Measuring the Performance of SMEs for Evidence - Informed Economic Development Policies in Albania

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Summary

Without any doubt, Small to Medium Enterprises (SMEs) represent a driving force in economic development today. SMEs by the numbers dominate the world business stage, although their contribution varies among countries. In Albania, SMEs represents about 98% of total companies with a significant contribution of about 70% to the national Gross Domestic Product (GDP). The structure and performance of the national economy is dependent on the economic performance of SMEs and the government has drafted several strategic programs that support the development of SMEs over time. The latest program, Business and investment development strategy for the period 2014- 2020 includes, for the first time, performance indicators that serve to monitor the achievement of strategic objectives for SME development. However, measuring the performance of SMEs and their ability to compete on national and international markets requires more comprehensive information. The analysis shows that although there has been a positive economic growth rate of the GDP over the last few years, the performance indicators of SMEs have shown a slightly negative trend, indirectly indicating the need for more support in order to increase their contribution in the national economy. Although the current results should be interpreted with caution, it's time for economic policy to be based and informed not only on the volume data of SMEs, but also on their performance, as it is the latter that guarantees the sustainability of the economy.

Keywords: SMEs, Business Strategy, Business Statistics, Performance Indicators, Evidence-Based Policy

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Introduction

After the political and economic shift of 1991, the private sector became the main contributor of the Albanian economy, with continuous positive growth trends in all sectors and particularly in services. SMEs are the main actors in Albania's economic development and if we compare their economic structure both at a national and European Union (EU)-level through some basic indicators, their impact in the non-financial business economy is evident. About 0.2% of companies in EU member states are classified as large and provide more than 43% of value added and 33 % of employment, while the rest is provided by SMEs. In the case of Albania, SMEs have a decisive role on economic development

(EC, 2017). More concretely, according to INSTAT (INSTAT, 2019a) SMEs in the Albanian economy account for:

- 99.9% of the total number of active enterprises,

- 82% of the registered employment, at the national level,

- 78% of sales (turnover) at the country level,

- 60% of investments at the country level, and

- 67% of the national GDP (excluding agriculture).

The table below shows the general features that characterize Albanian SMEs, demonstrating positive trends (similarly for large enterprises and the total economy).

Table 1. General Economic Indicators of SMEs in Albania

Main indicators of SMEs	Enterprises		Number of employed		Turnover (million ALL)		Investments		(million ALL) Value added	
	2016	growth rate	2016	growth rate	2016	growth rate	2016	growth rate	2016	growth rate
Micro (1-9 employees)	102,965	3.9%	194,015	7.2%	480,991	10.5%	30,397	39%	116,583	14.77%
Small (10-49 employees)	4,413	1.2%	87,796	3.5%	563,124	1.3%	86,318	58%	107,491	-0.06%
Medium sized (50-249 employees)	996	11.6%	98,491	11.9%	420,624	3.2%	49,130	-21%	104,518	8.90%
SMEs (1-249 employees)	108,373	3.8%	380,302	7.5%	1,464,739	4.7%	165,844	20%	328,591	7.69%
Large (250+ employees)	152	9.6%	89,363	9.6%	416,923	3.3%	55,559	-20%	162,435	6.67%
Total economy	108,526	3.8%	469,665	7.9%	1,881,662	4.4%	221,404	6%	491,026	

Source: INSTAT (2019b), calculations by author with 2015 as base year

As part of the general indicators, it becomes interesting to analyse the demographic indicators of SMEs because these trends show their behaviour against external factors. For instance, referring to the birth rate of newly created enterprises (SMEs) for the period 2013-2017, the long-term average rate of this indicator for all SMEs is estimated at about 23% per year, due to the increase in the number of newly created enterprises in 2015 (INSTAT, 2019b, calculations by author). The relatively high birth rate of

newly created enterprises, especially after 2014, may be attributed to the government's reform on the formalization of the economy between 2014 and 2016. Nevertheless, the trend of this indicator over the years shows that the Albanian economy has entered into a positive development path, whereby the 'boom' of the newly created enterprises (as a strong characteristic for the first decade of the market economy) has shifted to a more stable level, estimated at an annual average rate of 10-15% (ibid.).

The stock of active SMEs also depends on the variation of non-active SMEs. According to the author's calculations based on (INSTAT, 2019c) the annual long-term average of non-active/dead enterprises is estimated around 20,000, while newly-created SMEs are estimated at about 23,000. The annual rate of newly created enterprises shows a certain stability, while the annual rate of non-active enterprises exhibits positive growth in recent years. In 2016, this indicator achieved its highest level, at about 23,000 dead enterprises, or a 35% increase compared to the previous year (INSTAT, 2019c). There is currently no study on the reasons behind such changes, though the economic formalization reform undertaken by the government during the reported period could be a factor for variations in the demographic indicators for SMEs.

Table 2. SMEs Demographic Indicators

Years	1. Newly created SME	2. Stock at beginning+newly created SME	3. Stock of SME at the end of year	4. Non active (dead) SME (2-3)	5. Non-active as % over SME's stock	6. Growth rate of newly created SME	7. Growth rate of dead SME
2014	17,377	128,531	112,537	15,994	14%		
2015	37,540	150,077	133,041	17,036	13%	116%	7%
2016	19,104	171,392	148,406	22,986	15%	-49%	35%
2017	20,256	180,935	157,784	23,151	15%	6%	1%

Source: INSTAT (2019c), calculations by author

Overall, the Albanian economy can be defined as dominated by micro and small enterprises (95% and 4% respectively in 2017) (INSTAT, 2019a) defining its economic character as a micro-business oriented one. The major economic activity is services, with a prevalence of the trade sector. Geographically, about 70% of SMEs are located in the central area of the country (mainly Tiranë – Durrës – Fier – Elbasan), proportionally related to the distribution and changes of the population. The lowest number of SMEs is observed in the northern part of the country, with about 1% of the total SMEs (INSTAT, 2019c).

According to calculations made on the basis of INSTAT (2019a), SMEs account for 81% of total employment at the national level, while their rate of employment has increased by 7.5%. Hence, SMEs constitute the main machine generating new jobs. About 78% of the total turnover in the economy is produced by SMEs and its contribution by size class (micro, small and medium) remains nearly stable, realizing a growth rate of turnover of about 5% (INSTAT, 2019b). The value added of SMEs represents almost 70% of the total value added produced in the economy and has increased by 7.7% compared to the previous year (ibid.). As such, almost all of the basic economic indicators on SMEs during the period 2013-2017 show a positive trend, positively correlated with the trend of the GDP indicator.

However, an in-depth analysis of SME performance (using not only volume data as described above, but also more complex performance indicators (see Table 4)) leads to different findings and shows a slightly negative trend. An important question for further analyses is 'why does the performance of the national economy show a positive trend, while the SME performance indicators show a negative trend?'. Large datasets are required – in the form of statistics and research analyses – to identify the reasons behind this situation. That is why there is an urgent need to introduce a full set of performance indicators, which have to be systematically measured and used, into the strategic documents for SMEs to evaluate the factors that impact SME performance. Reliable statistics and performance indicators would improve the preparation of economic policy to support the development of the SME sector.

The Importance of SME Performance and How to Measure It

Although the above-mentioned figures provide a general overview of SME performance, a more detailed analysis is required to understand the full spectrum of SMEs. Performance indicators for the SME sector are useful and informative instruments for policymakers at the local and national level. Both can assist the government's policy response and improve the current environment of the sector. A strengthened SME sector would benefit the society at large, with an increase in productivity and access to more jobs.

The government has introduced several strategic programs to support SME development over time. The most recent program, 'Business and Investment Development Strategy for the Period 2014- 2020', is in line with EU strategies for SMEs, including the principles of the Small Business Act/ SBA, produced by EC since 2011. This strategy also reflects economic development policies aimed at improving the welfare of citizens and facilitating European integration. According to the Ministry of Finance and Economy (2014), the strategy determines the main directions of the SME development policy:

• Improvement of business climate;

• Promotion of entrepreneurship at all levels of education;

• Promotion of formalized SMEs;

• Improvement of access to finance;

• Promotion of woman entrepreneurs;

• Support of start-up businesses;

• Improvement of the dialogue and partnership between public and private actors;

• Stimulation of social businesses and corporate responsibility in business operations; and

• Promotion of 'Green SMEs' models.

However, as mentioned in the SWOT-analyses of the SME sector, the presence of weaknesses such as a high level of informality and lack of credible statistics in the analysis of economic indicators (Ministry of Finance and Economy, 2014) will threaten the effectiveness of policies to support SME development, including access to diversified finances (ibid.). The latter point is highlighted in the strategy as one of the key challenges faced by the sector. Improved performance of SMEs is one of the key conditions for facing this challenge.

This strategy (compared to previous strategic documents for the first time) includes some key indicators used to monitor the achievement of strategic objectives in SME development. Nevertheless, the indicators focused on SME performance are limited when compared to the large set of SME performance indicators recommended internationally. The Albanian strategy lists mainly volume data, such as the number of enterprises, employees, number of women-led enterprises, and disbursed credits of business conducted by women. This list is not sufficient to cope with the need for in-depth analysis and assessment of SME performance. The absence of data and indicators on performance does not provide a comprehensive view of the SME sector. As a result, national policymaking processes remain ill-informed, hampering the opportunity for place-based governance of economic development, particularly at local government level. In this context, it becomes very urgent to introduce a more complete list of SME performance indicators, and to systematically guarantee their measurement as a reference to validate the performance level of SMEs.

At the European level, the model used for that purpose is called the 'SBA Fact Sheets' (The Small Business Act for Europe). Introduced in 2011, it represents a valuable tool to facilitate SME policy assessments. This document is published on a yearly basis and is prepared using the latest statistics and data. It is important to underline that this document should be considered as an additional source of

information, which helps policymakers to improve the policy process and conduct evidence-informed governance. The concept of 'SME performance' used in this document refers to a wider set of criteria, such as: entrepreneurship, second chance responsive administration, state aid and public procurement, access to finance, the single market, skills and innovation, and environment. The overall Albania SBA profile produced by EC since 2015 maintains a consistent conclusion the results should be interpreted with caution (EC, 2018). This notice is due to the lack and shortage of national data and statistics (ibid.).

Another model to evaluate SME performance is the model proposed by the Asian Productivity Organization, which includes a considerable number of indicators as described in the following table. The advantages of this model include: simplicity in application, clarity, and transparency in the compilation methods. Due to these advantages and because there is a gap in terms of a technical guide or a handbook explaining what, why, and how to compile performance indicators in the case of Albania, the above mention handbook should be considered in making a preliminary analysis of Albanian SMEs.

Table 3. Summary of SME Performance Indicators

Sales per employee	Labour cost per employee
Customer satisfaction index	Labour cost competitiveness
Complaint ratio	Employee turnover rate
Compliment ratio	Employee satisfaction index
Customer retention	Employee participation rate in team activity
Sales growth	Employee participation rate in suggestion scheme
Value added to sales ratio	Cost saving from employee involvement activities
Profit margin	Training hours per employee
Annual inventory turns	Training expenditure/sales
Defects rate	Absenteeism rate
Customer rejects/return	Capital productivity
Scrap/rework level	Sales per dollar of capital
On time delivery commitment	R&D investment ratio
Labour productivity	Capacity utilization rate

Source: Asian Productivity Organization (2015)

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In reference to this model and the availability of annual business statistics, it becomes possible to establish a national model for SME performance indicators in Albania. However, the application of the model in the Albanian context is only possible with a selection of the recommended performance indicators, mostly those related to quantitative data. The rest of the

performance indicators are missing, due to the lack of information related to qualitative surveys on SMEs in the country (Rembeci, 2017b). The results prepared for the last five years are shown in Table 5. According to them, one can observe that:

• Almost all of the performance indicators of SMEs demonstrate a downward trend during the period 2012-2017.

• More concretely, the negative trend of SME performance indicators is evident in productivity lever 1, lever 3, and lever 4. Only in productivity lever2[1] – related to 'Improvement output per unit cost of production' – do the results show a slightly positive trend.

• In productivity lever 1, related to 'Enhance sales revenue,' it is important to mention that although we have the same indicator, the methodology recommends two kinds of measurements: 'VA /sales' and 'sales per employee'. According to the results, in the first measurement we identify a positive trend over the last two years, while in the second measurement the trend is negative for the whole period. Both measurements are important to evaluate the performance of sales as one of the the most important economic indicators of SME activity.

• Also in productivity lever 1, referring to the total sales, the SME sector shows a potential increase in volume. Yet, again, further detailed analyses are needed to understand the real reasons behind the negative trend of the second measurement apart from the increase in the number of employees, evaluated as a long-term average of about 8%, with value added of about 2.8% (INSTAT 2019b, calculations by author).

• In productivity lever 3, all three measurements around 'Optimize labour productivity' present a negative trend. The worst situation is identified both in cases of 'labour productivity' and 'labour

cost competiveness'. The trend of the third indicator described as 'labour cost per employee' appears to climb and fall, and reflects the efforts of SMEs to reduce their general expenses, specifically labour costs.

• In productivity lever 4, both measurements within 'Optimize capital utilization' demonstrate a negative trend. The most significant decline is identified at the 'sales per dollar' indicator at about -10% in 2015 compared with previous year. This is due to the fact that although there are positive growth rates for both sales and fixed assets, the growth rate for sales is less than the growth rate for investements (5 % and 10% respectively) (INSTAT 2019b, calculations by author).

The overall macroeconomic situation of the country, according to statistics from INSTAT (2019a), seems stabilized and the annual GDP growth rate is increasing gradually after its lowest level in 2012. According to INSTAT (2019a), in 2017 the national economy recorded an annual growth rate in terms of volume of about 3.8% compared to the previous year. From the production point of view, the main contributors to this growth were the processing industry, construction, and almost all services, respectively estimated for about 12.22%, 7.04%, and 6.6%. In terms of the GDP structure in 2017, again the majority of economic activities came from services (48% of the total GDP). Industry and construction both represented about 20.4% and the rest of GDP was composed of agriculture and fishing (20%) (ibid.). Other macroeconomic indicators, such as the increase in job creation, decrease in unemployment rate, and positive growth rate of FDI, support the conclusion that the economy so far has entered into a stable development path.

Table 4. GDP and SME Performance during the period 2012-2017

Performance of GDP and SMEs	2012	2013	2014	2015	2016	2017
Annual GDP, in million ALL	1,332,811	1,350,053	1,395,305	1,434,307	1,472,479	1,551,281
Annual growth rate of GDP	1.42	1.00	1.77	2.22	3.31	3.82
Total number of SMEs (no. agriculture)	83,491	84,678	85,075	104,395	108,373	107,511
Annual growth rate in number of SMEs		1.42%	0.47%	22.71%	3.81%	-0.8%
Value added of SMEs in million ALL	427,875	413,550	431,149	460,332	491,026	525,642
Annual growth rate of SMEs VA		-3.3%	4.3%	6.8%	6.7%	7.05%
SME performance indicators (annual change index)						
Labour productivity		-11%	- 3%	- 9%	- 1%	-2%
VA/sales		- 7%	2%	-1%	3%	1.1%
Labour cost competitiveness		-11%	- 5%	- 5%	-6%	-3.6%
Sales/fixed assets		3%	-5%	-10%	-2%	3.5%
Profit margin, profit/sales		-5.7%	-2.3%	41.5%	1.0%	-10.8%

Source: INSTAT, (2019a), performance indicator calculations by author

However as argued above, the role of SMEs in this economic performance is unquestionable. In terms of volume, the basic indicators of SMEs show annual increases, matching the overall macroeconomic trends. Statistically, using the correlation coefficient, there is a strong relationship between the GDP indicator and the number of SMEs. That coefficient is estimated at about 0.97 (INSTAT, 2019a) for the period 1994-2017, which means that the increase or decrease in GDP figures is strongly related to an increase or decrease in the number of SMEs. Nevertheless, detailed analyses (especially those related to SME performance indicators) demonstrate a different trend, which reverses those of the volume data, and is negative. Not only should the reasons behind these figures be investigated through further studies, but a key take-away is that models of indicators for SME performance need to be expanded to include qualitative data. This would of course require the introduction of statistical surveys being undertaken on regular basis.

Conclusions and Recommendations

SMEs are highly important for the still fragile Albanian economy due to their significant contribution to GDP and employment (70% and 80%, respectively, for the year 2017).

In terms of employment, the contribution of SMEs is increasing on a yearly basis. In 2017, the growth rate is evaluated to be 7.5% compared to the previous year, with SMEs remaining the main generator of new jobs in the national economy. The Albanian economy is characterised by a high birth rate of SMEs estimated at approximately 13% annually for the period 2013-2017. This can partially be considered to be as a result of the formalization reform initiated by the government, and/or an improved business environment in recent years.

During the last five years, the majority of the general indicators for SMEs demonstrate a positive growth rate (positively correlated with GDP growth rates), while the performance indicators show a downward trend. This mismatch between trends in the data indicates not only that the SME sector needs support for improving its performance and empowering its contribution to the national economy, but also that the current data (mostly volume-based) are not sufficient to inform policymaking in the economic development sector and therefore improve governance. In general, the current model of profiling SMEs remains incomplete, due to the lack of availability of detailed data, especially related to qualitative surveys on entrepreneurship and management issues.

Table 5. Summary Table of Performance Indicators in Organizational Terms, 2012-2017

	Indicator	What it measures	Formula	Total Economy/SME						Index of yearly changes				
				2012	2013	2014	2015	2016	2017	2013	2014	2015	2016	2017
Productivity lever - 1 Enhance sales revenue														
1	Sales per employee	Efficiency of market strategy	VA/sales	0.277	0.253	0.248	0.255	0.261	0.258	-8.6%	-1.9%	3.0%	2.2%	-1.13%
2	Sales per employee	Efficiency of market strategy	Sales per employee	4.895	4.751	4.690	4.139	4.006	4.133	-2.9%	-1.3%	-11.7%	-3.2%	3.17%
3	Sales Growth	The potential of the company for growth	[sales (t) -sales-(t 1)/sales -(t1)]		0.058	0.063	0.036	0.044	0.074		8.1%	-42.2%	21.7%	
Productivity lever - 2 Improve output per unit cost of production														
1	VA to sales ratio	Proportion of sales created by purchased materials and services	VA/sales	0.784	0.727	0.713	0.708	0.729	0.697	-7.2%	-2.0%	-0.7%	3.0%	-4.4%
2	Profit margin		Profit/sales	0.067	0.063	0.061	0.087	0.088	0.078	-5.7%	-2.3%	41.5%	1.0%	-10.8%
Productivity lever - 3 Optimize labour utilization														
1	Labour productivity	Efficiency and effectiveness of employees in generating VA	VA/number of employees	1353	1200	1162	1057	1045	1066	-11.3%	-3.2%	-9.1%	-1.1%	2.0%
2	Labour cost per employee	Average remuneration per employee	Labour cost/ number of employees	0.408	0.407	0.417	0.401	0.421	0.466	-0.1%	2.5%	-3.9%	5.0%	5.8%
3	Labour cost competitiveness	Efficiency and effectiveness of company in terms of its labour cost generating VA	VA/labour cost	3.320	2.949	2.787	2.636	2.482	2.393	-11.2%	-5.5%	-5.4%	-5.9%	-3.6%
Productivity lever - 4 Optimize capital utilization														
1	Capital productivity	Efficiency and effectiveness of fixed assets in generating VA	VA/fixed assets	2.875	2.539	2.378	2.211	2.218	2.269	-11.7%	-6.3%	-7.1%	0.3%	2.3%
2	Sales per Dollar (unit value of money) of capital	Efficiency and effectiveness of fixed assets in generating sales	Sales/fixed assets	10.398	10.049	9.596	8.655	8.499	8.793	-3.4%	-4.5%	-9.8%	-1.8%	3.5%

Source: Asian Productivity Organization (2015), INSTAT (2019b; 2019c) and author calculation

In these circumstances, the governments (local and national) should collect and interpret SME profiles with caution, due to the lack of data in various aspects of SME production and management processes. As a first step, the model of performance indicators for SMEs needs to be expanded to include qualitative data. One of the minimum requirements in order to achieve this would require the introduction of further statistical surveys conducted on a regular basis by INSTAT.

A national database should be established containing quantitative and qualitative micro data for SMEs. Access to this database should be regulated by law, to account for all stakeholders, including those who deal with SME policy and research analyses. This would lead to the adoption of a complete and systematic performance measurement system for SMEs. The same model should be used also at the regional and local level so that regional disparities can be better identified and more effective regional development measurements/policies can be endorsed.

Notes

1. Productivity Lever 1: Enhance sales revenue;
Productivity Lever 2: Improve output per unit cost of production;
Productivity Lever 3: Optimize labour utilization;
Productivity Lever 4: Optimize capital utilization

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