


“Challenges of small and medium enterprises during the COVID-19 pandemic: Case of Georgia”

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ARTICLE INFO

Amiran Maglakelidze and Gulnaz Erkomaishvili (2021). Challenges of small and medium enterprises during the COVID-19 pandemic: Case of Georgia. *Problems and Perspectives in Management*, 19(4), 20-28. doi:[10.21511/ppm.19\(4\).2021.02](https://doi.org/10.21511/ppm.19(4).2021.02)

DOI

[http://dx.doi.org/10.21511/ppm.19\(4\).2021.02](http://dx.doi.org/10.21511/ppm.19(4).2021.02)

RELEASED ON

Wednesday, 06 October 2021

RECEIVED ON

Monday, 09 August 2021

ACCEPTED ON

Tuesday, 14 September 2021

LICENSE



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JOURNAL

"Problems and Perspectives in Management"

ISSN PRINT

1727-7051

ISSN ONLINE

1810-5467

PUBLISHER

LLC "Consulting Publishing Company "Business Perspectives"

FOUNDER

LLC "Consulting Publishing Company "Business Perspectives"



NUMBER OF REFERENCES

32



NUMBER OF FIGURES

4



NUMBER OF TABLES

0

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BUSINESS PERSPECTIVES



LLC "CPC "Business Perspectives"
Hryhorii Skovoroda lane, 10,
Sumy, 40022, Ukraine
www.businessperspectives.org

Received on: 9th of August, 2021

Accepted on: 14th of September, 2021

Published on: 6th of October, 2021

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Conflict of interest statement:

Author(s) reported no conflict of interest

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CHALLENGES OF SMALL AND MEDIUM ENTERPRISES DURING THE COVID-19 PANDEMIC: CASE OF GEORGIA

Abstract

The COVID-19 pandemic has had a significant impact on small and medium enterprises (SMEs). The purpose of this study is to assess the impact of the COVID-19 pandemic on SMEs in Georgia, identify the challenges of SMEs in pandemic conditions, and analyze government economic policy measures. For this purpose, 102 small and medium entrepreneurs from different regions of Georgia were interviewed. The survey was conducted by sending a questionnaire through digital channels. The results were processed using data analysis, quantitative and qualitative research methods, and presented graphically. As a result, key challenges and development directions that are typical for SMEs operations in Georgia during the pandemic were identified. For 60.8% of surveyed SME owners, lockdown is the main challenge. Sales volume of 45.1% of SMEs decreased. In addition, 39.3% of the surveyed SME owners increased the innovative capabilities of a company and 37.2% increased the sales volume of a company through digital channels. The main challenge of the pandemic, lockdown, gave impetus to a change in entrepreneurial behavior. In a pandemic, entrepreneurial activity has become more favorable through digital channels. During the pandemic, there is a need to continue the government's program of tax incentives and subsidies for SMEs. In addition, the government should promote education in the fields of entrepreneurship, innovation, and technology.

Keywords

COVID-19 pandemic, SMEs, entrepreneurship,
innovation, economic policy

JEL Classification

H12, L25, L26, L53

INTRODUCTION

At the beginning of 2020, the world faced major challenges due to the COVID-19 pandemic. To stop the spread of the infection, the governments of the countries had to impose various restrictive measures and lockdowns. The COVID-19 pandemic created problems for the SME sector and consequently threatened the development of the countries' economies. For countries, SMEs are the backbone of the economy. They also have a big role to play in sustainable development (Šebestová & Sroka, 2020). SMEs are of great importance in the US, where they create two-thirds of all new jobs (USTR, 2021). SMEs accounted for 99.8% of all enterprises in the EU non-financial business sector generating 56.4% of value added (Muller et al., 2019). 99.7% of all firms in Georgia in 2017 were SMEs, accounting for 62% of total employment and 56% of total business sector turnover (OECD, 2019).

Governments have faced the need to take various anti-crisis measures. The pandemic placed an unprecedented burden on countries' health systems. Infection control measures led to an economic crisis, with a sudden halt in economic activity. It should be noted that currently, pandemic response measures are primarily focused on protecting the present, while less attention is paid to the future of economic activity

(Kuckertz et al., 2020). The severity and duration of a corona crisis depend on the duration of the pandemic. In this sense, today “the economy has become hostage to medicine” (Papava, 2020, p. 129). The COVID-19 pandemic and the current economic crisis have created problems for entrepreneurship and therefore for SMEs. In addition, the pandemic is an extraordinary way to discover innovative opportunities and creativity (Ebersberger & Kuckertz, 2021). The above-mentioned crisis was present in Georgia as well, where SMEs did not face challenges. The present study allows getting a deeper understanding of the problems of SMEs during the COVID-19 pandemic in Georgia.

1. LITERATURE REVIEW

Numerous studies have been conducted on the impact of the COVID-19 pandemic on SMEs and government support policies. For example, the situation, challenges, and implemented SME support policies in different countries of Europe and the world is described in the studies of Juergensen et al. (2020), Dörr et al. (2021), Kuckertz et al. (2020), Marona and Tomal (2020), OECD (2021), Papava (2020), and Adian et al. (2020). Yoshino and Hendriyetty (2020) reviewed the Japanese case, and the Chinese case was reviewed by Dai et al. (2021). Thukral (2021), Papadopoulos et al. (2020), Ebersberger and Kuckertz (2021), Slusarczyk and Pyplacz (2020), and Thierry et al. (2020) studied societal behavior change and the dominant role of technology and innovation in pandemic conditions.

Existence of many SMEs to provide employment and income to SME owners is important for the irreversible development of the economy. Starting an entrepreneurial venture is a complex phenomenon and it involves many issues, which is a major challenge for the entrepreneur as well as the uncertainty surrounding the success of the business. This burden is particularly heavy for founders of innovative companies, as there are also tasks in the area of product development and the uncertainty associated with it (Fritsch, 2019). More new entrepreneurial concepts mean more opportunities. The abundance of entrepreneurs brings new ideas, new inertia, and healthier competition. It diversifies the economy and society and expands the range of future alternatives (Faltin, 2018). The emergence of more SMEs in the field of innovation and technology is positive from the perspective of post-corona-crisis development of the country's economy.

Since the beginning of 2020, SMEs are facing great challenges. SMEs are more vulnerable to the

COVID-19 crisis than large firms because they have less financial capacity, a weak supply chain capability, and are characterized by a lower level of mastery of digital tools and technologies (OECD, 2021). In addition, SMEs are more flexible and adaptable than large enterprises, which is useful in times of crisis (Juergensen et al., 2020). Since the lockdown was imposed to stop the COVID-19 pandemic, the tourism and passenger transportation sectors were the first to experience problems. This led to the collapse of stock exchanges, which directly affected the real economy (Papava, 2020). Consequently, SMEs also faced problems. The COVID-19 pandemic has changed the way people work, which has largely moved into the virtual space, the Internet. This has affected almost all areas, from real estate (Marona & Tomal, 2020) to the sale of necessities. SMEs have been affected by significant behavioral changes in society caused by the COVID-19 crisis (Thukral, 2021). The intensive use of digital technologies has been given great importance to adapt to the given situation and to ensure business continuity (Papadopoulos et al., 2020). SMEs have strengthened the importance of Industry 4.0 solutions (Slusarczyk & Pyplacz, 2020) and innovative thinking. In response to the COVID-19 crisis, organizations have actively started using digital methods in offering to clients and in the business process (Thierry et al., 2020).

The COVID-19 pandemic is an unprecedented external shock affecting SMEs in Europe, both in terms of supply and demand. According to the May 2020 survey, in the UK, 41% of SMEs had stopped operations. In Germany, 50% of SMEs expected a negative outcome due to the crisis. In Italy, more than 70% said they were directly affected by the crisis. The situation is similar in other European countries (Juergensen et al., 2020). In the US, SMEs revenues fell to 40%-50% in the first quarter of 2020, and January 2021 revenue

decreased by 31% compared to the previous year. According to the Central Bank, small business sales in Australia fell by 15% between March 1 and September 30, 2020 (OECD, 2021). In China, 80% of SMEs were temporarily closed in February 2020 (Dai et al., 2021).

In order to stop the spread of coronavirus infection, the Georgian government had to impose various large-scale or ad hoc restrictions: international flights were restricted, intercity traffic, the use of public transport; the reception of foreign tourists was practically stopped; twice a year, restaurants, cafes, bars, gyms, shopping malls, stores (except grocery stores) and other businesses were temporarily closed. All of the above has left its mark on the business activity. According to the World Bank study, about 65% of SMEs in Georgia were temporarily closed during the outbreak (Adian et al., 2020).

The COVID-19 pandemic has placed the countries' entrepreneurship policies in a situation of force majeure. In Europe, SMEs have become the center of policy attention from the outset. Helping SMEs has become a top policy priority. Various types of financial assistance have been provided to prevent a liquidity crisis and to reduce employment losses (Juergensen et al., 2020). SMEs support policy in response to the COVID-19 crisis was implemented by countries in the direction of liquidity and structural support. According to an OECD study reviewing the policies of 55 countries with different incomes, the key measures to reduce liquidity problems for SMEs are wage subsidies, payment deferrals, financial support through direct lending, and loan guarantees. Among the structural supporting measures, there is support for teleworking and digitalization and support for product and service innovation (OECD, 2021). In response to the challenges of COVID-19, the activities of the governments of the countries to support SMEs are also recorded by the World Bank. The following eight main measures are distinguished: debt finance, employment support, tax, business costs, other finance, demand, business climate, and business advice (Adian et al., 2020). In Germany, fiscal policy measures, including liquidity subsidies and government guarantees, temporary change in insolvency law, short-time work (STW) scheme, played a major role in responding to the COVID-19 crisis (Dörr et al., 2021). The Japanese

government has implemented emergency loans and credit guarantees to help SMEs (Yoshino & Hendriyetty, 2020).

The government's special activity in Georgia to support SMEs began in 2014. Current supporting activities from the government include the program "Produce in Georgia", ENPARD in cooperation with the Ministry of Agriculture, Georgia Innovation and Technology Development Agency programs, and Startup Georgia.

Today, even under the conditions of the COVID-19 pandemic, favorable conditions are created in Georgia to start a business. According to the 2020 Index of Economic Freedom, Georgia ranks 12th out of 180 countries in the world and 6th in the European region (Miller et al., 2020). Georgia ranks 7th out of 190 countries in the world in terms of its ease of doing business (World Bank Group, 2020).

Starting a new business is a difficult and risky process. The biggest risk an entrepreneur may face is bringing a product to market that no one wants (Bortolini et al., 2021). Entrepreneurship can be initiated in both traditional and innovative ways. The innovative form is associated with the intensive use of digital technology in the entrepreneurial process, which can be called digital entrepreneurship. The peculiarity of digital entrepreneurship and the difference from traditional entrepreneurship is that the parties to a transaction find each other on a digital platform and conduct the necessary transaction. For example, Airbnb connects a hotel renter with a tenant. Airbnb differs from a traditional entrepreneurial hotel by being a digital platform, having no physical resources, and requiring relatively few employees (Pioch, 2019). It is the same with Amazon, where value is created not only by any product but also by the function of viewing, selecting, and transmitting the necessary information, free access to it in time and space, the possibility of electronic selection and ordering online (Kollmann, 2018). In the UK, for example, 51% of SMEs believe that digital technologies are essential to ensure their future competitiveness, while two-fifths of management considers them a top priority (Papadopoulos et al., 2020). In the COVID-19 pandemic, an innovative form of entrepreneurship and the use of digital technologies has become predominant. SME

owners, in order to adapt to the current situation, thought about increasing the innovation capabilities of their enterprise.

2. AIMS AND METHODOLOGY

This study aimed to investigate challenges faced by SMEs and the impact of the pandemic on their revenue and innovation opportunities, using the example of Georgia.

The study addresses the key challenges for SME owners and the behavioral changes that entrepreneurs have experienced in terms of innovating and using digital channels in Georgia, as well as an assessment of government policy by entrepreneurs.

According to the methodology of the National Statistics Office of Georgia, with the definition in force since 2017, the average annual number of employees in small size enterprises does not exceed 50 employees and the average annual turnover does not exceed 12 million GEL. The average annual number of employees in medium-size enterprises ranges from 50 to 250 persons and the average annual turnover – from 12 million to 60 million GEL (GEOSTAT, 2021).

For the purpose of this paper, a survey of SME owners was conducted. 102 of the entrepreneurs participated in the study. 19% of the enterprises are based after the onset of a pandemic. Geographically, entrepreneurs from the capital and 9 regions of Georgia participated in the study. Most of them (63.7%) operate in the capital Tbilisi. By field of activity, 40.2% of surveyed entrepreneurs are employed in manufacturing, 21.6% in services, 15.7% in trade, and 8.8% in ICT. The remaining 13.7% of respondents have businesses in areas such as tourism, agriculture, education, and more. The survey was conducted by sending a questionnaire through digital channels using Google Forms¹. The main questions were about the challenges faced by SMEs in the COVID-19 pandemic, as well as how their sales volume and innovative opportunities have changed. In addition, to determine the relevance of the government economic policy, the entrepreneurs evaluated the

economic policy and named the desired measures that would improve the activities of SMEs. The study process uses analytical and synthesis, quantitative and qualitative, interview/survey, graphing, and data analysis methods.

3. RESULTS AND DISCUSSION

Under the COVID-19 pandemic, many businesses in the world have been disrupted because of a lockdown, which is a necessary measure to stop the spread of the virus (Thukral, 2021). Lockdown has become a major challenge for SMEs. According to the survey, in the face of a pandemic, in Georgia, SME owners cite the imposition of restrictions (lockdown) (60.8%), access to financial resources (33.3%), and access to production materials (28.4%) as the main challenges. In addition, 19.6% of respondents cited access to international markets as the main challenge, 13.7% – shortage of professional staff, and 11.8% – high tax rates. In addition, 11.8% of the respondents considered unhealthy competition in the market as the main challenge, and for 9.8% the problem is barriers to market entry (see Figure 1).

The lockdown caused by the COVID-19 pandemic has led to a decrease in sales of goods and/or services for SMEs. The study confirms this. 15.7% of respondents said they had a significant decrease, and 29.4% said they had a decrease in the volume of sales. Consequently, the sales volume of products and/or services decreased for 45.1% of SMEs during the pandemic. At the same time, 24.5% of businesses had no change in sales volume (see Figure 2). According to studies conducted in various advanced countries of the world, since the beginning of the pandemic, there has also been a significant decline in the revenue and sales of SMEs (OECD, 2021).

Due to the COVID-19 pandemic, remote communication channels were preferred and a large part of activities shifted to virtual space. The same was true for entrepreneurial activities. After the restrictions were imposed, entrepreneurs began to think and act to increase sales of products or services through digital channels. This is confirmed

¹ The form is available at https://docs.google.com/forms/d/e/1FAIpQLSeGgG-5rSExJ640tE7HFYw4-7fLxHDD9R3mR0eHBcPiBeW3Sw/viewform?usp=sf_link

Source: Authors' compilation.

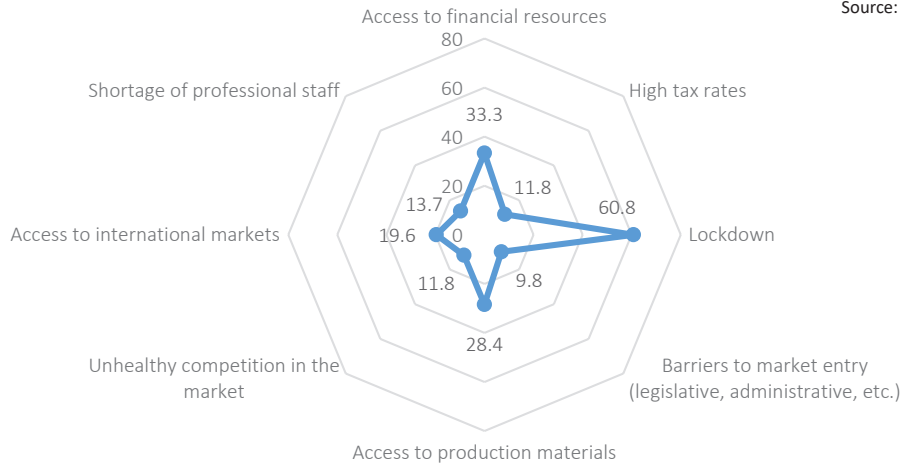


Figure 1. Main challenges of SMEs during the pandemic in Georgia (%)

by a survey conducted, in which 8.8% of SME owners surveyed said they had significantly increased, and 28.4% had increased sales of their products/services in digital channels. Accordingly, 37.2% of SMEs managed to adapt well to the current situation and recorded an increase in the volume of sales through digital channels. In addition, 33.3% of the SMEs surveyed did not see any change in the volume of sales via digital channels (see Figure 3). Although the survey was conducted through digital channels, 9.8% of SMEs do not use digital channels for sales. This indicates that the culture of using digital channels for sales is not yet fully established in Georgia.

Currently, the innovative aspect of entrepreneurship and the formation and efficiency of a knowledge-based economy are of particular importance (Bedianashvili, 2017). Thukral (2021) notes that entrepreneurial action, innovation, and creativity are essential to transform the challenges posed

by the COVID-19 crisis into opportunities. SMEs need to achieve a high level of resilience (e.g., having more than one supplier) in order to achieve better results in fighting the pandemic. In addition, crisis management is needed at both the micro (by entrepreneurs) and macro (by the government) levels and implementation of measures for the revival of the entrepreneurial ecosystem (by the government).

It was interesting to understand how the innovation capacity of SMEs has changed in Georgia in the face of the pandemic. Did they come up with new ideas considering the situation at hand; have they introduced a new product/process/service? 11.8% of SME respondents indicated that they have increased significantly under pandemic conditions, while 27.5% indicated that they have increased their company's ability to innovate. In a solid portion of the total SMEs respondents (39.3%), pandemic innovation opportunities are

Source: Authors' compilation.

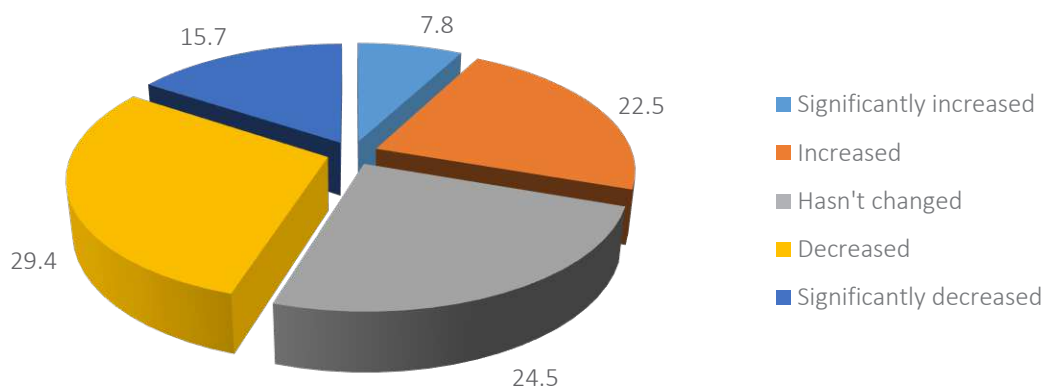


Figure 2. Changes in the SME sales volume of products/services since the start of the pandemic (%)

Source: Authors' compilation.

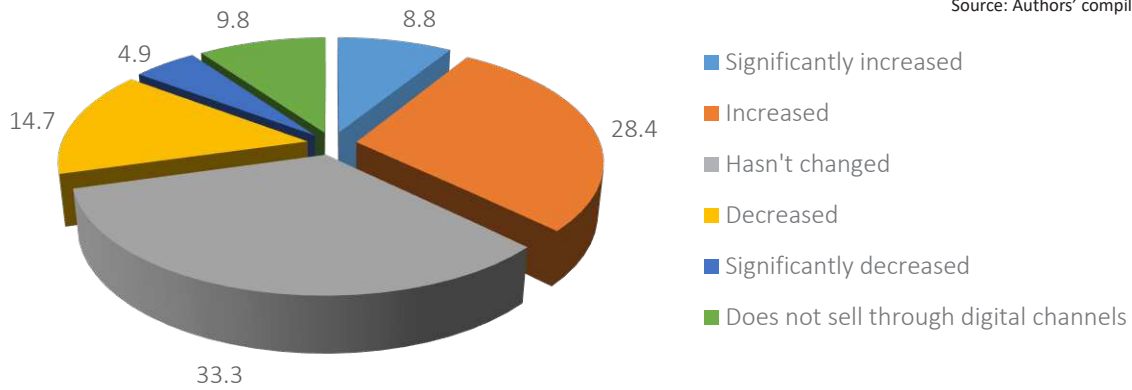


Figure 3. Changes in the SME sales volume of products/services through digital channels since the start of the pandemic (%)

characterized by an upward trend. 40.2% report no change, while 12.7% and 7.8% of SME respondents report a decrease and significant decrease in innovation opportunities. (see Figure 4).

In the context of the COVID-19 pandemic, support of SMEs is an extremely important task. In Georgia, the main problems are political instability and the existence of conflict zones; hard access to credit resources; inflation; high-interest rates on loans; and lack of investment and export subsidies (Erkomaishvili, 2016).

The Georgian government had to take special measures to mitigate the crisis effects caused by the pandemic. To respond to the challenges of COVID-19, the Georgian government mobilized more than 1.6 billion GEL in 2020 to support various businesses. The following measures were taken: for each retained employee, employers were subsidized for 6 months (May to October) – up to 750 GEL salaries were fully exempt from income tax, and up to 1,500 GEL sala-

ries were exempt from income tax (the program will continue in 2021). More than 33,000 businesses benefited from the income tax exemption in more than 425,000 jobs. More than 50,000 taxpayers have deferred tax liabilities of more than GEL 400 million and tax breaks have been implemented. Property tax in the tourism sector was abolished (continued in 2021). Interest expenses were subsidized for hotels and restaurants. The construction sector, agriculture, etc. were also supported (Ministry of Finance of Georgia, 2020).

The Georgian government has been implementing the state program “Produce in Georgia” since 2014. The goal is to help industrial and agricultural entrepreneurs start new businesses, expand existing ones, improve existing ones, and increase the competitiveness and export potential of the private sector through access to finance, real estate, and technical assistance (Government of Georgia, 2016). With the spread of the COVID-19 pandemic, existing entrepreneurship programs have expanded. In 2020, the

Source: Authors' compilation.

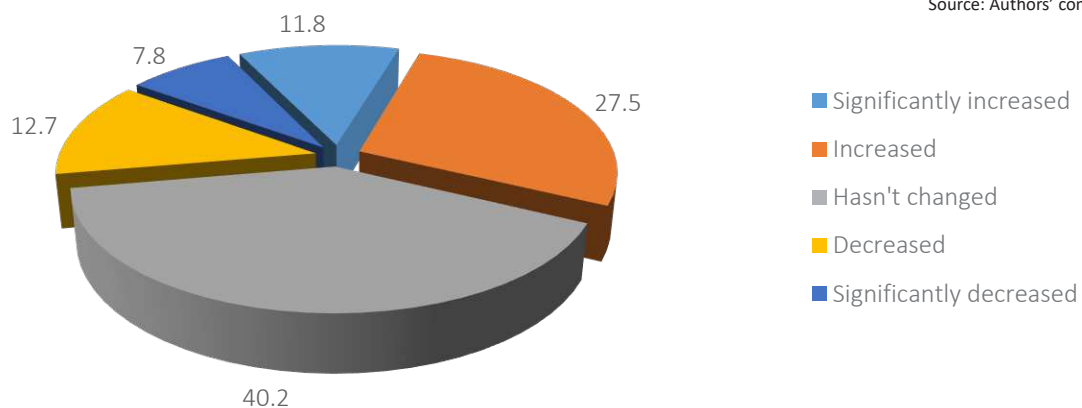


Figure 4. Has SMEs innovation increased during the COVID-19 pandemic (%)?

agency's budget increased from GEL 57.5 million to GEL 477 million (Enterprise Georgia, 2021).

Regarding the general evaluation of government support policies by SME owners, a solid portion of SME owners still do not evaluate government support positively, despite the support programs mentioned above. Regarding the question – “How would you rate the government's support policies toward SME owners?”, 17.2% answered that they would rate it negatively, while 24.2% said they would rate it mostly negatively. Overall, 41.4% of SME owners do not rate the government's efforts positively. Desirable actions of the government that would improve the activities of SME owners who rated the government's activities negatively or mostly negatively included promotion in sales; assistance in raising awareness; tax benefits, exemption from certain taxes in the start-up phase; the need for regular training organization of digital technologies, marketing training to improve the skills of employees; logic and appropriateness of criteria in the awarding of grants and funding; facilitating the search for investors; less bureaucracy, and more.

In Georgia, in the context of the COVID-19 pandemic, SME owners name the imposition of restrictions (60.8%), access to financial resources (33.3%), and access to production materials (28.4%) as the main challenges. In addition, 19.6% of respondents named

access to international markets as a major challenge. The study showed that for 39.3% of SMEs surveyed under the pandemic, innovation opportunities are characterized by an upward trend. It can be said that the pandemic was a good opportunity to increase the innovative capacity of the enterprise. 37.2% of the SME owners surveyed managed to adapt to the current situation and increase the sale of their products/services through digital channels. As for the general assessment of government support measures by SME owners, a large part does not evaluate the measures taken by the government positively. 17.2% of entrepreneurs gave a negative assessment of the government's supportive policy towards SMEs.

The Georgian government needs to eliminate the problems faced by the country's current business sector through the targeted implementation of rational economic development policies. It is necessary to achieve inclusive economic growth (Maglakelidze, 2019). The government needs to focus on the challenges mentioned by entrepreneurs. During the COVID-19 pandemic, the government should continue tax incentives and subsidies for SMEs. In addition, a long-term action plan should be developed to combat the crisis. In response to modern challenges, the government should promote education in the areas of entrepreneurship, innovation, and technology. It is necessary to attract investments and facilitate entry into export markets.

CONCLUSIONS

The COVID-19 pandemic has a significant impact on SMEs around the world, including Georgia. The study aimed to show the impact of the COVID-19 pandemic on SMEs in different areas, for example, sales volume, innovation opportunities, challenges, and government SME policy.

As a result, it was revealed that the main challenge for SMEs is a lockdown. In addition, access to financial resources and access to production materials is also a significant challenge. Under the pandemic, sales of enterprises decreased, while sales through digital channels increased. A solid portion of the enterprises has increased the innovative capabilities of the company. The policy of the government is negatively assessed by a large number of SME owners. Entrepreneurs named the main measures to be taken by the government that would improve their performance. For example, flexible tax system, sales promotion, training in digital technology and marketing, reduction of bureaucracy.

Thus, it can be concluded that the pandemic has created serious problems for SMEs. In this situation, the role of government support and rational economic policy is important to overcome the challenges in the SME sector and to continue irreversible development. In addition, the COVID-19 pandemic has become a good opportunity to develop innovative capabilities and make greater use of digital channels. This is a progressive trend and needs to be continued after the pandemic.

AUTHOR CONTRIBUTIONS

Conceptualization: Amiran Maglakelidze, Gulnaz Erkomaishvili.
 Data curation: Amiran Maglakelidze.
 Formal analysis: Amiran Maglakelidze.
 Funding acquisition: Amiran Maglakelidze, Gulnaz Erkomaishvili.
 Investigation: Amiran Maglakelidze.
 Methodology: Amiran Maglakelidze, Gulnaz Erkomaishvili.
 Resources: Amiran Maglakelidze.
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 Validation: Amiran Maglakelidze.
 Visualization: Amiran Maglakelidze.
 Writing – original draft: Amiran Maglakelidze.
 Writing – review & editing: Amiran Maglakelidze, Gulnaz Erkomaishvili.

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