbone of economic development. They have huge contribution for employment, utilization of entrepreneurial abilities, rational use of national and local resources, the creation of added value and the inclusion of the national economy in world trade through their internationalization. Their importance is due to their characteristics such as flexibility and rapid production reorientation, entrepreneurial orientation, and especially their creativity and innovation.

In the last two years, the world has been facing with a pandemic that has had major and serious consequences for human health and economy. Actually, the COVID-19 pandemic is a global phenomenon with unprecedented impact on individuals, communities, and organizations. There is no doubt that there is no segment of the society that was not under the pressure of the global pandemic. The COVID-19 pandemic crisis, has already become a permanent part of the 21st century and it cause a significantly changes in businesses operations. SMEs are facing with numerous challenges and problems as a consequence of the pandemic. Many studies shows that the competitive advantage of any modern enterprise is based on ability for innovation in products or production processes. Only through innovation SMEs will increase their and competitive advantage of the national economy. Considering this the focus will be on the innovation strategy and its necessity for overcoming the conditions and consequences caused by the pandemic.

The main aim of the paper is to identify the basic problems and challenges of small and medium sized enterprises during the corona virus pandemic in developing countries, specifically in North Macedonia, as well as strategies of transformation and adaptation to changes in the environment. To achieve the aim a survey will be conducted to the sample of SMEs in North

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Macedonia. At the end of the paper based on the obtained results we will provide recommendations for small and medium businesses on how to remain flexible or competitive through resilience and renewal strategies.

Key words: SMEs, pandemic, strategy

JEL classification: D2, O3,

Introduction

SMEs in EU represent 99% of the total number of enterprises. Their development allows us to feel their effects on the macroeconomic performance in terms of employment, production growth, strengthening competition and, entiresocial and human development. Therefore, the policies to promote the development of SMEs are common in both developed and developing countries. Nowadays, SMEs are the key driver of economic growth. They play an important role in creating employment, adding value and exports. Considering this fact, it is necessary to implement appropriate strategies that will enable SMEs growth and development. At the beginning of 2020, the world faced major challenges due to the COVID-19 pandemic. To stop the spread of the infection, the governments of the countries had to impose various restrictive measures and lockdowns. The COVID-19 pandemic created problems for the SME sector and consequently threatened the development of the countries' economies.

Considering this the main aim of the paper is to identify the basic problems and challenges of small and medium sized enterprises during the corona virus pandemic in the Republic of North Macedonia, as well as strategies of transformation and adaptation to changes in the environment, with special reference to the importance of innovation and innovation strategy. Section 2 deals with some previous work on this topic. Section 3 gives theoretical overview for SMEs. Section 4 gives information about the SMEs importance in Macedonia and the condition during pandemic. Section 5 provides insights into the data, methodology, and results of the analysis. The last section concludes conclusion and recommends.

Literature review

The repercussions of the COVID-19 pandemic have been felt across all economic sectors and institutions, including small and medium enterprises (SMEs) (Hasanat et al., 2020).¹ Many studies have shown that SMEs are confronted with various difficulties and challenges due to the COVID-19 pandemic. On the other hand SMEs are crucial sector for economy development. To protect this vital sector from collapse due to the COVID-19 crisis, many

¹ Hasanat, M. W., Hoque, A., Shikha, F. A., Anwar, M., Hamid, A. B. A., & Tat, H. H. (2020). The impact of coronavirus (Covid-19) on E-business in Malaysia. *Asian Journal of Multidisciplinary Studies*, 3(1), 85–90.

governmental and nongovernmental organizations (NGOs) have provided various forms of support to SMEs (Nawal & Ghadah). Governments have adopted several policies that will mitigate the negative effects of this crisis (Ahmd et al., 2020). SMEs have received some financial support from local and international NGOs and financial institutions during the COVID-19 crisis (Song et al., 2020).

Additionally, SME owners have adopted a number of practices and strategies to confront the ramifications of the crisis (Thorgren & Williams, 2020). The appropriate use of innovation strategies can create additional value for customers and shareholders and increase enterprise competitiveness (Baker, Grinstein, & Harmancioglu, 2015) (Rubera & Kirca, 2017). Innovation can also lead to increased organizational performance and revenue as business leaders develop and implement more efficient and effective processes for reducing costs or facilitating the development of better products (Chowhan, 2016) (Simester, 2016).

Theoretical background for SMEs

The last decades of the 20th century brought a change in the production philosophy of the world most developed countries, whereupon the era of gigantic corporations has been replaced with the era of small enterprises, which promote the creative spirit and individualism, against the standardization and globalization promoted by the big and multinational corporations.

Considering the fact that small and medium enterprises are a heterogeneous group, it is hard to determine a single criteria or a unique combination of criteria, which will give a definite and unique response. There is no single, uniformly accepted definition of a small firm. In that way, European Commission has given the definition for SME, and according to the last modification (in 2003), these are the quantitative criteria: number of employees, annual turnover and annual turnover and annual current assets.²

The qualitative aspect of determining the SME's takes into consideration the following criteria:³

- SME's are considered those business entities where the employees know each other and on that way act as a team, and not as group of individuals;

² <http://ec.europa.eu>

³ Stefanović I., Milišević D., Miletić S. (2009). Significance and development problems of SME's in contemporary market economy. *Serbian journal of management, 2009*

- centralization of the decision making (usually the owner is a top manager who must approve all decisions. This can cause serious problems when the business entity will develop, because one person cannot be responsible for all activities);
- low level of specialization, where the employees have wide range of tasks to perform, particularly at those business entities that operate in unpredictable and dynamic conditions;
- intuitional and informal strategy, where the management is oriented toward short-term planning;
- informal communication channels and external communication, because the internal communication is horizontal or vertical and bounds the initiatives and the ideas of the employees, while the external communication enables easier exchange of information between suppliers and buyers.

The key characteristics that small and medium enterprises need to possess are: flexibility; independence; proximity in business relations; great opportunities for creation of new jobs; the creativity among individuals and realization of their ideas, adapting to market needs and so on.⁴ The main advantages of SMEs are: greater flexibility and increased response capacity to adjust to market changes; their decisions are quick and prompt; have simple and low level hierarchical structure, so the control and other functions are accomplished immediately; usually the small enterprises due to its big number, contribute to maintaining a satisfactory level of competition, and therefore for development of products and services that meet customers needs; better access to information on the market; because of its flexibility, small enterprises have possibility continuously to innovate, introduce new products on the market, services or promotions without greater risk, compared to big companies which have complex organizational structure and extensive production program; increased ability for correction of the mistakes; the tasks in small and medium enterprises are executed with team work; compared to big companies they have greater productivity of the employees, because the communication with the management team is direct and positively impacts on their motivation.⁵

However, despite their advantages, it mustn't be neglected the shortcomings of their operation: lack of working capital and difficult access to it;

⁴ Suklev B., *Management of small business*, Faculty of economics- Skopje, 2006

⁵ Tomash R.(2010). *Applied economy*. Faculty of economics. Banja Luka.

lack of specialization; lack of effective management; high fixed costs resulting from the individual manufacturing; difficulties in mobilizing of highly skilled staff; undiversified project portfolio; the systemic information they dispose are fragmented; limited access on foreign markets because of the lack of resources for investment and access on foreign markets, as well as for production of an assortment of products aimed for foreign markets.

Many studies show that in the dynamic surrounding the competitiveness of small SMEs depends by the speed by which new products are introduced on the market and the costs for savings and improvements for them to be made. The innovations significantly contribute to increasing the productivity and quality of products and services, making companies more competitive. Really, they imply major changes in the company but if the subject does not change the products or services it offers, as well as the way they are created and delivered, then there is a risk other company to do that. Today, exist only the businesses that are capable of accurately targeted and constant change.

According to Paul Almeida professor at Georgetown University “SMEs play a unique, active and crucial role in the innovation process, technological advances and improving the high-tech information networks.

Usually, the innovations are divided as: product innovation, process innovation, marketing innovation and organizational innovation. An innovation strategy should determine what types of innovation should be pursued. It should also align activities in relation to core innovation goals and the key competitive advantage that the company is trying to gain. A vital element in this strategy is the relationship between creating and capturing new value.⁶

Therefore, a firm can have one of the sixteen possible innovation strategies at a given point in time. The strategies are: non-innovative; doing only product innovation in year; doing only process innovation in year; doing only marketing innovation in year; only organizational innovation in year; doing product and process innovations in year; doing product and marketing innovations in year; doing product and organizational innovations in year; doing process and marketing innovation in year; doing process and organizational innovations in year; doing marketing and organizational innovations in year; doing product, process and marketing innovations in year; doing product process and organizational innovations in year; doing product, marketing and organizational innovations in year; doing process, marketing and organizational

⁶ Chapa R. T., Implementing an innovation strategy in WCO; responding to disruptive events. World Customs Journal, Volume 14, Number 2

innovations in year; doing product, process, marketing and organizational innovations in year. The most popular ones are: (1) only product, (2) only process, (3) only marketing, (4) only organizational, (5) both product and process, and finally (6) all four types of innovation.⁷

SMEs during COVID - 19 pandemic

SMEs are facing with numerous challenges and problems as a consequence of the pandemic. The period of closure and movement prevention policies adopted by governments in many countries have greatly affected SMEs, paralyzing their operations, weakening their financial positions, and exposing them to financial risk. SMEs have suffered from a shortage of workers and production inputs because of distortions that marred supply chains, which negatively affected their sales and their ability to fulfill their financial obligations and pay employees' salaries. This problem has coincided with a decrease in consumer spending because of the reduction in consumers' income and widespread feelings of uncertainty. As a result, many SMEs found themselves incapable of dealing with the situation and some of them have stopped their activities and remained closed since the first months of the outbreak. Today, SMEs are forced to look for strategies in order to survive and to create existential prognoses of business operations during great economic and social uncertainty.⁸

In the Republic of North Macedonia, SMEs are also significantly affected by the consequences of the pandemic and on the other hand, they have a significant role for the economy and economic development in the country. In Macedonia according to the preliminary data of the State Statistical Office, the number of active business entities in 2021 was 72 922 and compared to 2020 it decreased by 0.2%. The data on the structure of active business entities by sections of activities show that the sections with the highest share in the structure in 2021 were Wholesale and retail trade; repair of motor vehicles and motorcycles with 30.0% and Manufacturing with 10.9%. The data on the structure of active business entities according to the number of persons employed show that the highest share of 82.0% belongs to business entities

⁷ Karlsson Ch., & Tavassoli S., Innovation strategies of firms: What strategies and why?. *The Journal of Technology Transfer*, 2016

⁸ Nawal A. A. & Ghadah A., (2021), Innovation practices for survival of small and medium enterprises (SMEs) in the COVID-19 times: the role of external Support, *Journal of Innovation and Entrepreneurship*.

with 1-9 persons employed, followed by business entities with no persons employed or entities with unascertained number of persons employed (no data on persons employed) with 8.2%, and entities with 10-19 persons employed with 4.5%. The share of entities with 20-49 persons employed was 3.0%, those with 50-249 persons employed participated with 2.0%, while entities with 250 or more persons employed had a share of only 0.3%. SMEs in Macedonia are known as job creators, in 2019 namely they create 73,5% of employment and participate in the creation of added value with 65,7%. In 2020, overall SME value added declined by 8.6%. The downturn was particularly pronounced in the accommodation and food services sector, with SME value added falling by 10.2%. The wholesale and retail trade sector, the largest sector in terms of SME value added, was also affected, albeit not as severely, with value added down 1.8%. In 2019, SMEs accounted for 65.7% of overall value added and 73.5% of overall employment, far exceeding the respective EU averages of 53.2% and 65.0%. However, SME productivity, defined as value added per person employed, was only EUR 10 900, around one quarter of the EU average of EUR 42 600.⁹

The table below shows key strengths and key challenges related to SMEs in Macedonia.

⁹ https://ec.europa.eu/neighbourhood-enlargement/system/files/2021-09/north_macedonia_-_sme_fact_sheet_2021.pdf

Table 1: Strengths and challenges of SMEs in North Macedonia

Key strengths	Key challenges
<p>* The government has managed to remove some administrative and regulatory barriers over the last decade, as reported by the World Bank's Doing Business Report. The number of tax payments has seen a significant decrease and now stands at 7 – this is 3 less than the EU average and 33 less than a decade ago. In addition, North Macedonia's businesses only take 119 hours a year to pay taxes – 54 less than the EU average.</p> <p>* According to the National Employment Agency, the number of startups that create new job openings has increased in the last 3 years with an average annual growth rate of 7.38% over this period.</p> <p>* According to the State Statistical Office, the number of innovative SMEs increased by 53% in 2014-2020. In recent years, the government has launched several measures to support innovation in SMEs and start-ups, including grants to support innovation activities in start-ups or low-interest credits to help SMEs with technological investment. The effectiveness of this support needs to be evaluated</p>	<p>* According to the National Bank of the Republic of North Macedonia, the country lags behind EU Member States in the share of private equity funding and non-banking sources available to innovative SMEs and entrepreneurs, such as venture capital, equity, mezzanine financing and business angel financing.</p> <p>* According to the State Statistical Office, SMEs' contribution to the economy's export performance is becoming less significant. In 2018, SMEs provided 26.7% of exports, while in 2016 their exports represented 31.2% of the total. Private sector representatives indicate that corruption is a significant challenge that continues to hamper SMEs' capacity to do business.</p> <p>* According to data from Transparency International's 2020 Corruption Perceptions Index, people's perceptions of public sector corruption in the country have been worsening since 2014.</p>

To overcome the consequences of the pandemic, the Government of Northern Macedonia prepared six packages of economic measures to support businesses and individuals, but still they proved to be insufficient.

Research

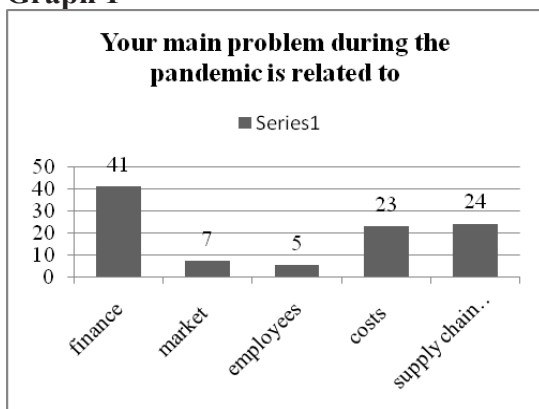
In order to give new prospect to this issue, a survey on small and medium businesses was carried out in April 2022. The survey comprised 55 SMEs from North Macedonia, and there were 50 questionnaires. The businesses that were part of the research are usually from the manufacturing industry and wholesale and retail trade. All respondents were managers responsible for day-to-day business processes – usually the entrepreneur, and otherwise a general manager. Most of the questions were set using a 5-point Likert scale anchored by strongly disagree to strongly agree. The questions were divided into fourth groups. The first set of questions concerns general company data. The second group is questions related to the problems of SMEs during pandemic. The third group of questions are related to technological changes and the anticipation of the importance of innovation. The fourth set of questions is related to the measures taken by the Government in order to overcome the problems of SMEs.

Research results

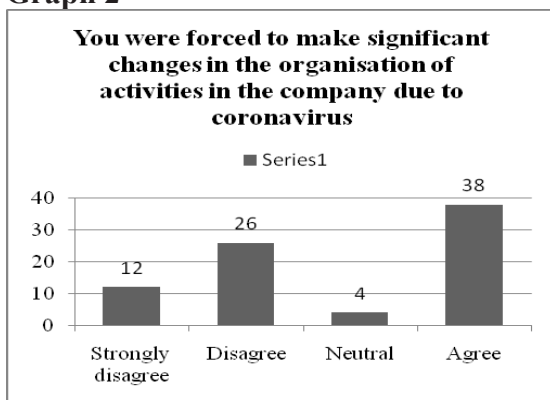
On the basis of data analysis from the first group of questions, the following results have been obtained: from the businesses-respondents, 36 were registered before 2010, and 14 were established after 2010, which means that the number of surveyed firms older than 10 years. Most of the respondents, i.e. 39% are small businesses, 7% micro and 54% medium businesses. The managers of the businesses that were part of the survey had more than 10 years of work experience.

The second group of questions is related to the problems of SMEs during pandemic.

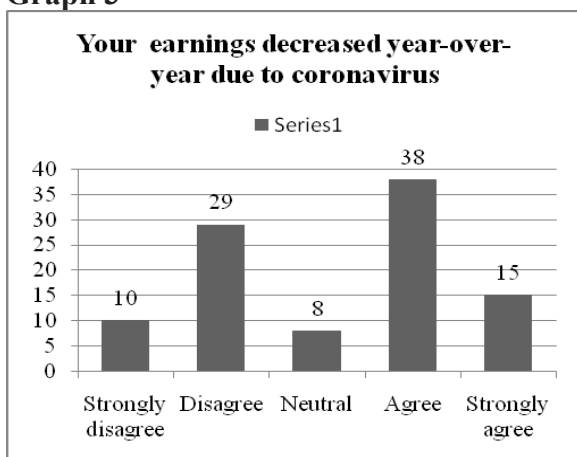
Graph 1



Graph 2



Graph 3



As can be seen from the data of the graph 1, the key problems of SMEs during the pandemic are related to finances, and 41% of respondents replied that finances are their main problem, 24% think the problems associated with the supply chain activities are most significant, 23% cited increased costs, 5% problems with employees and 7% problems with markets. On the question “You were forced to make significant changes in the organisation of activities in the company due to coronavirus”, 12% of the respondents strongly disagree, 26% disagree, 4% neutral, 38% agree and 20% strongly agree. The data from the graph 3 shows the following results: on the question “Your earnings decreased year-over-year due to coronavirus”, 10 % of the respondents strongly disagree, 29% disagree, 8 neutral, 38% agree and 15% strongly agree.

The third group of questions is related to technological changes and the anticipation of the importance of innovation for overcoming the problems caused by the pandemic.

Here are the result:

- On the question “Your company uses innovative ways to obtain new markets and to retain the existing customers” 22% of the respondents strongly disagree, 34% disagree, 7% neutral, 25% agree and 12% strongly agree which means that SMEs do not use some new ways to attract new markets and customers.
- The result of the question” You have transformed into electronic distribution of goods and services due to corona virus” shows that SMEs use classic (physical) ways for goods and services distributions (22% of the respondents strongly disagree, 40% disagree, 3% neutral, 20% agree and 15% strongly agree)
- Many surveyed companies believe that innovation strategy plays a crucial role in overcoming the consequences of the pandemic. Actually on the question” Innovation strategy has a crucial role for overcoming business crisis caused by COVID 19 pandemic” 18% of the respondents strongly disagree, 28% disagree, 2% neutral, 35% agree and 17% strongly agree.
- On the question “Your business introduces new products before the competitors do”22% of the respondents strongly disagree, 29% disagree, 7% neutral, 30% agree and 12% strongly agree which means that SMEs do not use some new ways to attract new markets and customers.
- The result of the question ”Your business has the ability to change the production methods quickly in accordance with changing in technology”

shows that most of the business actually 48% of the respondent strongly disagree or disagree and they are not prepared to make big changes in the production methods on the other hand the technology changes in their industry is very fast. (48% of the respondent strongly agree or agree).

The fourth set of questions is related to the measures taken by the Government in order to overcome the problems of SMEs. The results from the last two questions of the survey shows that large number of the respondents, actually even 42%, are sufficiently informed about the measures and programs for encouraging innovation in businesses and 67% of respondents said that the measures taken by the Government focus on fighting corona virus are inappropriate.

Chart 4

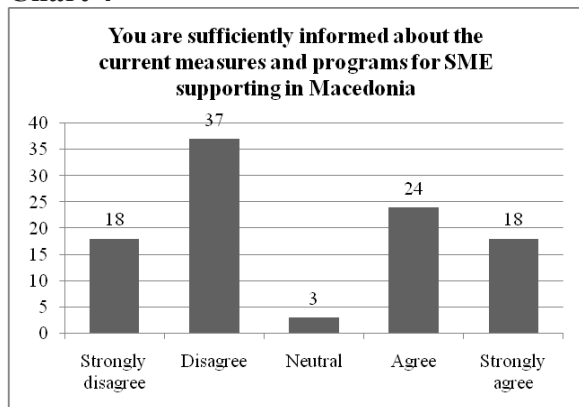
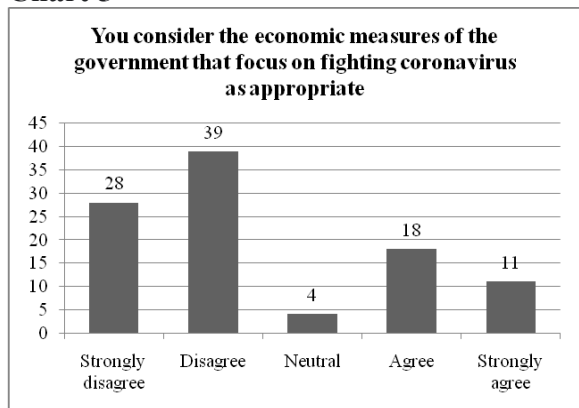


Chart 5



The results that emerged allow to formulate some initial considerations that many of the companies have financial problems, ie lack of own capital, hence the funds they allocate for research and development are very small. Also, a large number of the respondents, actually even 42%, are sufficiently informed about the measures and programs for encouraging innovation in businesses. To cope with the global economic crisis caused by the pandemic, SMEs have identified the challenges created and applied new strategies to protect their businesses. The data in Chart 6 underscore the importance of an innovative strategy for overcoming the consequences of the Covid pandemic 19.

Conclusion

SMEs have a key role in the development of the macedonian economy and it's necessary to create a business environment that will encourage their growth and competitiveness. Today, unfortunately, the functioning of businesses is affected by the consequences associated with the Covid 19 pandemic, and on the other hand, there are still those structural weaknesses that follow our economy from the beginning of the transition, and they come up to expression especially in crisis, such as: the constant trend of deindustrialization of our economy; the deterioration of the structure of the factors that create GDP; failure to create a sustainable model for economic growth and development; the asymmetric state of the labor market; Extremely weak institutions without adequate support and motivation of the private initiative and the private sector, etc. The government has adopted six packages of measures to support businesses but it is obvious that they are insufficient in this period.

In order to encourage and develop small and medium businesses in North Macedonia, the following measures and recommendations should be taken:

- Encouraging of export activities through increasing mobility of the production factors, higher accumulation and foreign capital inflow, encouraging of technical-technological development etc.;
- Creating ranges of products that meet the consumers' needs, appropriate assortment, design and packing of the products;
- Higher promotion activities in order Macedonian products to become recognizable for the foreign buyers;
- Establishing of business entities in different activities and encouraging collaboration between them;
- Creation of specialized production factors via financing and institutional

support of special educative programs and researches, investing in specialized infrastructure;

- Establishing and implementation of strict standards for customers and environment protection, which will enable the national companies to face the same or similar requirements as on the world markets;
- Stimulation of investments in research and development and in other activities that lead towards inventiveness and advancement of individual competitive abilities of the business entities, through encouraging projects of direct competitors within a definite industry.

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