

**ECONOMIC DEVELOPMENT BEYOND RESOURCES
SME POLICY FOR AZERBAIJAN**

By

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Executive Summary

The problem of the current research is the SME sector development policy for Azerbaijan. As there is a resource curse problem in the country, the Azeri government has decided to pursue the policy of SME sector development in order to diversify economy away from natural blessings and to develop the non-oil sector. I have investigated the business incubation model of SME sector development that was practiced in Kazakhstan in this research. Key insights and policy learning have been drawn from the success and failures of the case of Kazakhstan. In the light of these, policy recommendations are provided.

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Dedication

Sincerely dedicated to **Elshan Musayev**. I strongly believe that he will be able to realize first business incubation project in Azerbaijan very soon.

Table of Contents

| | |
|--|-----------|
| CHAPTER 1 - INTRODUCTION | 1 |
| 1.1 AIMS OF RESEARCH AND METHODOLOGY | 2 |
| 1.2 RELEVANCE..... | 4 |
| 1.3 ORGANIZATIONAL STRUCTURE..... | 4 |
| 1.4 SMALL FIRMS AND ENTREPRENEURSHIP: A PRIMER ON AZERBAIJAN | 5 |
| CHAPTER 2 –SMEs, SOCIO-ECONOMIC DEVELOPMENT AND PUBLIC POLICIES..... | 9 |
| 2.1 ROLE OF SMEs IN ECONOMIC AND SOCIAL DEVELOPMENT..... | 11 |
| 2.2 PUBLIC POLICIES FOSTERING SMEs | 13 |
| CHAPTER 3 – SME POLICIES IN RESOURCE RICH ECONOMIES: THE PROXY CASE OF KAZAKHSTAN | 19 |
| 3.1 RATIONALE FOR CHOOSING KAZAKHSTAN AS A PROXY CASE FOR AZERBAIJAN..... | 19 |
| 3.2 BRIEF OVERVIEW OF NATURE AND CHARACTERISTICS OF SMEs IN KAZAKHSTAN | 24 |
| 3.3 BUSINESS INCUBATORS IN KAZAKHSTAN | 25 |
| CHAPTER 4 – EFFECTIVENESS OF KAZAKHSTAN POLICIES: IMPLICATIONS FOR AZERBAIJAN..... | 29 |
| 4.1 ANALYSIS OF RESULTS OF BUSINESS INCUBATION IN KAZAKHSTAN | 29 |
| 4.2 KEY INSIGHTS DRAWN FROM THE CASE KAZAKHSTAN FOR AZERBAIJAN..... | 34 |
| CONCLUSION AND POLICY RECOMMENDATIONS | 36 |
| REFERENCE LIST | 39 |
| APPENDICES | 43 |

List of Boxes and Figures

Box 1: The State of the SME sector in Azerbaijan

Box 2: Definitions of SME's

Box 3: Assistance by International Organizations

Box 4: Background of Business Incubation

Box 5. infoDev Incubator Initiative

Figure 1: The New Thresholds

Figure 2: Structure of Merchandise Products

Figure 3: Map of Kazakhstan

Figure 4: Overview of Situation in South Kazakhstan

List of Abbreviations

BI – Business Incubator

EBRD – European Bank for Reconstruction and Development

EU – European Union

FDI – Foreign Direct Investment

GDP – Gross Domestic Product

GTZ - German Technical Co-operation Agency

ILO – International Labor Organization

IFC – International Finance Corporation

NGO – Non-governmental Organization

SME – Small and Medium-sized Enterprise

SMB - Small and Medium Business

SSCAR – State Statistical Committee of Azerbaijan Republic

UNECE - United Nations Economic Commission for Europe

UNDP – United Nations Development Program

UNIDO – United Nations Industrial Development Organization

USAID - United States Agency for International Development

WB – World Bank

Key words

Small and medium-sized enterprise (SME), public policy, socio- economic growth, employment, business incubation, resource curse

Chapter 1 - Introduction

Nowadays, it is not surprising that small and medium scale enterprises are in the spot light of public policy. Although in the era of market globalization large enterprises took so much time and efforts of policy makers, policies are much more focused on SMEs rather than LEs. Small firms are a major attraction for the governments and policies not only because of their ability to diversify economy, achieve sustainable economic development and macroeconomic stability, increase competitiveness and dynamism, reduce unemployment by creating new jobs and promote innovation, but also because of their assistance to governments to realize their social objectives like poverty reduction, creating enterprise culture and skills, advancing women entrepreneurship and minority inclusion, and having “stronger growth for everyone” (Schlögl 2004).

Precisely because of the above mentioned reasons SMEs achieved success and significance in almost all developed countries for a long period of time (McIntyre 2003, 1). Currently, countries of transition economies and also countries with “resource curse” tried to foster this segment in particular, in order to diversify economy, shape new values, promote entrepreneurship, thus providing for social, cultural and personal welfare and overall inclusive economic development (ibid.). In this regard, Azerbaijan is also not exception. Although oil-gas sector always played a dominant role in the economy of the country, the Azerbaijani government has also started to pursue significant policy to develop entrepreneurship and SMEs, after being prone to resource curse. The basic aims of this policy was diversifying away from resources and developing non-resource sector of economy and reducing unemployment. The influential role of SMEs is also acknowledged by current President of Azerbaijan in person. During his speech at the regional business forum President Ilham Aliyev emphasized that “[t]he development of small and medium business assumes

paramount importance for Azerbaijan (Today.az 2010). He also stated that making the SMEs a major part of the economy is one of the key priority policies of the country (ibid).

However, only with the help of *right* and well-structured public policies on SMEs, all the above mentioned objectives and goals of the Azerbaijani government can be reached. Therefore, this research aims to investigate the policy proposed by the Azeri government and will examine to what extent recent theoretical review from literature and empirical findings from the case study may assist to pursue a better policy in terms of SME sector development.

1.1 Aims of Research and Methodology

The Azerbaijani government is trying to revitalize its economy by the policy of promoting SMEs as the main factor for developing non-oil sector of the economy. That is why, the main aim of my study is to analyze and examine the proxy case study of Kazakhstan in order to find what the Azeri government should do or not to do in drawing learning from Kazakh experience of SME sector development policy which focused on business incubation to foster the SMEs. The other major aim is to define the general patterns of public policy on SME sector development and their contribution to socio-economic development in resource rich countries.

The case will examine differences in outcomes using such benchmarks as business incubation model of SME sector development policy in Kazakhstan and draw insights for the case of Azerbaijan. The case will give lesson-drawing for Azerbaijan by bringing significant empirical evidence to the study. The reason why use a proxy case instead of studying Azerbaijan itself is that, Azerbaijan has not applied any policy model so far. However,

Kazakhstan has some experience in application of business incubation initiatives as a part of its SME policy and also there is more data in Kazakhstan than for the case of Azerbaijan

I have selected the proxy case study of Kazakhstan which is comparable to Azerbaijan. The reasons why I primarily interested in looking at Kazakhstan are as follows: 1) both countries are abundant with natural resources and suffer from “resource curse” 2) both have non-inclusive and imbalanced development, regions are declining 3) both are transition economies, post communist countries with authoritarian regime 4) both of the countries linked their major national, socio-economic objectives with SME sector development trying to achieve macroeconomic stability by diversification 5) both countries received international assistance for SME sector development and finally, 6) both countries adopted support regulations, specific measures and programs, established SME funds for fostering small business development.

I have used mainly qualitative data sources including books, academic journals and policy papers, annual reports, think tank articles, internet/web resources. The research also entails some primary sources such as official government documents and reports on Azerbaijan.

Nonetheless, it is worth noting some limits of my study, mainly, the extent to which I expect to see the “hard” results in a socio-economic development like diversification of economy, reduction of poverty and unemployment, etc. with the implementation of SME policy like business incubation.

The other limitation that I have is the lack of data on results and contributions of business incubation in Kazakhstan. It was difficult to access, because Kazakh government did not report the results officially. That is why, the existing sources is complemented by interview

conducted by me with World Bank expert Stefan Schandera who provided capacity building in planning and management at SODBI Business Incubator Shymkent, Kazakhstan and coached the coordination team of the Central Asian Business Incubators Network in Kazakhstan.

1.2 Relevance

The research contains three important novelties. Although a lot of research has been done on small enterprises in the country, there was no empirical application of business incubation for SME sector development in Azerbaijan so far. There was no thorough research and empirical evidence in national level to investigate the effects of precisely such a strategy in the country. This thesis challenges this approach for the first time and evaluates the possible outcomes of business incubation model by drawing learning insights from a proxy case of Kazakhstan, as this country already introduced this model with the aim of contributing to development of SMEs sector. The second originality is related to that, very few or almost no studies from the public policy angle conducted on SME development in Azerbaijan, therefore, the research tries to confront this gap in the field. Thirdly, it elaborates the role and importance of SMEs in resource rich economies.

1.3 Organizational Structure

The thesis is composed of four chapters. The first chapter will provide introductory and background information and define the main rationale for the study. The second chapter of the thesis highlights the most relevant literature on SMEs, and in this chapter the debates of scholars on roles of SMEs and SME policies will be discussed in depth. Then comes third chapter with a description of a proxy case of Kazakhstan, an empirical part of the thesis, however, discussion of the results of the case and key insights drawn is being left for the next

chapter. In the fourth chapter the main research findings and what they actually mean for Azerbaijan will be set forth. I will provide deep insight into analytical framework and the proxy case, review some of the policy issues which comes out from the analysis. Finally, practical recommendations on SME policies are presented for government of Azerbaijan, other relevant structures & bodies, and policy makers.

So, before moving to second theoretical chapter I am providing a brief primer on Azerbaijan.

1.4 Small firms and entrepreneurship: A Primer on Azerbaijan

After gaining its independence and following oil and gas field discoveries Azerbaijan began to implement its own independent economic policy. Starting from Production Sharing Agreements (PSAs) signed with famous foreign oil companies on developing oil and gas fields in the Caspian Sea and after the construction of the Baku-Tbilisi-Ceyhan (BTC) pipeline and the South Caucasus Gas pipeline a considerable amount of Foreign Direct Investment (FDI) flowed to the country. Small and developing resource economy such as Azerbaijan found itself to be relatively wealthy because of the oil and gas sector. Thanks to resource blessings country started to perform well in terms of GDP development and achieved considerable results in the field of socio-economic development (Azerbaijan.az 2010). The average annual GDP growth rate for 2003-2008 was 20 percent - led mainly by oil and gas production. According to the World Bank, in 2006, the country had the highest growth rate worldwide: 34.5 percent¹. State budget has increased more than 10 times over the past five years. However, Azerbaijan has shown growth numbers only because of the oil and gas production and export and it was difficult for a country to keep those growth rates for a long period of time with already being prone to Dutch Disease (Mahmudov 2002, 18). The oil and gas blessings turned out to be a curse for Azerbaijan, economic growth became not

¹ World Bank, country brief on Azerbaijan, 2009

sustainable as all the other sectors were declining. For example, SME sector was one of them, the SSCAR reports that there were 24 thousand small firms in 2000, however this number decreased to 13 thousand in 2007, which show approx. a 55% decline in number of enterprises (SSCAR 2008, 1).

One of the side aspects of the “resource curse” and another reason to foster SMEs is non-inclusive economic development, meaning underdevelopment of the regions. Almost all the oil and gas industry of Azerbaijan is focused in the Absheron Peninsula where capital Baku is situated. There are deep discrepancies between Baku and other regions of the country in terms of economic development. In this regards small scale production is not exception. According to State Statistic Committee, 42% of all small and medium sized enterprises are concentrated in Absheron region and Baku (State Statistic Committee 2008, 14). Moreover, precisely these 42% of SMEs account for 78% of whole production by small and medium sized enterprises (ibid).

For this reason, entrepreneurship and SME sector development in the rural regions was the foremost part of the both “State Program on Socio-Economic Development of Regions” which was announced firstly for 2003-2008, and secondly for the period of 2009-2013 under the strict instruction of President Ilham Aliyev. According to government policy makers, the reason was and still is that SMEs can play a crucial role for diversification of economy, sustainable development of non-oil sector, ensuring job creation and achieving macroeconomic stability, enhancement of entrepreneurship conditions, increase of flow of investment into the economy, not least but last for reduction of poverty and consistent improvement of people’s welfare (APA.az. 2010).

Not pursuing relevant measures and policies for a long period of time made Azerbaijan to face the problem of one single sector of economy to be dominant. Taking into consideration above mentioned reasons, policy makers in the country started to think the ways to restructure oil and gas dependant economy to more competitive market economy. Oil rich transition economy began to develop non-oil sector of economy and diversify it by giving importance to small and medium sized entrepreneurship (Azerbaijan.az 2010). Development of SMEs started with the strong privatization policy and market liberalization implemented by government. Almost all the state owned small firms (SOs) denationalized. As a consequence of it, the share of small firms in the economy increased a bit (Szabo 2006, 121). However, compared to oil and gas sector, SMEs play a minor role in the economy of the country; for instance, the share of SMEs in GDP was 15% in 2006. That is why also development, support and promotion of small enterprises have been accepted as the major decision of development “non-oil” sector of the national economy (ibid).

Box 1. The State of the SME sector in Azerbaijan

The aim of this box is presenting the current status and economic dimensions of SMEs in Azerbaijan. The official definition currently applied to SME units in Azerbaijan is regulated by the decree No. 57 of the Cabinet of Ministries of the Republic of Azerbaijan on “Identification of the Small Entrepreneurship Subjects by Types of Economic Activity” issued on April 20, 2004 small businesses are defined as follows according to sector (IFC 2009, 28):

| Economic Sector | Headcount | Annual Turnover |
|--|------------------|---------------------------------------|
| Construction and industry | less than 40 | less than 200.000 manats (~\$247,000) |
| Agriculture | less than 15 | less than 100.000 manats (~\$123,500) |
| Wholesale trade | less than 10 | less than 300.000 manats (~\$370,500) |
| Retail trade, transportation, service and other types of economic activity | less than 5 | less than 100.000 manats (~\$123,500) |

According to the legal framework of Azerbaijan, there are two types of micro, small and medium sized entrepreneurship in the country: individual entrepreneurs (IEs)– natural persons who are sole owners of the enterprise; and small and medium enterprises (SMEs) who form legal entities (IFC 2009, 35).

According to the calculations by the State Statistics Committee, 93% of registered entrepreneurs are individual entrepreneurs and 7% are small, medium and large companies (IFC 2009, 35). As it seems from numbers, the majority of entrepreneurs are individual entrepreneurs (ibid). Although there was an increase in number of SMEs starting to operate in 2009, this growth didn't contribute that much to the GDP of the country (IFC 2009, 35).

SMEs recognized widely as a solution to major economic and social problems like unemployment, poverty alleviation, diversification of economy, development of non-resource sector within all the below mentioned programs and legislature adopted by Azerbaijani government from 2002 to 2007 for SME-sector development and stimulating entrepreneurship (Szabo 2006, 122):

- “State Program on Development of Small and Medium Scale Entrepreneurship in the Azerbaijan Republic” for the period of 2002–2005, approved by the President Decree No 753 as of 17 August 2002;
- The new Law on “State Support for small entrepreneurship” (No 508-IIQD/ as of 4 November 2003)
- The Law on “Entrepreneurial activity” (No 509-IIQD as of 4 November 2003)
- Measures for the Development of Entrepreneurship (MED) signed and approved by the Presidential Decree on April 30, 2007

In the primer on Azerbaijan, I tried briefly to refer to the oil dependence as a factor determining the country's economic path & development, as well as the major factor for triggering the need for development of SME sector. In the next chapter, I examine the socio-economic role of SMEs and public policies for their development stemming from the literature reviewed.

Chapter 2 –SMEs, Socio-Economic Development and Public Policies

“Small is Beautiful”

Joseph Schumpeter

The detailed literature review presented in this chapter is necessary and useful for the following reasons: First of all, it examines literature bringing out theoretical background and debate on SMEs and combines those debates within the framework of this thesis. Secondly, it briefly discusses the entrepreneurship history, development and position in the economy, the evolution of role of SMEs, how they became essential during the time and links entrepreneurship and SMEs to socio-economic growth. Finally, it tries to answer the question why SMEs should be a target for a public policy, and why they are inevitable for governments.

Starting from mid 1970s, with deregulation and globalization, Joseph Schumpeter’s famous concept “Small is Beautiful” began to receive new meanings and the role of small entrepreneurship in the economy and society changed dramatically (Audretsch 2004, 168). Previously, scholars believed that large enterprises were superior to small firms in terms of all factors of economic performance. They argued that SMEs were less efficient, had not committed to innovation activity, and they offered low employee compensation (Audretsch 2004, 168). A heated alternative debate has recently revived that small entrepreneurship has much more significant role in the economy that had been recognized in the previous economics literature (Acs and Audretsch 1993, 1). According to Audretsch and Thurik (2004), small enterprises started to flourish because of mounting globalization, “which has

shifted the comparative advantage towards knowledge-based economic activity”. They argue that knowledge changed to a factor of production and knowledge spillovers in SMEs become a source of economic growth. In this sense, knowledge emerged in one small enterprise started to commercialize in a new firm

Nowadays, substantial literature examines SMEs as backbone of economy, as they are “a major source of diversification, entrepreneurial skills, innovation, competitiveness, and employment” (EC 2003, 5). Being a sub-discipline in economics, entrepreneurship is not limited by it; rather, it is a multifaceted area which also involves social and economic fields of study (Acs 1999, 3).

Box 2. Definitions of SMEs

The term of small and medium sized enterprises has various definitions and measures, differing from country to country. They are “non-subsidary, independent enterprises which employ less than a given number of employees” (OECD 2000, 2). The most commonly used criteria for the definition are staff headcount, value of assets, and annual turnover (EC 2003, 5).. I will use EU standard definition (from the to Extract of Article 2 of the Annex of Recommendation 2003/361 of European Commission) “[t]he category of micro, small and medium-sized enterprises (SMEs) is made up of enterprises which employ fewer than 250 persons and which have an annual turnover not exceeding 50 million euro, and/or an annual balance sheet total not exceeding 43 million euro” (EC 2003, 5).

There is also a variation in determining criteria for above and below thresholds from country to country and across local statistic systems. For example, in USA, enterprise fewer than 500 employees are considered as an SME, thus countries can have different number limits in their definitions (EC 2003, 5). As from January 1, 2005 European Commission laid down the following criteria for definition of SMEs as shown in the figure below:

Figure 1: The new thresholds

| THE NEW THRESHOLDS (Art. 2) | | | |
|-----------------------------|-----------------------------------|--|--|
| Enterprise category | Headcount: Annual Work Unit (AWU) | Annual turnover | Annual balance sheet total |
| Medium-sized | < 250 | ≤ €50 million (in 1996 € 40 million) | ≤ €43 million (in 1996 € 27 million) |
| Small | < 50 | ≤ €10 million (in 1996 € 7 million) | ≤ €10 million (in 1996 € 5 million) |
| Micro | < 10 | ≤ €2 million (previously not defined) | ≤ €2 million (previously not defined) |

Source: EC 2003

2.1 Role of SMEs in Economic and Social Development

SMEs have very significant and at the same time very specific role in the economy. If we look through the numbers, we can see their tremendous share in economic growth all over the world. In EU countries 99% of all firms are SMEs and they create approximately 75 million jobs (EC 2003, 5). Also, in OECD economies small and medium enterprises provide 60-70% (two-third) of employment and SMEs represent 95% of all enterprises (OECD 2005, 17).

Almost in all academic literature, scholars are positive about the economic benefits of SMEs (van Praag and Versloot 2007, 351). According to recent analysis by the same authors, SMEs lead to higher employment creation and dynamism, growth in productivity and have substantial benefits in terms of commercialization of high-tech innovations. The other famous scholars writing in this discipline Acs and Audretsch argues, that learning by doing, dynamism and flexibility of SMEs make them very successful. Although SMEs considered as “poor cousins” of LEs, they always have stimulation to start small before expanding, the probability that SMEs can become large enterprises (LEs) is very high (1993). Moreover,

authors elaborate that SMEs bring income to the government budget by paying taxes although this amount is little or much, assist to the development of the regions and rural areas by creating geographical balance, and provide “disadvantaged groups” meaning young, minorities, women, and even disabled people with jobs as well (1993).

There are also other advantages of SMEs. As McIntyre points out, the incentives for workers in SMEs appear to be more straightforward, clear and strong, also governance issues in SMEs can also be tackled more easily, as monitoring the performance of employees is not so hard for the owners of the small firms (2003, 10). Author suggests that SMEs tend to have innovation potential and huge flexibility compared to LEs which are like a “big ship that cannot steer and turn quickly”. He argues that SMEs promote competitiveness, as well as abate the monopoly inclinations, particularly in transition and unsettled economies (2003, 10).

The scholars emphasize different contributions of SMEs to the economy. Acs and Audretsch note that, SMEs are significant in the process of technological change; they are source of important innovative activity (1993). In addition, they point out that SMEs present a mechanism for regeneration in the market by serving as agents of a change (1993). Brock and Evans add that small entrepreneurial firms promote competitiveness by “newly created niches” (1989). The final and most acknowledged contribution of SMEs in recent years is their dominant share in the new job creation (Storey 2003).

Although SMEs has well a lot advantages, there are few disadvantages of them that have been set forth in the literature. As proposed by the authors van Praag and Versloot, the counterparts of small firms and entrepreneurs are “large firms, older firms, incumbent firms or wage employees”, respectively (2007, 351). Authors adds that one of their disadvantages

is that SMEs are very vulnerable and volatile to the economic and non economic situations happening around them; secondly, their contribution to GDP is not so high compared to large enterprises; thirdly, the labor market they offer is not stable and secure, they cannot provide higher payment and afford the high quality of management that a large enterprise can. Moreover, LEs are more advanced particularly in the *adaptation* of the innovations rather than SMEs (2007, 351). That is why, the SMEs sector of economy can survive only in an environment with proper public policies and enabling formal and informal institutions.

2.2 Public Policies Fostering SMEs

As we have seen from previous section, the SME sector is playing a key role in economic growth. However, within the course of recent years, status of SMEs became interesting not only for economists, foreign and domestic investors, banks, finance institutions, business people, and researchers but also for public officials and policy makers. Nowadays, studying the SME structure and policies, deploying less bureaucratic, enabling and promoting policies that have huge impact on economic and social wellbeing has become an important issue area of public policy all over the world. That is why many country governments has increased their concern regarding public policies on SMEs (OECD 1998). In order to see the patterns of SME policies, first of all, we need to define. So, according to the research project *Entrepreneurship Policy for the Future* conducted by Lundstom and Stevenson in 2002, 2003, entrepreneurship and SME policy defined as following:

“.....aimed at the pre-start, the start-up and post start-up phases of the entrepreneurial process; designed and delivered to address the areas of motivation, opportunity and skill; and with the primary objective of encouraging more people in the population to consider entrepreneurship as an option, to move into the nascent stage of taking the steps to get started and then to proceed into the infancy and early stages of a business” (OECD SME Outlook 2005, 24).

As it seems from the definition, SME policies mainly cover the pre, post and start up periods of business development and as a major objective encouraging people for entrepreneurship is very important aspect. I will examine in detail what else can be covered by public policy for SMEs in literature.

In general, scholars such as Schlögl argue that, in order to meet the needs of small firms, governments must create such an overall business environment which is *contributive to entrepreneurship and favorable* for firm establishment and *promotive* for the prompt development and maturation of SMEs (2004). These favorable enterprise conditions may include but are not limited to “sound fiscal and monetary policies, and structural reforms to allow labor and product markets to function smoothly,the important areas like taxation, competition, financial markets and, of course, bankruptcy rules” (Schlögl 2004).

Moreover, Schlögl claims that government policies are intervened to lessen regulatory and administrative barriers that may apparently impact the activities of entrepreneurs, lessen their investment and R&D, and hinder the firms to grow. All these obstacles can discourage willing people to start up, as they would need too much time and efforts. According to him, policies even take into consideration the burdensome and strict exit issues, meaning closing down also should be easy as starting up, because large amount of SMEs open and close in the market every year which will meet the flexibility character of small firms (2004).

One of the major strategic scope areas of the public policy is defining the objectives and tools for the establishment of an enterprise culture which has a huge impact on career priorities of the society. For that, we need to first clarify what is a community with an enterprise culture and how it can be reached. A society with an enterprise culture is a one “in which the potential for individuals and groups to start a business is maximized” (OECD 2004, 35). In

this society individuals or group of people are imaginative, enterprising, and creative and they act in an entrepreneurial manner in all spheres of life. There is such a belief in this society that developing economically and socially can be best reached by the spread of “thinking out of box” concepts, new ideas and by not depending on others to take decisions or solve the problems (OECD 2004, 35). So, public policies mainly try to change and shape the culture of people engaged in entrepreneurship by stimulating them to have a sound ownership sense, to raise their engagement in the control of their enterprise or firm, to enable them to take the responsibility, risks, long term visions, reduce a stigma of failure, losses in business, to establish know how clusters and networks, to generate entrepreneurial behaviors which includes “risk-taking and reward principle” to learn from their past wrong doings, to think and plan strategically (OECD 2004, 36). In this regards education and trainings, techno parks, various development agencies, and mainly business incubators, can be one of the best tools for the creation of the enterprise culture. I will come back to this issue in the case study section of this thesis.

Public policies *position* SME development objectives within the framework of national macro-economic and social policy targets. Linking SME development objectives against overall national policies provides for governments to integrate and regulate the appropriate activities of various ministries, departments and to set priority aims (OECD & UNIDO 2004, 32).

One of the key challenges in the SME sector development for policy makers is the management policy and mechanisms through which programs are to be managed. There is no single, “one fits all” or “the best” model for setting out a management for the SME development policies, as it is very hard to define it, however, policy makers propose the ‘bottom up’ approach as an important aspect for gaining the confidence and cooperation of the SMEs while managing them (OECD 2004, 38). Depending on the objectives and targets

of the public policies on SMEs, there can be a separate governmental department, unit or an autonomous agency or ministerial committee which will be in charge of management and regulation small business development. For example, in Malaysia, co-coordinating Unit of the Prime Minister's Office, in the USA, the US Small Business Administration Office is in charge of SME sector development policies (ibid.).

Public policies are also involved in establishing SME associations and various entrepreneurial stakeholders in order to increase advocacy capacity, and stimulate the representativeness. Different chambers of commerce, councils, confederations, industry and sector associations, local business clubs, forums, and pressure groups can be considered as such kind of stakeholders (OECD 2004, 44). Well-founded and stable associations are in the interest of the governments for better policy development and enhancing the private public partnerships. Public policies can support their foundation differently and they can have public or non-governmental type of status (ibid).

Public policy plays a major role in SME sector development particularly when it comes to setting up a statement of mission, principles of governing, key targets and objectives, specific measures to be taken, etc. Moreover, public policies set frameworks for the intervention, for instance, when there is a need for establishing markets for services of SMEs, when there is institutional weaknesses, as well as regulatory interventions to remove barriers during the start up, growth and/or survival process (OECD 2004, 35).

When talking about enabling and favorable conditions scholars and policy makers also mention infrastructure issues that government should take care of in order to foster SMEs. These accounts for providing "broadband and secure servers", development of ICT sector in

order SMEs may benefit from recent and high tech solutions in business and acquiring “know how”s, as innovative SMEs are mainly engaged in e-business activities. In addition to that, training of “qualified e-business staff” should be achieved to in order to expect good results from the pursued policy. Furthermore, transaction security and trust issues should be also a target for the entrepreneurship policy of the government (Storey 2004).

Public policies should be also addressed to avoid asymmetric information that may occur between small and medium sized enterprise owners and potential investors (Acs 1999, 161). Because of the asymmetries in information entrepreneurs are prone to be excluded from the private investments (Myers and Majluf 1984; Greenwald, Stiglitz, and Weiss 1984). According to the authors, as the one of the major hurdles for development of SMEs are considered poor access to finance, these information disparities must be must be tackled very carefully with particular SME help desks, transparent and available portals and other tools of accountability.

Moreover, literature on economics argues that there are also positive externalities for a government to implement policies on SMEs. For example, the research and development expenditures subsidized by government may have positive spillover effect on other small enterprises or society can benefit from it (Griliches 1992).

In a nutshell, we have learned in this chapter the major theoretical background on socio-economic role and contribution of SMEs, main areas of interest of public policies for SMES, how SMEs become target area for policy makers, why developing this sector is inevitable for governments and decision- makers, and how they address their policy actions, tools, and mechanism in terms of SME sector development. We have also learned the contribution of SMEs to “hard” indicators like employment creation, diversification, reduction of poverty

and geographical imbalances, etc. and to “soft” indicators like enterprise culture and entrepreneurial skills which will be useful for the analytical chapter of the thesis. Moreover, I have made a theoretical case for SME’s and public policies on them as an object of analysis and laid out main theoretical findings for further empirical chapters based on the reviewed literature.

Chapter 3 – SME Policies in Resource Rich Economies: The Proxy Case of Kazakhstan

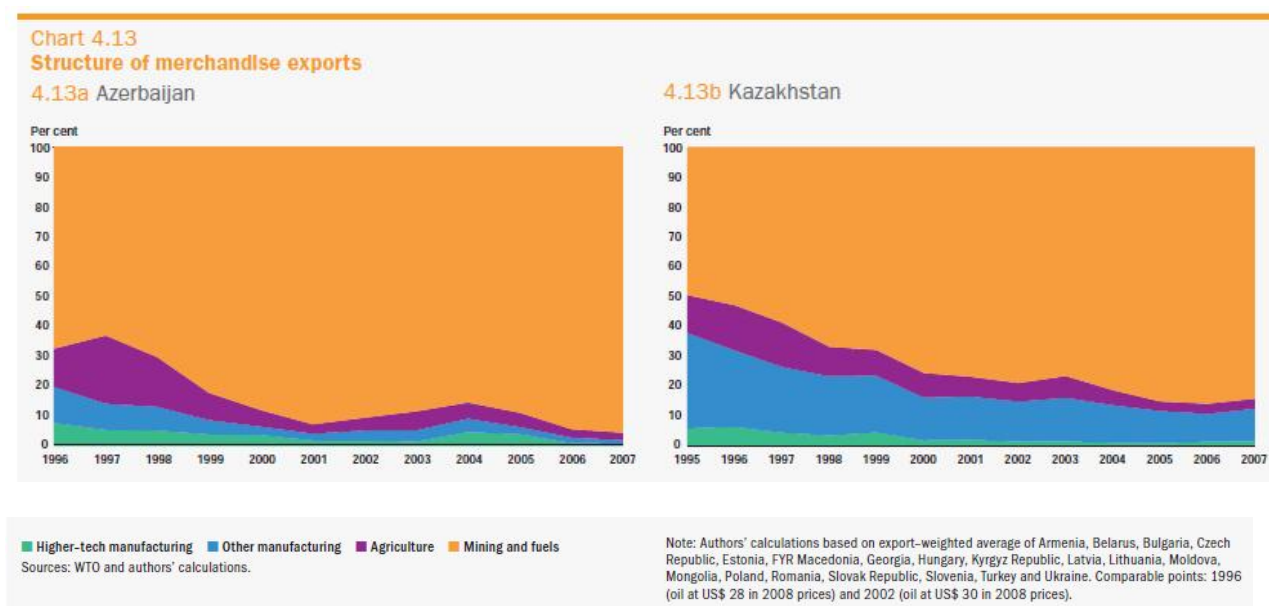
In this chapter, I am going to look at Kazakhstan as a proxy case to study public policies on development of SMEs, mainly, business incubation model, in order to draw key insights for the case of Azerbaijan and to answer my research question which is primarily related with Azerbaijan. The reason why I am going to use a proxy case instead of studying Azerbaijan itself is that, Azerbaijan has not come up yet with any policy model, there are regulations and policies, but, they are only on the papers. However, Kazakhstan, at least has already applied business incubation initiatives as a part of its SME development policy. Additionally, there is more data on Kazakhstan than for the case of Azerbaijan. The extent to what business incubation is successful in Kazakhstan and the degree to what I can apply the practice of Kazakhstan to Azerbaijan will be discussed in the next chapter.

3.1 Rationale for choosing Kazakhstan as a proxy case for Azerbaijan

There are several important similarities and trends of socio - economic development between, Kazakhstan and Azerbaijan. The rationales behind my task of looking at case of Kazakhstan are following:

First of all, both of the countries are resource-rich and very dependent on export of oil and gas, and negative impact of fluctuations in the commodity prices. If we look at the below figure, we can observe that within the last few years, in Azerbaijan, approximately 90%, and in Kazakhstan 80% of output exported was accounted for oil and gas commodities (EBRD 2009, 86).

Figure 2: Structure of merchandise exports



Source: EBRD 2009

During the last decade, Azerbaijan and Kazakhstan experienced typical problems in economic development directly related with the concept of the “resource curse”. On the one hand, income coming from resources generated great economic growth, on the other hand, those revenues and great amounts of foreign exchange inflows made them dependent on changes in oil & gas prices (EBRD 2009, 90). Both countries generated substantial revenues from exports, yet they did not use these revenues to improve their competitiveness, sectoral development, and diversification of economy, but just closed some urgent gaps, and they failed to have any further step other than that.

However, it is very difficult to keep rapid growth rates with the volatile prices in the long run. The above mentioned reasons prove that “that resource abundance may undermine rather than foster economic development over a longer period of time” (EBRD 2009, 90). For example, according to the same source, because of the fall in oil prices in 2008, the economic growth rates of the countries went down significantly.

Enjoying large revenues from natural resources, Azerbaijan and Kazakhstan started to carry out some state-led reforms and policies to restructure economy by diversifying it. However, “diversification away from resources” is not an easy job and achieving those policy goals is very challenging. By diversifying the economy these governments mainly seek to reap the two major policy goals as resource rich countries reduce the risk of being hit by external shocks and promote sustainable socio- economic development (EBRD 2009, 81).

As mentioned in previous chapters, one of the priority policy instruments for diversifying the “resource trap” economy and a well as for buffering it, is promoting development of the small and medium scale entrepreneurship (SMEs) and creating the conducive environment for entrepreneurial activity. In this respect, business incubation has been widely acknowledged as a remedy for a variety of economic and social policies. Davies cites principal contribution of business incubation as job and welfare creation, support for SMEs, stimulation of innovation, assistance to small firms in pre, start-up and post start up period, transfer of technology and know how, evaluation of SMEs risk profile, establishment of primary links between universities, research and development institutions, think tanks, development of enterprise clusters etc (2009, 5)

Second ground for looking at Kazakhstan is that these two countries have non-inclusive growth, which means the development of rural areas is declining and there is strong degradation of the regions. Both are post communist, authoritarian regime and entered the oil boom with underdeveloped, shaky, and ineffective institutions (EBRD 2009).

Thirdly, both countries are considered as transition economies according to the EBRD Transition Report (2009, 90) and the essence of the socio- economic shift of any transition

country is the establishment of the private sector, mainly the improvement of entrepreneurship and promoting small and medium-sized enterprises (Szabo et al 2006, 122). Therefore, both countries linked their mainstream national socio-economic objectives with SME sector development, trying to achieve macroeconomic stability by diversification strategies, although their efforts have not be so successful so far.

Moreover, almost all the international organizations and institutions which are active in the economic development discipline like World Bank, EU, IFC, EBRD, ILO, UNECE, ADB, USAID, etc allocate very special attention to the SMEs. Their assistance to SMEs includes areas like technical, capacity building, and of course, the most important, financial aid. This tendency has not bypass Azerbaijan and Kazakhstan; both countries have been recipients of international assistance to SME sector development. The government policy to develop SMEs for the diversification of the economy and developing the non-resource industry has been supported by the external community. These institutions also go in line with state policy in the sense that Azerbaijan and Kazakhstan should utilize their natural resources wisely and enable good public policy mechanism to foster SME sector development, because sooner or later these resources will run out. In this context, I will point out below in the box the contribution of several projects and programs by major international organizations for small and medium size enterprise development that have been carried out in both countries within past years.

Box 3. Assistance by International Organizations

IO Assistance in Azerbaijan

Asian Development Bank in conjunction with Bank of Baku initiated credit program to small scale firms in the year 2007 of (Asian Development Bank 2007). According to the project, 6 million USD had been assigned for financing SMEs. This project enhanced the access to finance by SMEs and contributed to the development of private and sustainable economic development of Azerbaijan (ibid).

In 1998, in the name of financing SMEs, **EBRD** has launched a project amounted for 20 million USD (EBRD 1998, 1). The loans were allocated to the entrepreneurs the International Bank of Azerbaijan which owned by state and other private banks for SMEs (ibid.)

IO Assistance in Kazakhstan

Kazakhstan has been the first country that signed a joint development agreement directly with the US Government, namely with the **USAID**. According to the Program for Economic Development, the USAID guarantees to finance the entrepreneurial and economic development in Kazakhstan by rising installments per year (Year 1 – 25%, Year 2 – 35%, Year 3 – 45%, Year 5 – 50%). Within this program, the USAID and the Government of Kazakhstan (GOK) have decided to jointly finance the programs such as the Kazakhstan Small Business Development Project, which will provide assistance to foster SME's (Toxanova 2007, 1).

Furthermore, as a support measures both countries have set up SME funds for promoting and assisting to small firms and businesses and developed some internal conditions for their growth. Azerbaijan government established the Azerbaijan National Fund for Entrepreneurial Support (ANFES) in 1992. The major responsibility of this Fund is promoting the development of entrepreneurship and assisting the entrepreneurs with finance, mainly crediting SMEs with very affordable interest rates for a long period of time (ANFES 2010). For example, the Fund rendered 465 million manats² for more than 8000 projects of small and medium entrepreneurs in 2008 (ibid).

The “Small Business Development Fund” JSC which was established in 1997 by the Kazakh Government (GOK) sought to promote the economic growth of SMEs by using the state financial assets to finance small business development (Toxanova 2007, 3). Annually, 10 billion tenge (approx. 83 million USD) from the state budget were allocated to Small Entrepreneurship Development Fund (SEDF) for developing and backing small business until 2007. The credit and loans by SEDF were given for up to 5 years with 10-12% annual interest

² Manat – the currency of Azerbaijan Republic. Rate of AZN to USD according to Central Bank of Azerbaijan Republic; 1 USD = 0.8036 AZN.

rate (Toxanova 2007, 3). Since 2007, the Fund has been subject to conceptual changes, namely status of the fund has changed from Small Entrepreneurship Development Fund JSC to DAMU Entrepreneurship Development Fund JSC and has become from a financial institution into an assets manager for government allocations. As a result, the mandate of the fund has been broadened to supporting of small and medium business (DAMU 2010).

We can also pursue that despite the fact that Azerbaijan set this fund up much earlier than Kazakhstan; the latter still is the better case to look at as fund in Azerbaijan did not function that much.

In brief, from this section, we can understand that number of factors and variables can be “hold constant”, including IO involvement when we look at Kazakhstan and Azerbaijan path and development, economy and SME sector development priorities.

3.2 Brief overview of nature and characteristics of SMEs in Kazakhstan

SME sector has great importance in national economy of Kazakhstan, too. In Azerbaijan it does not have – only on paper yet. According to the official data the Statistics Agency of the Republic of Kazakhstan as of December 1, 2010, there are 1,842,641 active small business entities registered (SARK 2010). The same structure also reports that the large numbers of SMEs are focused in big cities like Almaty 35 %, Astana – 9.1 %, South-Kazakhstan region – 9.1 % respectively (Toxanova 2007, 1) (See map). Share of the SME sector on overall registered companies in Kazakhstan is 77,9%; in South Kazakhstan 75% (Ministry of Entrepreneurship and Industry of the Republic of Kazakhstan 2006).

Figure 3: Map of Kazakhstan



The main deficits of the SME development policy are the lack of skilled SME development professionals among local authorities on the regional levels, and the lack of reliable information about the situation in the SME segment, including reliable official statistics. The main structural problems of the SME sector are low diversification level, low employment level, low overall productivity, and low qualification level of entrepreneurs and labor force (Schandera 2006, 11).

In February 2004, the Kazakh government launched the “SME support program 2004 – 2006”. The main objective was the diversification of the SME sector, and the main instruments were the decentralization of the SME development policy from the national to the regional level, and the strengthening of small and medium sized cities in the field of SME in Kazakhstan (Schandera 2006, 11). Training and information services for SME and micro crediting were also among the instruments. In 2007, the new Law on Private Enterprise of Republic of Kazakhstan has also been approved (Toxanova 2007, 3).

Recently, Sovereign Wealth Fund of Kazakhstan “Samruk-Kazyna” JSC has been established according to the Presidential Decree of the Republic “On Some Measures on Competitiveness and Sustainability of National Economy” in 2008 (Samruk-Kazyna 2010). Announced as a main “anti-crisis operator” to buffer and safeguard the economy, one of the main priority

tasks in front of the fund is diversification, modernization, and stabilization of national economy by promoting and financing SMEs in particular (Invest.kz 2010).

3.3 Business Incubators in Kazakhstan

In Kazakhstan, the incubator program started in the late 1990s, namely in 1999. Forty four business incubators have been established in Kazakhstan so far. However, not all of them fulfilled their primary objectives, and out of 44 BIs that initially supported, only 6-8 that are operating now. Their profile was mixed ranging from NGO to governmentally supported ones.. In the meantime, some of the BIs tried to meet international standards of business incubation like SODBI (Shymkent), Almaty City Business Incubator, and International Incubator/Business Centre in Uralsk (Toxanova 2007, 9). Therefore, I will describe SODBI more in detail.

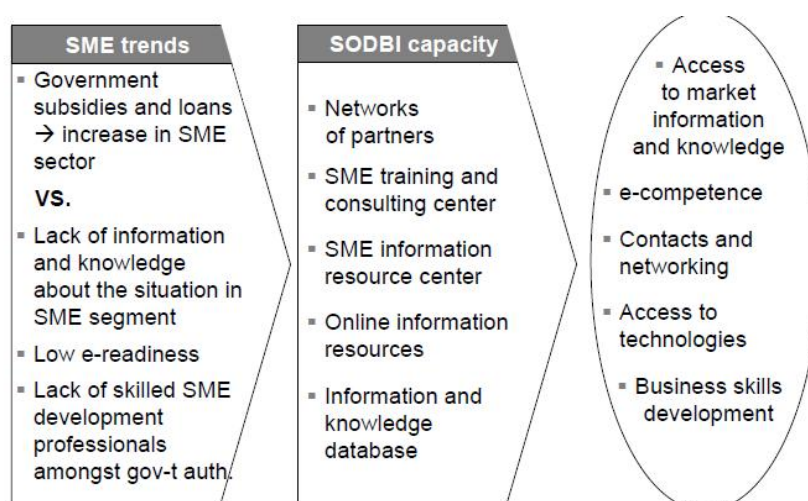
SODBI was officially registered in April of 2000 with 4500 sq.m of space in property for the period of 10 years. The Incubator is situated in the north part of Shymkent in South Kazakhstan, where there are a lot of micro-regions. The population of micro-regions account for 20 per cent of total population dwelling in the city. The legal form of the incubator was the nonprofit, NGO. There were 38 business incubator (BI) residents in the SODBI and the average incubation period was three years. Legal forms of residents of business incubation were companies, individual entrepreneurs. The main cluster policy in South Kazakhstan was food processing, agriculture, textile, tourism and construction sectors. The strategic outreach of SODBI was using the existing networks and channels, launching new pilots and projects; they focused mainly on tourism and agri-businesses (ibid.)

Box 4. Background of Business Incubation

First business incubation systems started in US in 1959. As Davies summarizes, business incubator is a structure or “physical location” which provides office space and other facilities, compromising lease conditions, financial assistance, enables access to technology, as well as services like marketing, HR, PR, consulting, and others (2009, 5). As in business incubators, small enterprises are situated very close to each other under one roof, this structure allows knowledge exchange among them (2009, 5). Also, being in the incubators the costs of small firms for office, staff, and other facilities are reduced dramatically. As the young small firms and entrepreneurs are especially weak during their start ups because of the lack of experience of running business, lack skills, technology, trainings, professional services, in this context, business incubators can be of great importance. There are different forms of incubators like techno parks, centers for innovations, science parks etc. Although they are launched first in developed economies like US, UK, then other countries of Europe, incubation system of businesses become a spotlight in the developing and transition economies as a main source of support for entrepreneurship and SMEs as well (2009, 5). These projects are mainly conducted under supervision and promotion of the World Bank Group, infoDev project. According to infoDev 2008 data, Global Network of Business Incubators has 13.900 resident companies that are currently incubated, 118.500 employees in incubated firms, 5.600 graduated firm from the incubator since beginning of the initiative, 115.000 current employees in graduated firms (iDISC 2008, 2). However, it should be also emphasized that because of the overall business environment, education, culture of entrepreneurship, government or institutional support the outcomes achieved in Europe and USA can be in totally different degrees in developing countries and the extent of success can vary from country to country (iDISC 2008, 2).

Main objectives in establishing SODBI business incubator were to support small and medium scale business development on start up period, promoting the creation of new business subjects and young entrepreneurs, adopt them to the business situation in the country, consultation and information, contribution to the socio-economic development in South-Kazakhstan, reach the rural areas of Kazakhstan. The main donors were Eurasia Foundation, GTZ, and Soros-Kazakhstan Foundation (SODBI 2010).

Figure 4: Overview of Situation in South Kazakhstan



SODBI also closely cooperates with iDISC - the **infoDev Incubator Support Center** which is an outcome of World Bank led Information for Development -*infoDev*'s (Information for Development) Incubator Initiative. The initiative was launched in 2002 in support of structures fostering ICT-enabled entrepreneurship in developing countries (idisc 2010).

Box 5. infoDev Incubator Initiative.

infoDev = information for development, launched in 1996 , by World Bank
 Incubator initiative launched in 2003, promoted by Japanese government
 Focuses on financing and technical assistance for BIs in developing countries
 Growing global network: 173 incubators from 76 countries over the world (as from September 2008)
 Research area: First assessment of incubator impact in developing countries
 Global working groups: Women, Youth, High Growth
 www.idisc.net: Global learning and exchange platform for incubator (idisc 2010)

Although business incubator initiatives started with great enthusiasm in Kazakhstan, they did not accomplish their tasks to the extent they were supposed to. The results, opportunities, threats, obstacles of business incubation system for developing SMEs in Kazakhstan will be discussed in the next chapter as well as lesson learned from Kazakh case will be set forth to analyze to potential development of the system in Azerbaijan.

Chapter 4 – Effectiveness of Kazakhstan Policies: Implications for Azerbaijan

In this chapter, I examine whether the measures taken by Kazakh government to promote business incubation had the intended result, whether this approach met the most important criteria of SME sector development policy like job creation, diversification of economy, development of entrepreneurship, poverty reduction, removing the geographical imbalances and non-inclusiveness, creation of enterprise culture, etc (Schlogl 2004) that mentioned in the chapter two. Moreover, I will look into the main public policy issues and obstacles that hindered businesses incubation to contribute to overall socio economic objectives of SME development policy and set forth what they can imply for Azerbaijan, what key learning can be drawn from Kazakh case for Azerbaijan.

4.1 Analysis of results of business incubation in Kazakhstan

In order to able to analyze the impact, I will look first at the results of the business incubation program in Kazakhstan on the example of SODBI. As shown in chapter two, there are several indicators to assess the impact of SME policies, the success or failure of the measures. These can be hard indicators like the number of new start-up and survival firms in the economy of the county, number of job created, and the contribution to diversification or to reduction of poverty and soft indicators like improvements in enterprise culture, skills, business perception etc. If we look from the perspective of hard indicators, the results are minimal. According to the numbers in 2006, the number of new jobs created by the SODBI business incubator was 249 and there were only 14 enterprises that were successfully incubated and started to work (Schupulung 2006, 6). Although the contribution is not that much, however, it says something about the future potential. For instance, if all the 44 business incubators that were created could have more or less such numbers, then we could

speak about the economic impact much more. However, there is lack of tangible data on the results of other BIs that could bring more critical and open look to our analysis.

Nevertheless, if we look from the perspective of soft indicators like scale of entrepreneurial activity, development of enterprise culture, innovation made by the business incubators, the changes in perceptions among businessmen and foreign investors, the contribution of business incubation model of SME creation process is positive.

Notably, SODBI has a number of achievements that indicates the visible impact of business incubation. For instance, it has certainly contributed to the establishment of Central Asian Business Incubators Network (CABIN) and Technological Parks as a network coordinator, has conducted a number of trainings for governmental authorities and business people in rural areas on assessment of business ideas, on cooperation in marketing, on internet use for SMEs in rural areas with the large numbers of trainees (SODBI 2010). The methodologies and research studies on doing business developed by them are currently put into use by 30% of the participants of trainings in the rural regions. The incubator also contributed to the regional development by providing expertise in innovation for business development and in internationalization of regional/local governments. It has established a systematic benchmarking system for evaluating and monitoring BIs. Moreover, projects like Shymkent.com enterprise information portal containing overall database of SMEs and businesses in South Kazakhstan, First Tourism Business Club for local tourism business network, «Agrotech» agro-technology and equipment enterprise and business incubation network have significantly contributed to the rise of enterprise culture in South Kazakhstan (SODBI 2010).

It is easy to see that, the measures taken have lifted up Kazakhstan in World Bank Knowledge Economy Index within past years. For example, in 2000 the rank of the country was 90th, however in 2009 it jumped 12 places and was ranked to 72nd place out of 145 countries, for its knowledge economy trends which mainly achieved by innovative SMEs. Moreover, after the business incubation projects, according to the Doing Business reports, Kazakhstan ranked to higher places than it used to be in recent years on “ease of doing business” scale which mainly includes starting business, getting permits, employing workers, etc. Obviously, because of the improvements in these scales and rankings, perceptions in foreign investors to start a business in Kazakhstan might change markedly.

Starting from the beginning of 2007, as a result of the reforms, the country also has been accepted as a member of the GEM - Global Entrepreneurship Monitoring Consortium which conducts valuable research on entrepreneurial activity all over the world, as the first Central Asian country to be so (Toxanova 2007, 1), however, Azerbaijan is still not member of this structure yet.

Although there are optimistic results, not every business incubation initiative that is launched succeeded in Kazakhstan; as noted there were few successful ones. For example, after break even, meaning covering its initial operating cost and achieving self sustainability they turned into a consulting service provider, premise renter, business center by moving away from their primary objectives.

As there were almost no data on the failure reasons, I conducted an interview with World Bank infoDev incubation expert in Kazakhstan, Stefan Schandera to find out what was the main reasons for the lack of success and why business incubators could not accomplish their

initial targets to the degree they were supposed to. According to the expert, if the below mentioned aspects could be taken into consideration, the contribution of business incubators would be much more visible and substantive:

Objectives and Planning: The incubators in Kazakhstan mainly did not have a clear impact mission and development objectives. Control aspects and risk of crowding-out effects were not included in the mission. As regards, there unrealistic expectations that BIs would become successful and financially sustainable after the 2-3 years. They did not take into account that process might take up 8 to 10 years. Within the time framework the projects have run, it was difficult to ensure the success. Donors had money for incubators and Kazakh government agreed to apply it without clear cut objectives. This means the government was looking for the foreign money first of all but was not really interested in the success.

Positioning: The positioning of incubators within the socio-economic development context was not taken into consideration appropriately in Kazakhstan. The incubators were not integrated into the overall innovation, and socio-economic system.

Management: In the case of Kazakhstan, government officials were placed into management of the business incubators who had no competency in this sector, which brought failure. There were cases very committed local governments tried to do it well, and these incubators worked for a little while. So, the situation there was the following, as government officials change very often in Kazakhstan and after committed official changed, as consequence, a while later incubator was also closed. Lack of ongoing support by government after launching business incubators was a case in this respect.

Ownership: In the Kazakh case, business incubation was mostly externally driven, meaning by donors. The most successful programs that do well are driven by the government after the thick analysis of the situation in the country and coming to the conclusion that incubators would be the best tool for business creation process and for promotion innovation in SME's - compared to other tools such as training centers etc.

Demand and size: Market demand is the main factor. However, in Kazakhstan, even feasibility studies for business incubation often started with step 2, ignoring the more important step 1, which is demand side. As a consequence of lack of demand for services offered by the incubators, they had to close down. The Kazakh government wanted to have an incubator, but they did not the purpose of having it. All the threats and possibilities were not clearly assessed. The clients of the business incubator residents were not clearly defined. Such analysis takes time and needs to be carefully designed.

Determination of Government policy and function: The role of the government and the function it wanted to have in the business incubation process was not clearly stated in Kazakhstan. The government function was first of all to provide a framework for the promotion of business incubators (legal framework etc.). A second task of governments was to make interventions to promote for example certain areas (like IT, innovation in specific sectors etc.). However, this second task was not a government task by nature which was not well understood in the Kazakh case. The government tried to intervene, but often failed because it did not have necessary expertise and experience.

In addition, in the SODBI business incubator, idealistic self-sustainability aims and overstated technology commercialization beliefs pursued by finance cuts was also among the major reasons of not being successful to the degree expected to be.

4.2 Key insights drawn from the case of Kazakhstan for Azerbaijan

Now, after finding the major results and hurdles that hindered success, we can draw the key insights for Azerbaijan from Kazakh case.

First of all, the chance that Azerbaijan can learn from the Kazakh case of SME sector development policy is certainly positive in itself. Secondly, there is indeed, a lot of experience generated from these incubators that can be used for other new programs of SME development, there are innovations, although might simply not be high tech. However, Azerbaijani government should be careful with the adaptation of them to their context. Thirdly, geographic size of Azerbaijan can play a positive role compared to Kazakhstan, Kazakhstan is as large as Western Europe and because of its vast size there was low and sometimes almost no integration between the business incubators in the regions and rural areas.

After examining the results and out of all these empirical findings, I can see that much more needs to be learnt from Kazakhstan errors. We know that new models often don't move quickly, within the time framework the business incubation projects have run and with the objective of being self-sustainable after foundation, apparently, it is difficult to expect the huge impact on economy. It takes time to restructure the whole understanding of doing business with the standards of BI. After all, and this is also confirmed by examples in Germany and other Western countries, "incubating" the incubators takes time, good incubation programs are usually designed with a ten or more year development strategy and those incubators are not necessarily self-sustainable, not even intended to be so.

On the other hand, in order to assure that things do not go wrong, we would need to assume that unless the country puts regulatory and nepotism issues in position, Azerbaijan cannot

expect better results. Although the absence of democratic institutions and regime is not the topic of this thesis, these are the features the two countries have in common, therefore, we can expect that the problems that arise in Kazakhstan to be prevalent in Azerbaijan, too.

Building on practical experience of Kazakhstan business incubators that was researched and discussed above, several key recommendations can be made. This key learning can be useful for policy makers and the government of Azerbaijan in order how to put them into the context, to take them into consideration in their policies and future plans in terms of fostering micro, small and medium-scaled enterprises.

- The Business Incubator should have clear impact mission and development objectives. The role of the government and the function it want to have in the business incubation process should be clearly stated
- There should be a "long-term commitment" for BIs because it is not a 2-year exercise. The development plan and strategy should be at least 7 years. If the government is not ready be that patient they had better not invest
- Positioning should be from the prospective of the client, not of the incubator. Business Incubators and planners of incubator should realize “positioning and value proposition – and its monitoring – within both the non-commercial and commercial context”
- The incubator has to be managed like an enterprise, not like a government agency; otherwise, it will very likely fail. The government should do the supervision but not management. Incubator managers should be entrepreneurs, innovators and networkers.
- It must be driven by the government, not by external donors; donor should mainly assist in realization of the project, not own the whole process.
- There should be realistic evaluation of the real market demand for incubation services. BIs should realize the competition including but not limited to for-profit competition and other BDS

Conclusion and Policy Recommendations

The present research has shown that there are lessons that can be learn from Kazakhstan like clear objectives, positioning, management, ownership, demand and size, policy etc issues. These lessons can be learnt not only successes but failures also. These are the failures partly due to the type of regime and lack of expertise in marketisation. At the same time, these are the features Azerbaijan and Kazakhstan have in common. Therefore, in applying the insights from Kazakhstan case to Azerbaijan, it is important for Azerbaijan to be very careful with the problems that Kazakhstan also had. The following recommendation can be made if Azerbaijan applies business incubation model of SME creation and development:

- Acknowledging the share of business incubation in promoting entrepreneurship and be aware of their potential to foster regional, rural and sectoral development ;
- Providing clear, management, status and mandate for business incubators;
- Ensuring suitable support back-up partners for business incubators in different levels like local and international ;
- Concentrating the business incubator on local entrepreneurs and local needs;
- Selecting the location/accommodation and the site of the business incubator very cautiously and making sure that appropriate facilities can be easily accessed and infrastructure can be supplied;

In addition to that, there can be made number of general policy recommendations for the SME sector development policy for Azerbaijan. Given above, if such steps are not taken now, Azerbaijan will suffer from not doing anything when its oil and gas runs out in 25 years.

- Hiring professional management and applying “business-like operational practices” in order achieve positive results in terms of promoting entrepreneurship as well as helping to foster a new entrepreneur culture and networking (OECD and UNIDO 2001, 57);
- Enable the business incubator operating terms, services and charges/costs open and transparent to clients (OECD and UNIDO 2001, 59)
- Make the use of important international experience on business incubators and communicate and disseminate policies largely to guarantee their realization (OECD and UNIDO 2001, 60)
- Defining the obstacles for establishment of an enterprise culture; for start-up and survival procedures and finally for the maturity and growth of existing businesses
- Evaluation and assessment of the programs and projects by public and private policy makers and providing “feed forward” (OECD & UNIDO 2004, 79)
- Cooperation with universities, connecting SMEs with R&D institutions, knowledge centers and technology transfer, linkage to new know-how source in marketing
- Providing active monitoring and stimulation of environment, fostering efficient networking and clustering policy
- Commercialization of innovations and their adoption
- Providing information about business on external market and legislation, advisory assistance in searching for business partners for application to other international projects; information about sources of funding from EU and other donor funds and programs
- Removal of administrative barriers (tax, registration, etc) and creating favorable environment for entrepreneurship
- Enhancing the export orientation and access to foreign markets

After looking at the Kazakh case it can be concluded that business incubation is a good idea to implement if all the guidelines of the incubation system are applied rightly in practice, if they are well-managed and integrated, however, still it is not the entire story. Apparently, business incubation can take out number of large boxes in terms of SME sector development targets, but Azerbaijan should not entirely rely on this model, simply because it is not enough. Azerbaijan may also benefit from experience of other countries that successfully managed to find solutions to tackle with Dutch Disease and succeeded in development of non-resource sector. Within the limits of this thesis, I tried to apply the best and worst practices drawing from the Kazakh case to the degree I could apply and did not investigate the regulatory, nepotism, corruption barriers (although mentioned them) that could be tackled. Those issues can be a topic of new thesis, study area suggestion from me for further researchers, scholars, and practitioners.

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Appendices

Map of Azerbaijan



Source: IFC 2009