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## **BARRIERS TO THE DEVELOPMENT OF ENTREPRENEURSHIP DEMONSTRATED BY MICRO, SMALL AND MEDIUM ENTERPRISES IN POLAND**

**ABSTRACT.** The article is aimed at presenting the functioning and development of micro, small and medium enterprises (SME sector) and their significance to Polish economy. It discusses the most formidable barriers to managing a business encountered by entrepreneurs. Finally, it presents the results of reports published, among other things, by Civil Development Forum, World Bank (Doing Business 2011) and Polish Confederation of Private Employers Lewiatan (PKPP Lewiatan).

**JEL Classification:** L26, P2      **Keywords:** SME sector, entrepreneurship, barriers to development.

### **The significance of micro, small and medium enterprises to the economy**

Günter Verheugen, Member of European Commission, said: "Microenterprises as well as small and medium enterprises are driving forces behind European economy. They are the main source of employment, inspire and promote the entrepreneurial and innovative spirit in the EU, and thereby are of key importance to greater competitiveness and higher employment". P. Drucker considers it "the essence of market economy" that guarantees democratic economic order. Experience learnt by the developed countries indicates that micro, small and medium enterprises play a crucial role in the economy and have an effect on economic growth as well as increase in employment. K. Sasin (2003, p. 47-60) highlights the role of SME in socio-economic life of a given region in the scope of:

- development of innovativeness,
- employment effect,
- ecological effect,
- development of local production,
- ability of small firms to cope with recession, economic crisis and slump in an effective way,
- regional decentralisation,
- capital mobilization.

According to M. Olinski (2006, p. 134), small and medium enterprises perform a number of positive functions in every well-developed market economy. Generally speaking, they may be divided into social and economic ones. The main social function fulfilled by SME sector is the formation of economically independent middle class (small and medium enterprises are often referred to as enterprises typical of this class). It is generally believed

that the prosperity of a given state and effective functioning of market mechanism depend on the extent to which middle class has developed in a particular society.

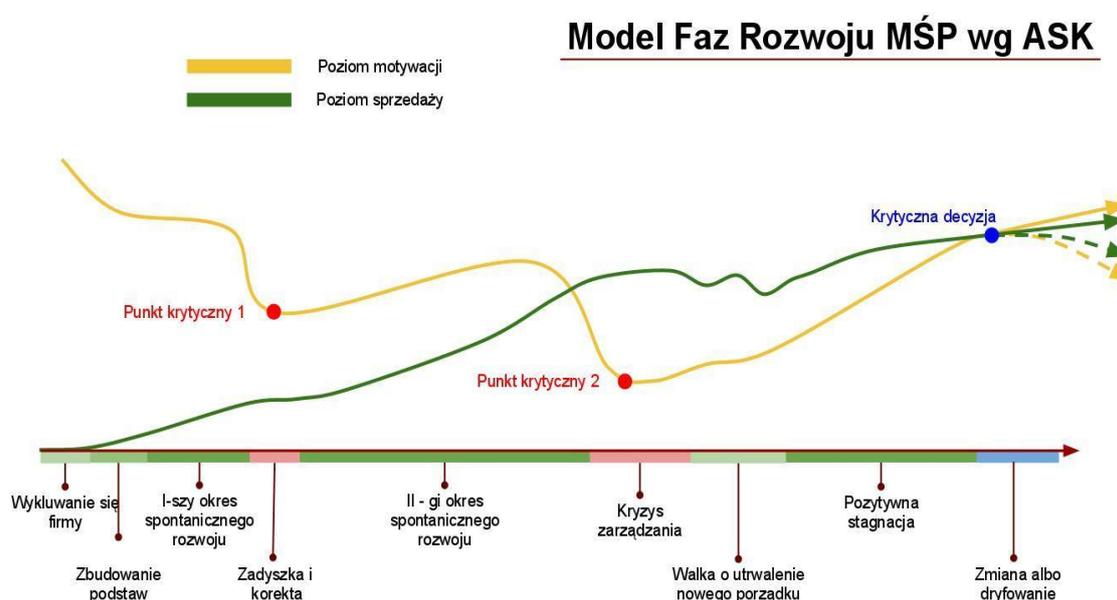
Profound importance of SME sector has made the EU pursue active policy supporting entrepreneurship as well as small and medium enterprises. The actions involve, among other things, the creation of conditions favourable to running a business as well as providing direct access to funding. This is particularly important as SME very often have to deal with market failures and encounter difficulty with generating capital or obtaining a credit, especially when starting a business. They have limited resources at their disposal, which may restrict their access to new technologies or innovations. Due to this fact, one of priorities identified by European Commission is to support micro, small and medium enterprises in order to stimulate economic growth, create new jobs as well as promote economic and social cohesion.

The fact that SME sector plays a crucial role in Polish economy is proven by the following data: in 2009 there were 3 880 237 enterprises registered in REGON system (National Official Business Register) in Poland, which entails a 0.3% increase compared to 2008. The structure of enterprises by size was as follows: microenterprises – 3 672 853 (94.7% of all enterprises registered), small enterprises – 170 182 (4.4%), medium ones – 31 648 (0.8%) and finally large – 5 554 (0.1%). There were 3 874 683 enterprises in SME sector, which constituted 99.9% of all firms. In 2008 the number of enterprises registered in REGON system increased quite considerably (by 1.9% in comparison with 2007). This was the most substantial rise during the period 2003–2007 when average increase amounted to 1.0%. On the contrary, in 2009 the number of enterprises under discussion was not subject to such a significant increase (up to 0.3% in comparison with 2008). The reason behind this state of affairs was slump in Polish economy as a result of rapidly worsening economic situation in the United States and the Member States. Both in 2008 and 2009 the most substantial annual increase in the number of enterprises was observed in the case of small firms (3.4% and 3.3% respectively). In 2008 the number of medium enterprises was subject to significant rise (by 3.2% compared to 2007). However, it was rather moderate in 2009 (a 1.4% increase). With respect to the number of microenterprises, it rose by 1.9% in 2008, whereas in 2009 the increase was not so dynamic and amounted to 0.2% (Raport o stanie sektora małych i średnich przedsiębiorstw w Polsce w latach 2008–2009, 2010, p. 31-33).

### **Entrepreneurship and stages in the development of micro, small and medium enterprises**

Entrepreneurship is a supranational and timeless socio-economic phenomenon. In Poland conditions favourable to its development were provided at the beginning of the 1990's. It was then that market economy was introduced, and to be more precise rules underlying economic democracy and providing everyone with freedom of establishing and managing firms as well as equal rights regulating their functioning. Thanks to the principles of economic democracy, entrepreneurship has become a process supporting market economy and gradually changing its ownership structure in favour of private sector. Having accepted the opinion expressed by J. Targalski (2009, p. 13-16), it should be stated that the development of entrepreneurship is one of factors significant to sustainable economic growth. When asked if entrepreneurship development observed in the 1990's is still as dynamic as then, J. Targalski replies that the first hypothesis that might be formulated in order to forecast the development of entrepreneurship in the future is that quantitative development will be weakened for the benefit of qualitative development (taken the hitherto existing development into consideration). Quantitative development of entrepreneurship was observed during economic transformation and stemmed mainly from the fact that SME sector had not functioned yet and people had to deal with market shortages as far as goods and services were

concerned. Due to the fact that the number of business entities in the private sector increased dynamically during the period 1989-1999, it can be anticipated that further quantitative development will not be so dynamic any more. On the other hand, one may expect increase in the number of dynamically expanding medium enterprises, mainly due to development processes occurring in small firms that are already successful on the market. Furthermore, it may be assumed that the number of firms that are legal entities will be subject to substantial increase, contrary to considerable advantage of firms managed by natural persons observed at present. According to J. Targalski, such forecasts are based on trends in the development of SME which, provided with favourable conditions (e.g. opportunity to operate on a thriving market), need about 10-15 year to successfully go from the stage of entering the market to the stage of organizational, legal and economic maturity. Once established and developing over time, every firm goes through various stages in its life cycle. Particular stages determine the size of enterprise and its organizational structure. *Figure 1* presents author's model describing **nine stages in the development of small and medium enterprises** that was created on the basis of ten-year experience that ASK company has gained in providing advisory services for SME sector (Dudziak, Kisil, 2011).



Model Faz Rozwoju MŚP wg ASK – Model representing stages in the development of SME created by ASK company

Poziom motywacji – Motivation level

Poziom sprzedaży – Sales level

Punkt krytyczny – Critical point

Krytyczna decyzja – Landmark decision

Figure 1. Model representing stages in the development of SME

Source: W. Dudziak, A. Kisil, *Etapy rozwoju MSP*, w: *Gazeta Małych i Średnich Przedsiębiorstw*, Nr 4 (108), 2011, Kwiecień 2011.

**Stage 1. The emergence of a firm** – at this stage, a number of visions of enterprise in the future are being developed, but most of all, actions to be taken are defined. Initial stage in the development of the firm may involve the following two scenarios:

1. Entrepreneur or partners agree on what they will do, what a new business will consist in – what will be produced? For whom? How?

2. A firm receives an order for a given product/service, which in a way makes entrepreneur/partners organise the activity.

**Stage 2. Basis formation** – once order placed by first clients have been fulfilled and corporate profile has been adopted, corporate activity is subject to formalization.

**Stage 3. The first period of spontaneous development** – orders placed by first clients have been fulfilled and organizational framework has been established. This stage in the development consists mainly in canvassing and order processing.

**Stage 4. Breathlessness and adjustment** – a moment when the firm becomes “breathless” and the owners become exhausted. Struggle begins at the following three fronts:

- Market – for attracting and keeping the clients, for image and quality,
- Corporate – for motivating employees and reducing costs,
- Personal – for motivating oneself to make efforts.

**Stage 5. The second period of spontaneous development** – another period during which growth is observed. New people are employed. Cash flows are subject to increase.

**Stage 6. Management crisis** – management becomes too complicated. A strong need arises to re-organise the firm.

**Stage 7. Struggle for maintaining a new order** – the implementation of new systems and tools is not enough – the owner has to convince his/her employees that they are effective, teach them how to use the systems and tools as well as motivate them to do so.

**Stage 8. Positive stagnation** – if the two previous stages have been accomplished successfully, a new order is introduced into the firm.

**Stage 9. Change or drifting** – the time has come to think what next with the firm and make decisions.

The author agrees entirely with the creators of the model who assume that if subsequent stages are described in a professional way, business management will be much easier. The stages in the development will be a guidepost and a hint to managers, namely will suggest to what special attention should be paid and what actions should be taken. Only then is enterprise able to develop in a more stable and predictable way, go smoothly through consecutive stages as well as provide the owners with satisfaction and profit.

### **Barriers to entrepreneurship demonstrated by micro, small and medium enterprises**

As it has already been stated, it is beyond any doubt that micro, small and medium enterprises have laid foundations for contemporary European economies. They exert effect on the economy, and particularly on labour market, due to which public authorities have to continually develop and improve the infrastructure as well as conditions for their operation. In order to determine ways of expanding entrepreneurship, one should at first define barriers to its development. Micro, small and medium enterprises most often face the following three obstacles:

- **barriers found on the market and in environment**, relating to problems caused both by changing economic situation and competition terms;
- **problems with management** caused by limited knowledge and skills acquired by entrepreneurs and managers;
- **financial barriers.**

Undoubtedly, *financial barrier* is the most effective obstacle to the development of entrepreneurship. In Poland, it is limited access to funding that is one of key problems discouraging people from being enterprising and developing this potential. Savings and private property, which a potential entrepreneur has at his/her disposal, is as a rule insufficient for starting a business on a large scale. Furthermore, a strict policy for entrepreneurs pursued by banks, namely that they do not grant credits willingly, is the main problem with generating

the capital. This leads to a situation when micro, small and medium firms have to deal with the lack of financial liquidity and lack of borrowing power since the very beginning of their functioning, which hinders their development. This has been proven by the survey conducted by the Management Observatory Foundation in 2009 which indicated that, apart from high staff costs and taxes, difficulty with receiving funds is a major problem mentioned by the representatives of business environment. It is worth emphasizing one more time that the development of SME sector in every country depends mainly on the amount of equity capital that entrepreneur has accumulated as well as access to external financing.

The development of microenterprises is determined by two types of factors (Wilimowska, Urbańska, 2009, p. 23), namely external (environment-related) and internal. From the point of view of the smallest entities, the factors in question should be analysed as potential barriers to their development. Obviously, business environment provides firms with opportunities to expand, yet to be seized only if the barriers have been overcome. The obstacles are reflected in the following phenomena and spheres: character of entrepreneurship, preferred ethical and moral standards, society's approach to activity undertaken by microenterprises, specific form of competition in the economy, sources of funding, fragmentation, type and scale of activity, inefficient legal system, poor effectiveness of policy aimed at supporting SME sector and finally, the fact that their interests are hardly represented.

In Poland, there are a great number of barriers to the development of entrepreneurship. Obstacles to running a business have been identified in, among other things, reports published by Civil Development Forum, Polish Confederation of Private Employers Lewiatan (PKPP Lewiatan) and World Bank. Below there is a brief discussion on barriers identified in:

▪ **Report published by Civil Development Forum<sup>1</sup>** in 2008 (still valid) entitled *How to release entrepreneurship in Poland?* It presents the main problems faced by entrepreneurs in Poland, namely:

1. *High taxes* – Poland is among countries with the highest fiscal charges. Only three states, i.e. Denmark, Sweden and Hungary, have imposed higher burdens.
2. *Administrative barriers* – entrepreneurs claim that there are too many administrative procedures and obligations to administrative bodies.
3. *Poor quality of legal system* – entrepreneurs pay attention to a multitude of contradictory legal regulations, problems with interpreting them in a transparent way, as well as repeated amendments to legal acts.
4. *Difficulty with receiving funds* – entrepreneurs mention a high cost of capital generation and lengthy procedures for awarding grants.
5. *Difficulty with enforcing receivables* – enforcing the receivables entails following 38 procedures which usually lasts 830 days.
6. *Too strict regulations on the conditions of employment and dismissal* – entrepreneurs mention a limited number of flexible forms of labour organization.
7. *Barriers to using Structural Funds* – entrepreneurs state they lack information about the support they may receive from the European Union.
8. *Problems with declaring bankruptcy* – in Poland it takes on average three years to follow the procedure for declaring bankruptcy, i.e. six times longer than e.g. in Ireland.
9. *Expensive medical examination* – employers are obliged to pay for medical examination of a new worker and cannot employ anyone who has not been subject to such a procedure.

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<sup>1</sup> For more information see: [www.for.org.pl](http://www.for.org.pl)

▪ According to **Report published by World Bank, Doing Business 2011**<sup>2</sup>, Poland is not friendly to entrepreneurs. Complex procedures are one of the main reasons behind unwillingness to start a business demonstrated by natural persons. With reference to ease with which one may establish a firm, Poland occupies 70<sup>th</sup> position in the ranking listing 180 countries and published by World Bank. Taken the time it takes to receive a building permit into account, Poland is assessed negatively as it takes 311 days to complete all the procedures. The situation is slightly better when it comes to paying taxes (121 position). As for actions to be taken in order to start a business, Poland occupies 113 position. On average, it takes 32 days to start a business. For the sake of comparison, it takes 1 day to complete all the formalities in New Zealand.

▪ **Report published by Polish Confederation of Private Employers Lewiatan (PKPP Lewiatan)**<sup>3</sup> – "Black list of barriers to entrepreneurship 2011" compiled by PKPP Lewiatan includes 367 obstacles, ambiguities and inconsistent solutions encountered by entrepreneurs while starting and running a business. Most obstacles are posed by stringent regulations included in the labour code (90) and faced within a given branch (85). As indicated by the report, nearly 40 tax revisions were completed in Poland in 2010 which, instead of reducing the number of tax barriers, imposed new ones. As for building permits, no major changes were introduced. In Poland, the time it takes to receive the permit in question is still one of the longest in the world. Entrepreneurs have to deal with lengthy administrative procedures as well as the fact that no amendments have been introduced into Spatial Planning Act. Unfortunately, e-administration system, which could enable people to contact public offices via the Internet, is not functioning effectively in Poland. Furthermore, starting a business may be difficult as some types of activity are licensed.

The survey addressed to Polish entrepreneurs and conducted by **the Polish Chamber of Commerce** in the last quarter of 2010 indicates that the majority of respondents expect demand to grow, both on domestic or Community market. Furthermore, company owners anticipate that trading with countries other than the Member States will be intensive. It is worth noticing that two thirds of entrepreneurs expect their turnover to increase in 2011, which – taken the global economy into account – is a very optimistic signal. The main reason behind such a state of affairs is a systematically growing demand (both domestic and foreign). However, it should be stated that the situation in some industries (such as construction or transport) is still unstable. Labour market has been subject to stabilization, yet general economic situation is still uncertain, which is proven by the fact that nearly half of respondents are not planning to introduce any personnel change in the current year. It is alarming that over one fourth of firms reduced capital outlay last year. One of reasons behind such a decision is the fact that the inflow of Community funds as well as expenditure incurred by public sector (on the co-financing of SME) are to be reduced in 2012 and afterwards.

According to K. Dworznik (2011), Polish entrepreneurs have a considerable potential for growth that may be used for stabilizing the conditions in which they function. In 2011 Polish economy needs reforms aimed at, among other things, improving the quality of law-making as well as facilitating the investment process. Entrepreneurs hope that in 2011 Polish economy will be subject to deregulation. They expect the government to take actions in order to provide more stable conditions for running a business. Entrepreneurs consider it extremely important to be certain in what direction the economy develops, due to which they can formulate long-term plans. Polish firm owners emphasize the fact that administrative barriers and high labour costs (not relating to remuneration) are the most formidable obstacles to unconstrained development of entrepreneurship in Poland. One of barriers, i.e. the shortage of

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<sup>2</sup> [www.doingbusiness.org/rankings](http://www.doingbusiness.org/rankings)

<sup>3</sup> [www.pkpplewiatan.pl/\\_files/publikacje/CLB2010.pdf](http://www.pkpplewiatan.pl/_files/publikacje/CLB2010.pdf)

qualified workers, is a kind of novelty on the list compiled by entrepreneurs. Despite high unemployment rate and hence low employment level, company owners consider this barrier effective. It is believed that the main reason behind such a state of affairs is the fact that labour market has not been structurally adjusted to the requirements of economy. This stems from ineffective educational policy, emigration of Polish people to other Member States as well as ineffective legal regulations. The fact that academic circles do not demonstrate entrepreneurship is another problem. Actions to be taken in this scope should be aimed at creating conditions favourable to the development of entrepreneurship in Poland<sup>4</sup>. These actions include reducing bureaucracy, lowering real activity costs, reducing the number of permits and registers of regulated activity, licences or authorisations, providing easier access to liberal professions, eliminating regulations unfavourable to entrepreneurs from Polish law, introducing acts that will provide legal solutions essential from the point of view of entrepreneurs, developing arbitration courts, facilitating and accelerating the course of arbitral proceedings, as well as offering greater possibilities of transforming the form of activity.

What Poland lacks is a comprehensive way of thinking about conditions for the development of economy. A set of regulations and practical solutions is not consistent. It is difficult to find a keynote, and if any – one may come across an opinion that entrepreneurs should not be trusted and every possible restriction should be placed on their way just in case. Even if new governments are willing to improve management conditions, they do it very selectively. Removed barriers are replaced with new ones. Therefore, the overall result is not subject to change.

## Conclusion

As it can be noticed, the activity of micro, small and medium enterprises is currently entrepreneurship-oriented. This attitude involves taking advantage of changes occurring on the market and treating them as opportunities to develop. Entrepreneur managing a small or medium firm has to flexibly respond to market requirements, actions taken by competitors as well as changes in environment. Micro, small and medium enterprises allow forming a solid basis for economic growth. It is in such conditions that the greatest number of new jobs is created. Furthermore, they enable enterprises to be flexible and adjust to consumer expectations and changing conditions of management in an easier way. Firms use available production factors in a more effective way. In the case of the developed economies, economic success to a large extent depends on effectively functioning SME. The firms under discussion have been competing with companies from the developed countries particularly since Poland joined the European Union. Barriers they encounter, e.g. lack of adequate support from the state, limited support from business environment institutions, or ineffective management of financial resources might widen competitive gap between Polish and foreign firms. Therefore, Polish law, administrative bodies and economic courts should be subject to comprehensive reforms so that business environment they represent could facilitate and not obstruct the development of entrepreneurship and Polish enterprises. Overcoming the barriers that hinder the development of SME sector in Poland should be an essential element to be taken into consideration while formulating the state policy pursued with reference to this sector.

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<sup>4</sup> <http://www.lppa.wssm.pl/index.php/artykuy/151-bariery-rozwoju-przedsibiorczoci.html>

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