



SUPPORTING “GENERATION START-UP”: OPPORTUNITIES FOR MACEDONIA

This case note presents our research findings and analysis on the start-up enterprise landscape in Macedonia. This research was designed to identify current good practice among financial services providers and international organizations serving start-ups; understand the future potential role of microfinance vis-a-vis start-ups; and propose concrete and practical steps to bring about more support for start-ups. This project is being implemented within the four-year Framework Partnership Agreement of MFC and the European Commission within the EaSI Programme.

THE BIG PICTURE

Despite being a small, landlocked economy, the Former Yugoslav Republic of Macedonia has proven to be relatively competitive and dynamic in comparison to its regional competitors. Overall economic growth has been subdued in the post-crisis period, but recovered strongly in 2015–2016. It reached 3.2% in 2015, and is estimated to have slowed down to 2.4% in 2016. This volatility seems largely caused by spillovers from the crisis-afflicted Western European economies, rather than as a result of major domestic imbalances. Nonetheless, the economy is expected to strengthen in the short term as a result of positive business environment reforms in recent years.

Since its independence in 1991, Macedonia has made progress in liberalizing its economy and improving its business environment. Its low tax rates and free economic zones have helped to attract foreign investment, which is still low relative to the rest of Europe. Corruption and weak rule of law are significant problems. Some businesses complain of opaque regulations and unequal enforcement of the law. Macedonia scores 37 on Transparency International’s Corruption Perceptions Index (ranging from 1–100, with 100 representing the ‘most clean’), which is low compared to many other Balkan countries (Slovenia: 61, Croatia: 49, Montenegro: 45).

Unemployment has remained consistently high at about 23% (2016–2017), compared to the average among the EU

candidate countries¹ (16.5%), but a figure which masks informal employment in the extensive “gray market”, estimated to be between 20% and 45% of GDP, and which is not captured by official statistics. Youth unemployment is particularly high, at 47%, the highest among EU candidate countries (which average 37%).

THE START-UP LANDSCAPE

According to the data of the State Statistical Office, the number of active business entities in Macedonia in 2016 was 71,519, an increase of 1.9% compared to 2015.

SMEs account for the same share of the total number of businesses as the EU average, or 99.7% of all registered enterprises. The SME sector is a significant contributor to the economic growth with around 68% of GDP participation and two-thirds of the employees. According to Makstat data, almost 7,000 new enterprises were created in 2016, mainly in the form of a limited liability company. The new enterprise creation rate (number of limited liability companies created during the year per 1,000 adults) in Macedonia is 3.7, which is comparable to the world average of 4.0.

The informal sector is significant and remains the biggest problem for SMEs. The informal market is estimated to account for 20%–45% of GDP.

¹ EU candidate countries include Albania, Macedonia, Montenegro, Serbia and Turkey.

THE SURROUNDING ECOSYSTEM

National Strategy for SME Development

Macedonia has made limited progress on developing its institutional framework for SMEs. The previous National Development Strategy for SMEs (2011–2013) has expired, but while the new SME development strategy has been drafted, it is still pending approval.

Several reform activities have been implemented to stimulate the development of entrepreneurship and SMEs in the following areas: simplification and reduction of taxes, quick and simple registration of new businesses, simplification of administrative procedures (such as filing taxes), reduction of costs, procedures and documents for doing business and facilitating access to investment (by creating an innovation fund, for example). At present, the priority of the economic policies of the government is to increase the competitiveness of the Macedonian economy.

The following national strategies relate to SME development: Regional Development Strategy 2009-2019, Strategy for Development of Crafts 2012-2020 and Innovation Strategy 2012-2020.

The Agency for Promotion of Entrepreneurship (APPRM) carries out the implementation of some support programmes, based on an annual action plan developed in accordance with national and EU SME policy priorities.

Entrepreneurship education

Entrepreneurial learning is high on the national policy agenda, with the Entrepreneurial Learning Strategy of Macedonia 2014–2020 developed to improve the entrepreneurial culture (risk-taking, innovation, leadership). The aim was to implement the activities through a multi-stakeholder partnership between public, private and civil society institutions. Entrepreneurial learning has been defined as a key competence objective for both lower and upper secondary levels. In September 2013, the subject of “Business and entrepreneurship” was introduced as a stand-alone course in elementary, secondary and higher education. However, it remains a voluntary subject. Entrepreneurial education, on the other hand, is a mandatory part of the curriculum for all students, inasmuch as it is integrated into other core subjects, such as mathematics. The country stands out as one of the few in the region that has already carried out training on entrepreneurial learning for school leaders and teachers, and indeed it has plans to increase such training.

Perception of entrepreneurship

According to the Global Entrepreneurship Monitor (GEM), the general perception of the opportunities for

entrepreneurs is high in Macedonia, and among the highest compared to the countries studied in the project. 38% of adult Macedonians think that there are opportunities to start a business in the area where they live. Many Macedonians (56%) also feel capable of starting a business. In addition, 25% of adults intend to start a business in the next 3 years, a statistic which distinguishes Macedonia from many other countries in Europe (e.g. 7% in Bulgaria, and 15% in Hungary). However, as yet, the intentions do not fully translate into business creation, in terms of seeing a comparable percentage of adults in Macedonia and in the other countries register a company and continue with it for several years. Entrepreneurship is seen as a good career choice, but one that is driven by the necessity rather than seeking opportunities for self-improvement. Macedonia stands out among other countries, as over 50% of the nascent and new businesses (Total Early-Stage Entrepreneurial Activity) were started because of no other work opportunities. Compared to several other countries, Macedonian entrepreneurs rarely are driven by the desire to create employment for others. Less than 20% of nascent and new businesses plan to employ more than 6 people in the next 5 years. This is surprising, as the conditions for registering of business are very favorable, with few procedures and little time needed to register a company.

According to the representatives of the institutions supporting entrepreneurship, people in Macedonia are entrepreneurial, but they lack courage to actively and intensively engage in setting up and running the business. The younger generation is more active, especially in the IT sector. However, high demand for IT specialists in the corporate sector attracts young people to eager for secure, well-paid employment, instead of turning their innovative ideas into their own business.

That said, being an IT startup seems quite fashionable among younger generations. They participate in “hackathons” and seem to do well (they get high scores and receive rewards) but do not follow through with building sustainable businesses. One of the reasons is lack of knowledge how to move to the next step from a project to running a company, how to enter the market and access financing. Most of the successful startups are usually spin-offs (from existing companies), and even they have difficulty reaching sustainability.

Those we interviewed reflected that despite interest and eagerness, young people lack the motivation needed to weather the start-up years. Often at the first sign of difficulty, or a new opportunity for employment, they tend to fold their start-up projects. Given the economic uncertainty following the global financial crisis, many young people prefer working in the public sector rather than look for other alternatives. Younger people tend to be more entrepreneurial in general, however mature professionals

that have had entrepreneurial experience (i.e. are running or have run their own companies) will start a new business a lot quicker than young people.

According to the research conducted by the Association of Business Women, running a business is not a very popular choice for women. They open their own business as a necessity, not as a result of an opportunity. They are mostly involved in micro and very small businesses which have low turnover and profit levels. Most of the startups that are run by women are meant to fill the gaps in the family budget, not make a large profit. The research also states that women tend to be less entrepreneurial, because they are more risk averse— for instance they are more reluctant to put up their homes as collateral to for a new business loan. Women usually start businesses that are based on their existing skills without the need for additional education and training, and that have low investment needs.

Starting a business regulations

Macedonia continues to be one of the easiest places to open a business, currently (2017) ranking 4th out of 189 economies of the *World Bank Doing Business - Starting a Business indicator*.

A “one-stop shop system” was implemented on January 1, 2006. The Central Register is the single institution for registering LLCs and other forms of trade companies, foreign representative offices, and other entities. Registration of LLCs must be conducted in electronic form, with the assistance of authorized registration agents who are the only authorized entities to submit applications for registration. The electronic registration process is free of charge. Connection is now established between the Central Registry and the Employment Agency which allows registering of first employment of directors through the Central Registry of Macedonia and registering employees with the social fund.

The entire company registration procedure is completed in the office of the registration agent. It takes one day. Companies launching a commercial activity that is predicted to achieve turnover over 15,000 Euro are required to register for VAT. The regulatory simplification was achieved within the SME development strategy 2011-13.

Globally, Macedonia stands 9th in the ranking of 190 economies on the ease of paying taxes. In the last 10 years, the corporate tax rate was reduced from 15% to 10%, but there were new taxes and para-fiscal charges added. There is no tax relief, grace period, etc. for start-ups. Taxes are paid for the whole year in advance for companies whose turnover exceeds 100,000 Euro; if it is lower, taxes are paid quarterly. The only relief is that companies with less than 15,000 Euro turnover are VAT exempt.

Overall, business regulations are constantly in flux, and keeping up to date is a challenge for businesses, who need to task a member of staff with keeping up to date, or hire a lawyer or accountant to do so (a costly alternative). Additionally, if a company wants to apply for a public tender, they have to prepare many documents, and the cost of obtaining these can be high. These documents are valid for only 6 months, so often when the company wants to apply for the next tender, they need to prepare new documents.

While opening a company is easy and inexpensive, closing a company is difficult. If tax has been overpaid by the business, then the tax inspectors must conduct an onsite pre-refund audit, which lengthens the process. Usually, it takes more than 6 months to close a company.

Access to finance

Banking sector

There are 15 commercial banks in Macedonia, all of which serve the SME sector—although the share of SME credit in the total loan portfolio of the banking system is estimated at only 35% (about 1.4 billion Euro). However, banks do not serve start-ups or early-stage enterprises, as they require a minimum of 12-month business history for a company to be eligible for a loan.

State programs

The government supports start-ups with several grant and loan programs for unemployed people. The Self-Employment Program is jointly implemented by the Ministry of Labor and Social Policy, and the Employment Agency, with support from the UNDP. The program is part of the Operational Plan for Active Programs and Measures for Employment and Labor Market Services for 2017.

- Grants up to 5,000 Euro for the unemployed who register a firm (10,000 Euro if the company has two co-owners).

Grants are offered to the unemployed people registered with the Employment Agency who complete a training course and prepare a business plan. According to the annual report of the Employment Agency of Macedonia, 1,009 people have received grants to date. The workplan of the Employment Agency for 2017 assumes that the grant and training program will reach 1,050 unemployed.

- Loans for registered unemployed people who are active job seekers and want to open their own business

For small-scale activities, the loan amount is 3,000–9,000 Euro (3,000 Euro for each job created up to a maximum of 3 jobs). In case of larger businesses, the total loan amount

is up to 17,000 Euro (5,000 Euro for starting a business, plus 3,000 Euro for each additional job position created, with the maximum of 5 people employed). The repayment period is 3 years, with a grace period of 1 year for loans up to 9,000 Euro, and 5 years including a grace period of 1 year for loans exceeding 9,000 Euro.

- Loans for young people (up to 29 years old) who are registered unemployed and active job seekers who want to open their own business.

The loan amount is 7,000–23,000 Euro, depending on the number of jobs created, with the maximum of 5 new jobs created. The loan is to be repaid in 7 years with a grace period of 1.5 years. In both loan programs, the interest rate is 1% per annum. The borrower needs to provide their own contribution of at least 25% of the amount of the loan requested. Loans can be guaranteed by a mortgage or a bill of exchange.

According to the 2016 annual report of the Employment Agency of Macedonia, loans were disbursed to 166 unemployed people, 62 of whom were under 29 years old. In the nine years of the self-employment program of the Employment Agency, 8,730 businesses were created, 35% of the initiatives are run by female entrepreneurs and 31% are young people aged up to 29 years.

The Macedonian Bank for Enterprise and Promotion (MBDP) acts as an agent for the Employment Agency to channel funds of the above two lending programs through the commercial banks. The bank also manages ten credit lines for MSMEs, but none of them is dedicated to supporting start-up enterprises.

Fund for Innovation and Technology Development (FITD)

The mission of FITD is to encourage and support the innovation activity in micro, small and medium-sized enterprises for achieving accelerated technological development. Their approach is based on knowledge transfer, research for development and innovation that contributes to job creation and economic growth and development, while improving the business environment for developing the competitiveness of companies. The Fund currently offers two types of financing: co-financed grants for newly established companies: start-ups and spin-offs up to 6 years old, and co-financed grants and conditional loans for commercialization of innovation for businesses of any age.

Between 2015–17, FITD held four open calls for co-financed grants for start-up and spin-off companies and commercialization of innovation for micro-, small- and medium-sized enterprises. The funds were provided by the budget of the Republic of Macedonia.

The first instrument provides funding for up to 85% of the total budget of the project, up to a maximum of 30,000 Euros. The remaining amount of the total project budget should be provided by the applicant. In the first 2 years (2015 and 2016) 30 businesses received such grants. So far, the Fund has supported projects in the following industries: ICT, mechanical engineering, electronic engineering, waste management treatment, education, tourism, creative industries, and construction.

FITD provides consulting support to its beneficiaries, mostly to strengthen their managerial skills and, based on their need assessments, in other fields of interest such as IP, freedom to operate, licensing, EU programme Horizon 2020 and technology benchmarking. It plans to introduce the other technical assistance instruments for start-ups in future, including a network of mentors that will support start-ups in various areas of business development.

Equity funds

Venture capital activities in Macedonia are in their infancy, but the government has taken important steps to improve the ecosystem for venture capital funds and put in place the relevant legal framework. Currently, several private equity and venture capital funds are available for Macedonian SMEs, but the total investment portfolio is as yet limited.

The Center for Entrepreneurship and Executive Development (CEED) supports a range of start-ups through small equity investments or loans. This seed money is intended to move the start-up into its next development phase (e.g. prototype development), from which it is easier to attract outside investment. The companies that the organization invests in are chosen by the Management Board of the CEED Foundation. The Foundation also runs Business Angels Club, with 16 members ready to invest in business ideas or existing businesses. Since the launch in 2014 the Club members have invested in four enterprises.

Business development services

A number of institutions across the country offer different forms of non-financial support to start-ups.

The Agency for Entrepreneurship Development and Promotion (APPRM) is active in providing non-financial support to micro, small and medium-sized companies. The scheme offers vouchers for consulting services for micro-, small- and medium-sized enterprises. Start-up enterprises can receive vouchers of the value of 500 Euro (750 Euro in case of mature enterprises) and use them to pay for the services of 250 authorized consultants. In 2016, vouchers were extended to 21 beneficiaries. Additionally, the APPRM offers what it calls 'InfoPult', a program that provides information to SMEs about foreign markets, financing for

start-ups and mature businesses. Both programs are implemented by eight regional business support centers and enterprise support agencies.

Recently, APPRM has been working on a solution with Japan International Cooperation Agency (JICA) to set up a system of mentoring services. Mentors will guide entrepreneurs through all stages of growth. In the pilot program, mentors will be paid from the state budget.

The Employment Agency offers training and mentoring (up to 45 hours) for young people aged under 29 years who have completed secondary education, and who are registered at the Employment Agency as active jobseekers. The training helps them to acquire necessary knowledge in the field of entrepreneurship, and to develop a business plan for successful self-employment. The program reached its target of 950 trainees in 2015. The activities of the project directly contribute to the achievement of the objectives of the Operational Plan for Active Labor Market Measures for 2017.

There are several incubators in Macedonia located in the regions of the country.

YES Incubator

Youth Entrepreneurial Service (YES) Incubator supports micro-, small- and medium-sized enterprises in the ICT field through the process of business incubation, offering access to services for accelerating their growth and development. The services include office space, training and mentoring, connecting with potential clients, and networking events. While the incubator does not provide funding, it facilitates the access by linking tenants with financing sources (i.e. FITD and other companies via the Enterprise Europe Network.) and through trainings on how to access financial support and investment.

Some services are fee-based (space rental and certain trainings), while the others, which are project-based, are free of charge as they are financed by donors (mentoring, other trainings). Free services are available only for the tenants, while paid trainings can be also attended by any other businesses.

Tenants can stay in the incubator for the maximum of 2 years. Currently there are 15 tenants, the maximum number that the incubator can host at any one time. To date, more than 85 companies have graduated from the incubator and 90% of them are still in business.

Seavus Incubator

Seavus Incubator is a multi-functional working space intended for tech start-ups and entrepreneurs, digital artists and online media companies.

The pre-acceleration program of Seavus is a highly-intensive program dedicated primarily to business development issues. The program is six weeks long, seven days each week. The program is delivered by international mentors and local businessmen. The program ends with a “demo day” where the start-ups present in front of potential investors.

Seavus incubator also offers co-working space for IT companies and mentoring services for its tenants. The pre-acceleration program is free of charge, while the co-working space is rented for 30 Euro per month.

Last year, there were 21 start-ups participating in the pre-acceleration program, this year it started with 10 but will end with 8 (2 start-ups quit). Additionally, there are 32 tenants that only use the co-working space.

Start-up Macedonia

Start-up Macedonia is an association created by a group of Macedonian start-up enthusiasts, experts, investors, start-up support organizations. This community includes start-ups, investors, FITD, consultants and innovators. Its main objective is to create a Macedonian start-up community to encourage and help start-ups to create favorable environment for innovation. The organization, registered as an NGO, was formed by five enthusiasts. The aim of Start-up Macedonia is to become an umbrella organization for all needs that start-ups have. It promotes the entrepreneurial spirit, helps start-ups grow, encourages collaboration, provides access to international networks, promotes start-up events and provides legal support. The short-term goal of the organization is to map the start-up ecosystem in Macedonia, to identify the current issues that the ecosystem is facing and propose relevant solutions.

CEED Hub

Apart from the traditional services provided to MSMEs, the CEED HUB has, in the past three years, focused on developing and running two programs specifically for start-ups:

- Pre-acceleration program: a “light” program that includes training and mentoring, as well as co-working space. It involves training and mentoring twice a week for three months, hence it is less intensive than the acceleration program.

- Acceleration program: the intensive program with activities every day for 14 weeks. The support includes training, mentoring and co-working space. Mentors come from established companies, and members of the CEED Business Clubs, thus ensuring that start-ups can learn from real-world experience of seasoned entrepreneurs.

CEED Hub's programs are free of charge as they are donor-funded. CEED Hub does not target any specific type of start-ups, it supports all types of enterprises. Both programs have two cycles per year with 10–15 start-ups per cycle. To date, 300 people benefited from the two CEED Hub start-up programs.

NEEDS OF ENTREPRENEURS

Macedonian start-ups lag behind those from other Balkan states, in that the latter are moving into an international market, while Macedonian start-ups are struggling to gain local recognition. In this way, mentorship and experience-sharing with existing and experienced entrepreneurs would help them develop their market strategy.

Support with risk capital is also needed in order to encourage them to move forward and develop beyond the concept-testing phase. Young people seem to be risk averse, hence if financed and given some time (1–2 years) to develop a project and put it on the market, they might have a higher success rate. Activating alternative sources such as business angels and VC funds could also encourage faster growth of start-ups. To achieve this, better legislation for start-up financing, especially for smaller investment funds aimed at start-ups, is needed.

Those we interviewed reflect that many start-ups have difficulty managing their finances efficiently. Mentoring and trainings on how to most effectively use financial resources would go a long way to fill this knowledge gap.

Additionally, the start-up support services, especially those relating to the IT sector, are centralized in Skopje. Therefore, there is a need to spread the services more evenly across Macedonia to give equal access to all start-ups.

CURRENT MICROFINANCE INITIATIVES

Horizonti

Horizonti was established in January 2000 as a microcredit project of the Catholic Relief Services, and transformed in 2005 into a microcredit foundation. By 2017, it has disbursed more than 10,000 loans.

Horizonti provides access to financial services for the economically-active population with low incomes, mostly women microentrepreneurs and members of socially-

excluded and marginalized groups. Lending products include agro loans of up to 10,000 Euro, microbusiness loans of up to 5,000 Euro and housing loans. In order to be eligible for a business loan, an enterprise needs to be at least 6 months old, and able to present its business track record. Start-ups younger than 6 months are seen as too risky to serve. However, the Foundation is interested in extending its services to newly-established microfirms, although it recognizes that it would need to learn how to assess the chances for the business to be successful and how to manage its credit risk.

Moznosti

Moznosti Saving House has been in operations since 1996. It provides services to micro- small- and medium-sized enterprises that operate in trade, services and production, offering financial products and services such as loans and savings. It offers agricultural, business, personal and housing loans. Business loans of up to 50,000 Euro are disbursed to established businesses with a business track record. Moznosti does not work with emerging enterprises as they are high-risk ventures, and Moznosti does not have a sound methodology for assessing risk in these cases. It is also of the opinion that commercially-priced loans are not the best mean for financing start-ups. Rather, subsidized loans or other forms of 'soft' funding provided by institutions/entities prepared to incur financial losses would be more appropriate.

FULM

FULM Saving House is a credit union which offers deposit and loan products. Since it began operations in 1999, the saving house provided over 25,000 loans. Loans of up to 5,000 Euro are disbursed to individuals and farmers for personal as well as business needs. Currently, FULM does not serve legal entities. However, recognizing the fact that many of the loans taken by individuals are used for financing business needs, it plans to introduce a new product: a business loan, which will be extended to established businesses as well as start-ups.

Additionally, a substantial proportion of FULM loan clients (35%) are registered unemployed, and for whom a dedicated loan product is on offer. The unemployed often use these loans to engage in an income-generating activity or to set up a regular business.

Macedonia Enterprise Development Foundation (MEDF)

Established in 1989, MEDF's mission is to support the development of small enterprises. Its programs focus on promoting entrepreneurship and financial services. So far, MEDF has implemented over 10 projects for the EU and USAID on access to finance, corporate social responsibility,

local economic development, and employment. MEDF also conducts annual Global Entrepreneurship Research (GEM), the largest research of entrepreneurship in the world, the results of which are presented in the section of entrepreneurship in the beginning of this report.

In terms of services for start-up enterprises, MEDF implements a training and mentoring program within the program for unemployed grant recipients managed by Employment Agency of Macedonia.

MEDF also provides access to loans for micro and small enterprises through financial institutions. In the last 20 years, almost 14,000 clients were served, half of them were women, and nearly 40% were rural. However, start-up enterprises are not served, as the selection of clients is done by the financial institutions that disburse the loans. Currently, MEDF is considering establishing an accelerator to support innovative business ideas through the provision of office space, administrative and technical services, mentoring and training, consultancy and training, provision of initial funding and of professional help for start-up and growth of businesses.

Alliance of Microfinance Organizations (MFO)

MFO is an association of microfinance institutions focused on supporting start-up entrepreneurs, micro and small enterprises, and other financially-excluded groups (Roma, rural communities, etc.). MFO members include Horizonti, Moznosti, FULM and MEDF.

MFO engages in analysis and research, trend monitoring, awareness-raising campaigns and other advocacy work, preparation and suggestions of relevant legal acts and mechanisms supportive business environment, capacity building through training and consultancy, and public events.

NEXT STEPS

The representatives of the institutions that form the start-up ecosystem, and with whom we talked during the project, provided numerous ideas on how that ecosystem could be improved, and what kind of services for start-ups would be beneficial. In general, recommendations can be grouped into: non-financial support, access to finance and the regulatory sphere.

Non-financial support (BDS)

- Increase the amount of advisory mentoring for start-ups
- Bundle non-financial service delivery with finance provision (loan plus business advice or mentoring)
- Improve infrastructure to support entrepreneurship, including incubators, accelerators
- Develop special 'tech parks', where start-ups can work on new ideas (these can be linked to tech universities, whereby the companies commercialize innovations emerging from the student body)
- Create an online information platform that details how to start a company, where to register, where to obtain licenses/permits, where to get financing, available training resources, consulting services, etc.
- Organize networking events for IT start-ups.

Access to finance

- Capacity building for MFIs to serve start-ups (especially risk assessment)
- Develop self-sustainability models for MFIs for serving start-ups
- Organize study tours to other MFIs serving start-ups sustainably
- Set up foundations providing microcredit with subsidized loans more appropriate to the increased risk profile of start-ups
- Activate and formalize alternative sources of finance, such as business angels and venture capital funds
- Link start-ups with investors.

Legal and regulatory sphere

- Ease compliance and reporting requirements for microenterprises
- Lower penalties for non-compliance for microenterprises
- Introduce tax privileges for start-ups
- Support associations, institutions that could lobby on behalf of microenterprises.

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This publication has received financial support from the European Union Programme for Employment and Social Innovation "EaSI" (2014-2020). For further information please consult: <http://ec.europa.eu/social/easi>. The information contained in this publication does not necessarily reflect the position or opinion of the European Commission.