

# Development of Small and Medium Entrepreneurship in the Republic Of Croatia

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## Abstract

Entrepreneurship is a key driver of economic growth and a generator of employment opportunities in all modern economies across the world. Small and medium enterprises (SMEs) are the engines of modern entrepreneurship. In the Republic of Croatia, SMEs are also indispensable in the effort to boost employment and economic growth. The global economic crisis has virtually brought the national economies worldwide to a halt, causing a considerable decline in production, consumption, and gross domestic product. In such conditions, the development of individual entrepreneurial competencies and entrepreneurial culture represents the main preconditions for successful economic growth and development. The SME sector plays a key role in achieving this by increasing the national economy's competitiveness in the regional and European Union markets. The aim of this paper is to present the position of entrepreneurs in the Republic of Croatia, to identify challenges that come with setting up a business, and to describe the state of small and medium entrepreneurship in the Republic of Croatia.

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## Introduction

Small and medium enterprises have long been recognised as an important building block of economic growth. They have a large potential, which is corroborated by the fact that they account for 99% of all enterprises and about 60% of all employees in the European Union. Entrepreneurship is a key driver of national economies. The importance of SMEs has also been recognised by policymakers at the EU level. Thus, various action programmes have been adopted, such as the Small Business Act, Horizon 2020 and COSME, with the aim of supporting SMEs to become competitive through research and innovation, and facilitate their access to finance.

In the Republic of Croatia, there are more than 78,000 companies classified as SMEs, which employ 47.5% of the total number of employees in Croatia. Entrepreneurship is slowly becoming a leading sector and a driver of the country's national economy.

The paper describes the historical development of entrepreneurship, further, the concept of entrepreneurship is defined, advantages and disadvantages of entering entrepreneurship, research methodology, then the results and discussions are presented and finally, a conclusion is made.

## Literature review

### *A short history of entrepreneurship*

The history of entrepreneurial activity can be traced back to the period between the 12<sup>th</sup> and 15<sup>th</sup> century. At the time, it included trading, money lending and currency exchange, shipping, but also expeditions. The early entrepreneurs were pirates, feudal lords, government officials, speculators, merchants and artisans. The first trading companies were established in Italy in the 12<sup>th</sup> century. In the late 14<sup>th</sup> century, permanent associations were formed that were organised in a similar fashion to today's public limited companies. The enterprise, in economic terms, was created when a for-profit activity became independent from the entrepreneur's household, that is when the enterprise was established as an autonomous economic entity. The company, as a more widely spread phenomenon, appeared only in the 15<sup>th</sup> century (Hisrich et al., 2008).

Creative entrepreneurship developed only in the 17<sup>th</sup> century. Until then, there were two types of entrepreneurs: the early entrepreneur, who traded in slaves, fur, animals, etc., and the early-capitalist entrepreneur, who exchanged European products for tropical and subtropical goods. At the moment when the entrepreneur began to perform his entrepreneurial function continuously and permanently, an enterprise was created as an economic and organisational entity for performing economic activity. Specialisation in the field of trade and, in particular, the separation of banking activities began only in the 18<sup>th</sup> century. In the mature stages of industrial society, opinions emerged suggesting that, on the one hand, the role of entrepreneurship was diminishing and it was becoming obsolete, and, on the other, that in large corporations the ownership and the management functions were separating, whereby the management function was taken over by managers and technostructures. Market competition, the development of science and technology, and the struggle for economic dominance have enabled the growth of profits and led to the concentration of production and capital, the creation of multinational companies, corporate groups, trusts and other organisational forms that have become symbols of economic development in today's capitalism. Therefore, in modern business corporations, the management function is performed by a corporate manager, not an individual entrepreneur (Škrtić, 2002).

Today, even small entrepreneurs need to embrace information technologies, especially if they wish to export to global markets. A trend has emerged in developed western countries, whereby consumer demand is shifting from branded products of recognised manufacturers to no-name products, thus creating significant opportunities for smaller companies (Bobera et al., 2015).

### *The notion of entrepreneurship*

The term entrepreneurship comes from the French word *entreprendre*, which is usually translated as "to undertake" and implies taking action rather than waiting for something to happen (Brusić et al., 2009). Entrepreneurship is the process of creating new value through various activities, whereby the entrepreneur recognises a new business opportunity, establishes a company and manages it, mobilises the necessary resources to take advantage of that opportunity, develops a product, captures a market, sells the product, distributes increased (newly created) value, and recognises a new business opportunity (Tafra, 2012). According to the Croatian dictionary "An entrepreneur is an individual or a legal entity that innovates or improves work processes and seeks to profit by taking risks" (Hrvatski enciklopedijski rječnik, 2004). An entrepreneur is a person who organises and manages a company and takes risks to make a profit, a person with knowledge in the fields of marketing, finance, management, and business decision-making that has been acquired through formal education. Several key factors are involved in the entrepreneurial process: the entrepreneur, the business opportunity, and the resources needed. The entrepreneurs risk their money, time and reputation (Pejić Bach et al., 2018). They must have a vision, know how to set business goals and design a business strategy, and be able to develop a business plan. The most important factor in the entrepreneurial process is the entrepreneur because, without him, the entrepreneurial process cannot be initiated. A business idea is an idea for a new product or service that has not yet been validated in business, while a business opportunity is a validated and viable business idea. A product can be an idea, a service, a commodity, or any combination of these three concepts (Ženko et al., 2017). The main precondition for entrepreneurial activity is the existence of such economic freedoms that allow the transfer of physical and human resources from old and unprofitable branches of economic activity to new and profitable ones (Hunady et al., 2019). The freedom to transfer resources is needed in order to take advantage of business opportunities by introducing new and higher-quality products, new production and business processes, by increasing the efficiency of production, and by reaching out to domestic and foreign customers (Ožanić, 2011).

### *Advantages and disadvantages of becoming an entrepreneur*

Empirical research shows that small business owners believe that by working hard they will make more money and be happier than being a salaried employee. According to the respondents, the main advantages of becoming an entrepreneur are (Scarborough et al., 2009): being in control; being able to change things; being able to fulfil one's potential; unlimited income potential; social prestige and having an opportunity to pursue one's passion.

One of the advantages of becoming an entrepreneur is being in control - owning a business gives the entrepreneur the freedom and ability to achieve his goals. True entrepreneurs do not think of their daily business activities as work (Heck et al., 2006). The most successful entrepreneurs choose the activity they are most interested in and enjoy the most, following the advice of Harvey McKay who said: "Find

something you love to do, and you'll never have to work a day in your life" (Škrtić & Mikić, 2011).

Although owning a business provides many benefits and opportunities, everyone entering entrepreneurship must be aware of the potential disadvantages: income uncertainty; risk of loss of invested capital; undefined working hours and hard work; lower quality of life in the initial phases; high level of stress; unlimited liability and discouragement (Pejic Bach et al., 2016).

Running one's own business can be a very positive experience, but also a very stressful one. Most entrepreneurs invest significant amounts of money in their businesses, leaving behind the security of a job with regular pay (Moric, 2013). Often, entrepreneurs take out a mortgage loan, i.e. invest their entire property in their business. In such cases, the failure of business would mean financial and psychological strain, which causes high levels of stress and worry (Zahra & George, 2002). Most entrepreneurs are likely to face many problems that they will not be able to solve due to lack of knowledge (Jurčić et al., 2020). At the same time, the decisions they make directly affect the success or failure of the company, as well as everyone involved in the business (Dumičić et al., 2014). Entrepreneurs quickly learn that they are indistinguishable from their company and that starting a business requires commitment, discipline and perseverance. Successful entrepreneurs also know that obstacles should not discourage them, but rather drive them to do even better (Mencer, 2012).

## Methodology

A survey was conducted on a sample of 155 respondents during October 2019. The sample comprised persons of different sex, age, educational level, employment status and social status to make sure that it is as representative as possible in all key characteristics.

The goal of the research is to determine the percentage of respondents who are considering starting their own business and identify the biggest challenges for start-ups and nascent entrepreneurs. Furthermore, the paper aims to establish whether, in the respondents' opinion, the Republic of Croatia provides sufficient support to prospective and current entrepreneurs. The null hypotheses relating to the stated objectives are as follows: (1) A large number of individuals are considering starting their businesses. (2) The biggest challenge in starting a business is bureaucracy. (3) The Republic of Croatia provides sufficient support to prospective and current entrepreneurs.

## Results

### *Entrepreneurship in general*

**Entrepreneurship intentions.** In total, 41.3% of the respondents are considering starting their own business, 9.7% of them already have their own business, while 49% are currently not considering that idea. The results indicate that existing business owners are the least represented in the sample, while the largest proportion of respondents are not considering the idea of becoming an entrepreneur at present. It may be concluded that the entrepreneurial climate in the Republic of Croatia is still unfavourable, despite numerous reforms and development strategies that have been implemented to strengthen the entrepreneurial potential and foster an entrepreneurial culture. In line with the current Entrepreneurship Development Strategy, entrepreneurship and the economy of both the Republic of Croatia and

the European Union will develop in the long term only if a large number of Croatian citizens start seeing entrepreneurship as an attractive and viable option for their future.

**Reasons for starting an entrepreneurial activity.** For the majority of the respondents (38.1%), the reason for starting their own business is income potential. 37.4% believe that they have a good business idea, 21.9% are dissatisfied with their current job, while for 2.6% the reason would be the fact that they cannot find employment. The results suggest that the majority of the respondents would start their own business for income potential, followed by those who would start a business because they believe they have a good business idea. It is interesting that the percentage of respondents who would start their own business because they are unemployed, i.e. because they need a job, is the smallest. About 22% of the respondents are dissatisfied with their current job, which is not too large a proportion.

**Advantages and disadvantages.** For the majority of the respondents (49%), the biggest advantage of embarking on an entrepreneurial career is the greater possibility of exploiting their potential. 24.5% find it is financial independence, 14.2% believe it is being in control, while 12.3% reported it is an opportunity to pursue their passion. None of the respondents considered social prestige the greatest advantage of entering into entrepreneurship. In total, 38.7% of the respondents believe that the biggest downside of entering into entrepreneurship is income uncertainty, 37.4% consider that it is the risk of loss of invested capital, 12.3% find that it is the difficulties arising from the lack of knowledge and experience, while for 11.6% the biggest disadvantages are undefined working hours and hard work.

### *Entrepreneurship in the Republic of Croatia*

**Support for entrepreneurship.** The respondents were asked to rate their level of agreement, on a scale of 1-5, with the following statement: "The Republic of Croatia provides future entrepreneurs with sufficient financial incentives". 3.2% of the respondents strongly agree, while 19.4% strongly disagree with this statement. Most SMEs have difficulty with obtaining start-up funding because of an insufficient supply of microloans. The financial system in the Republic of Croatia has yet to be developed to provide a comprehensive product portfolio. The respondents were asked to rate their agreement, on a scale of 1-5, with the following statement: "The Republic of Croatia seeks to increase the number of entrepreneurs through tax reform by providing them with tax reliefs". 3.2% of respondents strongly agree, while 22.6% strongly disagree with this statement. The respondents were asked to rate their agreement, on a 1-5 scale, with the following statement: "The entrepreneurial climate in the Republic of Croatia is favourable". 0.7% of the respondents strongly agree, while 40.6% strongly disagree with this statement. Most respondents (95.5%) find that the government does not provide sufficient support for entrepreneurs, while 4.5% of them believe that entrepreneurs have sufficient government support.

**Information on starting the business.** The majority of the respondents (94.2%) believe that the citizens of the Republic of Croatia are not sufficiently informed about how they can start a new business, while only 5.8% believe that citizens have sufficient information available. The respondents were asked to rate their agreement, on a 1-5 scale, with the following statement: "The Croatian Chamber of Commerce provides entrepreneurs with sufficient information and support". 0.6% of the respondents strongly agree, while 18.1% strongly disagree with this statement. Most respondents (72.9%) do not know all the details required to start a business, while 27.1% find that they have all the information they need.



**Obstacles.** According to the respondents, the biggest obstacle for young entrepreneurs in the Republic of Croatia is corruption (36.1%), followed by frequent legislative changes (27.1%), lack of capital (26.5%), unfair competition (5.2%), customs procedures (1.9%), bureaucracy (0.6%), all the stated elements (1.3%), and taxes (0.6%). Besides, the respondents were asked to rate their level of agreement, on a 5-point scale, with the following statement: "In the Republic of Croatia, potential entrepreneurs are discouraged by bureaucracy". In total, 60.6% of the respondents strongly agree with this statement, while only 3.9% strongly disagree with this statement.

**Utilization of EU funds.** The respondents were asked to indicate their level of agreement, on a 5-point scale, with the following statement: "Entrepreneurs in the Republic of Croatia fully exploit EU funding opportunities". 2.6% of the respondents strongly agree, while 16.1% strongly disagree with this statement.

**Education for entrepreneurship.** The respondents have rated their agreement with the following statement on a scale of 1-5: "The education system in the Republic of Croatia promotes entrepreneurial initiative and innovativeness in young people". 2.6% of the respondents strongly agree, while 31.6% strongly disagree with this statement. The results suggest that the Republic of Croatia needs an education reform to shift the focus towards entrepreneurship. However, such reforms cannot be implemented without sufficient financial resources. Investing in entrepreneurial education will bring long-term benefits to society and the economy, given the significant role of entrepreneurship in economic growth.

## Conclusion

The survey results show that the majority of the respondents (almost 50%) are not considering starting their own business, while the rest either are considering it or have already done it. The majority reported income potential and having a good business idea as the reasons that would prompt them to start their own business. The respondents consider that the greatest advantage of entering into entrepreneurship is the possibility to fulfil their potential, while the uncertainty of income and the risk of loss of invested capital are reported as the greatest disadvantages of becoming an entrepreneur. The respondents find that entrepreneurs in the Republic of Croatia are discouraged primarily by bureaucracy. Most respondents neither agree nor disagree that entrepreneurs in Croatia fully exploit EU funding opportunities. They believe that the education system does not promote entrepreneurial initiative and innovativeness in young people. According to the respondents, the Republic of Croatia does not provide sufficient financial incentives for future entrepreneurs. The respondents neither agree nor disagree that the Croatian Chamber of Economy provides entrepreneurs with sufficient information and support. The same opinion is given for the government's efforts to increase the number of entrepreneurs by providing them with tax reliefs. Most respondents disagree with the statement that the entrepreneurial climate in Croatia is favourable. The majority of the respondents consider that the citizens of the Republic of Croatia are not sufficiently informed about how they can start a new business and that they do not have sufficient information about what is required to start a business. Most of them believe that the government does not provide sufficient support and find that the biggest obstacles to young entrepreneurs are corruption, lack of capital and frequent legislative changes.

The presented results indicate that most respondents do not consider starting their businesses, which is a cause for concern. A vigorous entrepreneurial climate contributes to employment, the main indicator of a healthy economy. Furthermore,

entrepreneurship increases the efficiency and competitiveness of companies and helps to adapt the economic system to the modern global market. It is the authors' opinion that through education reforms, the Republic of Croatia could enhance entrepreneurial capacity and raise awareness of the role of entrepreneurship in society. This could, in turn, stimulate entrepreneurial activity and reduce the unemployment rate.

Entrepreneurship is central to achieving economic prosperity. Thus, it is particularly important to foster entrepreneurial spirit to stimulate its growth, which will, in turn, drive innovation, increase competitiveness and positively affect the entire economy. Increasing market globalisation and democratic processes have further highlighted the importance of entrepreneurship as a driver of economic growth.

National strategies have had a positive effect on entrepreneurship development, but there are still problems that need to be addressed to encourage entrepreneurial initiative as much as possible. The difficult macroeconomic environment has negatively affected this sector by closing down small businesses due to reduced demand and sales. The tax rates imposed by the Croatian tax system are high. The system itself is subject to frequent changes, and tax policies do not stimulate entrepreneurial growth.

In conclusion, the research results indicate that the Republic of Croatia needs to undertake a thorough education reform to promote entrepreneurship and thus stimulate productivity and employment. Moreover, the country needs to implement robust entrepreneurship development strategies. Reforms of the tax system and public administration are also needed to enhance the economic strengths and competitive advantages of the small business sector at the national and global levels.

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