Economic context

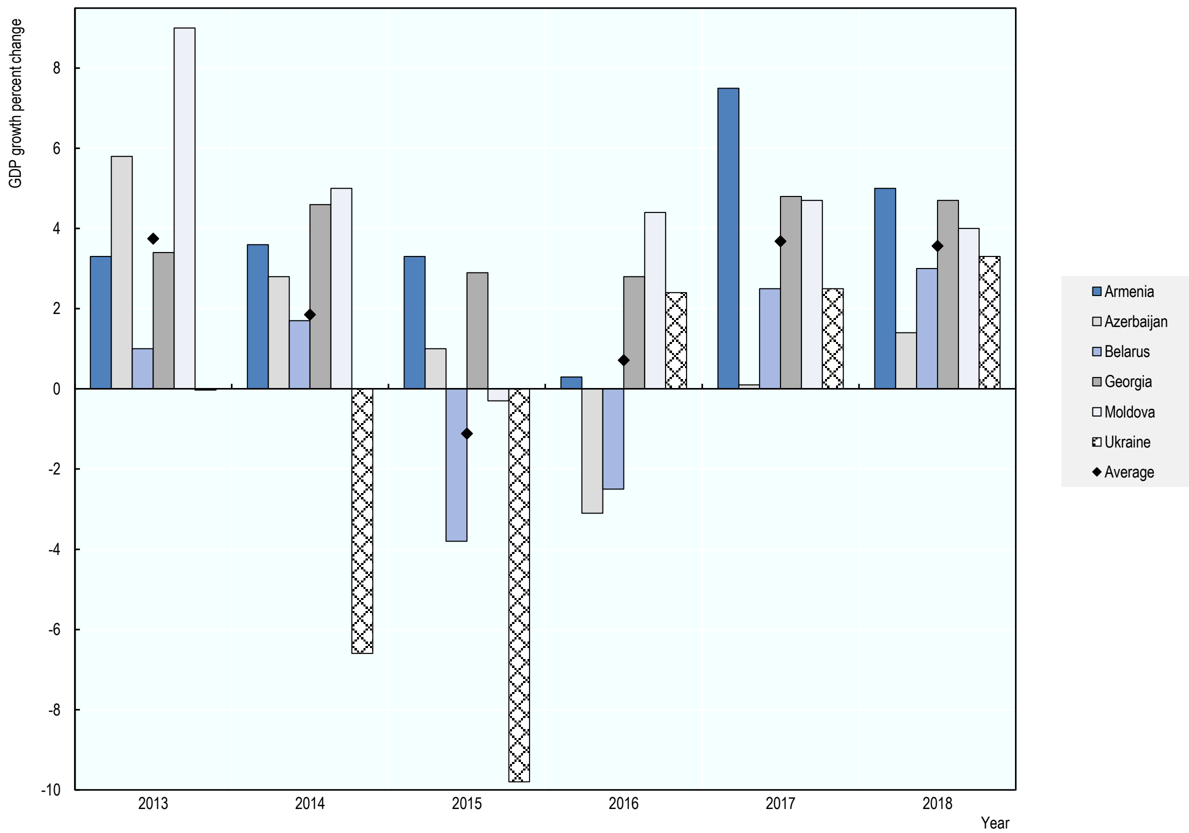
The countries of the Eastern Partnership (EaP) region were hit by a series of political and economic shocks in 2014-15, including the end of the commodity super-cycle, slower growth in China and Western Europe, and the conflict in Ukraine that followed Russia's seizure of Crimea and its intervention in Eastern Ukraine. Western sanctions and counter-sanctions also hit the EaP countries to varying degrees. Azerbaijan, Belarus, the Republic of Moldova and Ukraine all underwent recessions, while Armenia and Georgia experienced slowdowns. The region as a whole contracted in 2014-15 before starting to recover in 2016 (Figure 4). Although the pace and strength of the recovery varied from one country to another, it gradually gained momentum in 2017-18, supported by more favourable economic conditions and successful macroeconomic stabilisation efforts by some EaP governments. As of mid-2019, EaP countries are continuing to record vibrant economic growth rates, despite some signs of moderation.

The EaP countries remain heavily dependent on Russia, albeit to varying degrees, owing to its importance in regional trade flows. However, EaP trade is steadily diversifying *away* from Russia; Azerbaijan, Georgia, Moldova and Ukraine, in particular, are redirecting their exports towards the EU. This trend was likely amplified by entering the Deep and Comprehensive Free Trade Area (DCFTA) with Moldova and Georgia in July 2016, and with Ukraine in September 2017.

Sustained and more resilient growth will be contingent on a continued supportive regional economic backdrop and efforts to address the structural weaknesses revealed by the economic downturn of 2014-15 – which exposed, in particular, the limited diversification of the EaP economies and their lack of competitiveness in most sectors.

Small and medium-sized enterprises (SMEs) play a significant role in the economies of the six EaP countries, but their potential remains largely untapped. Even though all EaP countries have recognised the importance of improving the business environment for SMEs and are striving to simplify business-related legislation and to provide SMEs with targeted support, they must still do more to improve general level-playing-field conditions – competition, contract enforcement and business integrity. These fundamental pillars of open and fair economies are preconditions for developing a vibrant private sector, ultimately enhancing economic competitiveness and trigger inclusive and sustainable economic growth.

Figure 4. Real GDP growth, 2013-18



Source: OECD calculations based on data from the World Bank's (2019[1]) *World Development Indicators* Database.

StatLink http://dx.doi.org/10.1787/888934086337

A heterogeneous region with a diverse economic structure

The EaP countries' location makes the region an important transit corridor. Georgia and Ukraine have access to international sea routes through the Black Sea, while Azerbaijan has a coast on the Caspian Sea. Belarus, Moldova and Ukraine all border the EU. However, as Table 1 shows, the EaP countries vary significantly in terms of population, resource endowments and economic structures (see Table 27 later in this section for economic snapshots of the EaP countries).

Table 27. Key data for the Eastern Partner countries, 2018

	Total area (km²)	Population (million inhabitants)	GNI* per capita (Atlas method**, current US$)	Arable land (% of land area)	Rural population (% of total population)
Armenia	29 740	2.95	4230	16	37
Azerbaijan	86 600	9.94	4050	24	44
Belarus	207 600	9.49	5670	28	21
Georgia	69 700	3.73	4130	5	41
Moldova	33 850	3.55	2990	56	57
Ukraine	603 550	44.62	2660	57	31

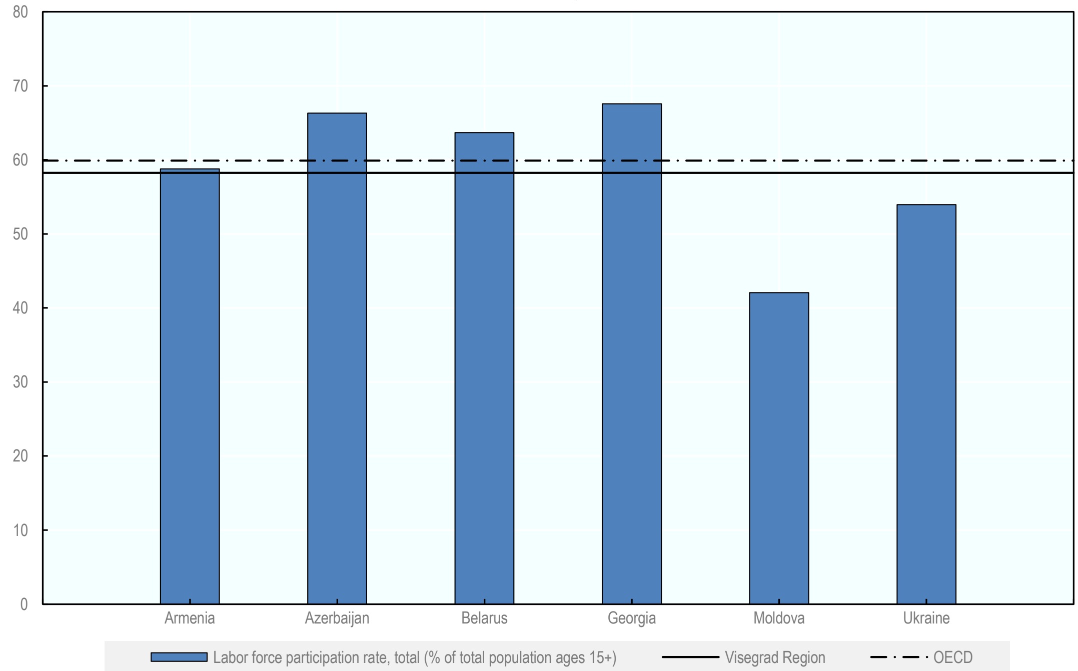
* GNI: gross national income.
** The *Atlas* method consists in applying a conversion factor that averages the exchange rate for a given year and the two preceding years, adjusted for differences in rates of inflation between the country and international inflation (from 2001, the euro area, Japan, the United Kingdom and the United States).
Source: World Bank's (2019[1]) *World Development Indicators* Database.

All EaP countries except Azerbaijan have limited natural resource endowments. Total natural resources rents[1] as a percentage of GDP range from 5.8% in Armenia to 0.3% in Moldova (World Bank, 2019[1]). In Azerbaijan, by contrast, hydrocarbon rents represent 21% of GDP (World Bank, 2019[1]) and the vast majority of exports. Ukraine is the 15th-largest exporter of iron and steel in the world, accounting for 2.4% of world's exports in 2018 (ITC, 2019[2]).

Despite falling as a share of GDP and employment, agricultural production remains substantial in all six countries – particularly in Armenia and Moldova where it accounted for 14.9% and 12.1% of gross value added in 2017. Ukraine is a large exporter of cereals, accounting for 6.6% of world total exports in 2018, while Belarus is the world's fifth-largest fertiliser exporter, generating 5.4% of world exports in 2018 (ITC, 2019[2]).

The region has a highly literate population; literacy is close to 99% in all countries and secondary school enrolment is over 85% in all countries except Moldova. However, considerable discrepancies remain in terms of unemployment rates – which range from 3.4% in Moldova to 17.7% in Armenia (World Bank, 2019[1]). In 2018, labour force participation rates averaged 58.6% across the EaP countries, slightly below the OECD average of 59.9%, but gender disparities persist (Figure 5, Figure 6). Moldova shows the lowest female labour force participation (38.9%) while Georgia displays the biggest gap (male labour force participation reached 78.7% in 2018 while female participation stood at 57.8%). Moreover, the limited evidence available suggests that the informal sector is relatively large in most EaP countries, especially in agriculture and services.

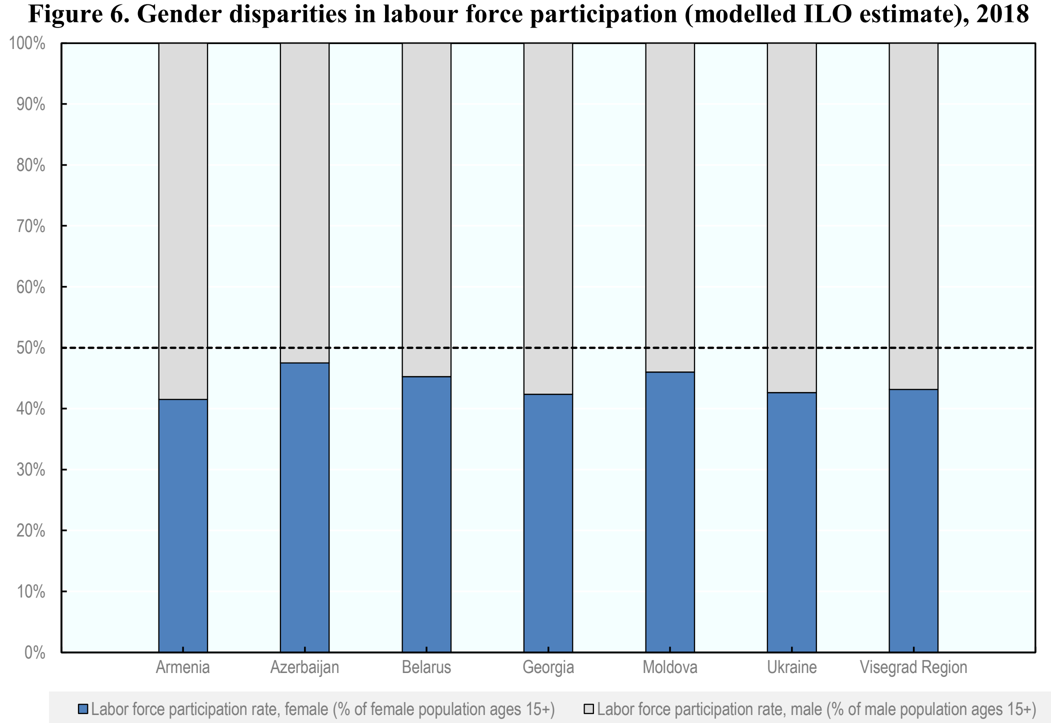
Figure 5. Labour force participation rate, total (% of total population ages 15+; modelled ILO estimate), 2018



Source: OECD calculations based on data from the World Bank's (2019[1]) *World Development Indicators* Database.

StatLink http://dx.doi.org/10.1787/888934086356

Figure 6. Gender disparities in labour force participation (modelled ILO estimate), 2018



Source: OECD calculations based on data from the World Bank's (2019[1]) *World Development Indicators* Database.

StatLink http://dx.doi.org/10.1787/888934086375

Box 5. Economic snapshots of EaP countries

Armenia, a landlocked and mountainous country, is the smallest of the six EaP countries. Its economy is driven mainly by the industrial and agricultural sectors, which in 2017 accounted for 25.3% and 14.9% of GDP, respectively, with ores and metal accounting for nearly 40% of exports in 2017. The country is highly reliant on Russia both in terms of trade (roughly a quarter of total exports in 2018) and in terms of remittances (64% of total received in 2017 (World Bank, 2019c[3]). The country became a member of the Eurasian Economic Union (EAEU) in January 2015. Following near-stagnation in 2016, Armenia saw real GDP growth accelerate to 7.5% in 2017 before moderating in 2018.

Azerbaijan's economy is dominated by the oil and gas industry, which accounted for around 38% of GDP and 90% of exports in 2018. This makes the country vulnerable to fluctuations in oil prices. Recovery from the oil-price drop in the middle of the decade has been slow, as the economy recorded just 1.4% real growth in 2018, supported by the upward trend in oil prices, though non-oil GDP expanded somewhat faster. The ongoing expansion of gas production (through the construction of the Southern Gas Corridor between Azerbaijan and Europe for 2020-21 completion) as well as efforts to develop non-oil sectors should support export capacity and growth. Key trade partners are the EU (54% of total exports in 2018), Russia and Turkey. Russia accounts for a comparatively small share of total exports but is the most important destination for *non-hydrocarbon* exports.

Belarus's economy is dominated by large state-owned enterprises, which generated nearly one third of value added in 2016 (IMF, 2019a[4]). The Belarusian economy is driven mainly by manufacturing, which accounts for 41% of GDP, followed by agriculture, wholesale and retail trade, each accounting for nearly 10% of GDP in 2017 (Belstat, 2019[5]). As a member of the EAEU, Belarus is largely dependent on trade with Russia, which accounted for 38% of total exports in 2018. The country also benefits from access to Russian energy at subsidised prices and preferential access to the Russian market. A recession in 2015-16 gave way to modest recovery, with growth of 2.5% in 2017 and 3% in 2018.

Georgia's economy is based on a relatively small industrial sector and on agricultural processing, which accounted respectively for 22.6% and 6.8% of GDP in 2017. The country imports most of its natural gas and oil products. Georgia is located at the centre of an important regional transit corridor, and transport services accounted for 24.6% of commercial service exports in 2017. New transport infrastructures –with the Anaklia Deep Sea Port scheduled for 2021 completion and the recent signature of trade agreements with the EU and China – are expected to transform the country into a logistics hub. In 2018, the EU became the first export destination of Georgian products, accounting for 22%, while exports to Russia represented 13% of total exports (United Nations, 2019[6]).

Moldova relies heavily on exports of basic agricultural products such as vegetables. These make up 27% of the total export basket, making the country particularly vulnerable to variations in food prices in key exports markets, such as the EU, to which nearly 70% of exports were directed in 2018. The Moldovan economy is highly dependent on remittances (20.16% of GDP in 2017), particularly from Russia (32% of total remittances in 2017; (World Bank, 2019c[3]).

Despite the unresolved conflict in the east of the country, **Ukraine** remains the largest EaP economy, generating over 45% of the region's GDP. Industry and agriculture continue to drive the Ukrainian economy and represented 24% and 10.2% of GDP respectively, in

2017. GDP contracted by 16% in 2014-15 and the subsequent recovery has been modest, though gaining in strength. Growth in 2018 reached 3.3%, with aggregate GDP in real terms still almost 15% below the peak recorded in 2008. The country possesses 30% of the world's richest black soil, giving its agricultural industry a huge potential. Key trade partners are the EU and Russia, which respectively received 43% and 8% of Ukrainian exports in 2018.

Sources: Unless otherwise specified in the text, figures are from (World Bank, 2019[1]) and (ITC, 2019[2])

Table 28. Key macroeconomic indicators for Eastern partner countries, 2018

Indicators	Unit of measurement	Armenia	Azerbaijan	Belarus	Georgia	Moldova	Ukraine
GDP growth*	Percentage, y-o-y	5.2	1.4	3.0	4.7	4.0	3.3
Inflation**	Percentage, average	2.5	2.3	4.9	2.6	3.1	10.9
Government balance[1]**	Percentage of GDP	-1.8	5.6	2.4	-0.9	-1.1	-2.2
Current account balance*	Percentage of GDP	-9.4	12.9	-0.4	-7.7	-10.5	-3.3
Exports of goods and services*	Percentage of GDP	37.5	54.3	70.2	55.1	30.4	45.2
Imports of goods and services*	Percentage of GDP	52.9	37.7	69.1	66.7	56.3	53.8
FDI net inflows*	Percentage of GDP	2.0.	3.0	2.5	7.3	2.1	1.9
General government gross debt**	Percentage of GDP	51.3	18.8	47.8	44.9	29.7	60.2
Domestic credit to private sector*	Percentage of GDP	55.6	20.8	27.8	68.0	23.5	34.1

[1]General government net lending/borrowing.
[2]Modeled ILO estimates.

Source: *World Bank (2019[1]), *World Development indicators;* **IMF (2019b[7]), *World Economic Outlook*, both accessed on December 2019

Regional recovery but uncertain prospects

After the region's average annual growth plunged to -1.1% in 2015, the trend reversed (all six countries reported positive real GDP growth) but reached a plateau in 2017/2018 – with the region's aggregate growth rising to 2.3% in 2017 and 3.1% in 2018. A more favourable external environment and less volatile macroeconomic conditions helped the countries to recover through remittances, trade and investment channels, albeit to varying degrees. Rising real wages and remittance inflows supported by Russia's return to growth have bolstered domestic demand, which continues to be the main contributor to growth. Stable macroeconomic conditions – thanks to deft monetary policies and reductions in public debt – helped to reduce inflationary pressures and maintain relatively stable exchange rates (EBRD, 2018[8]).

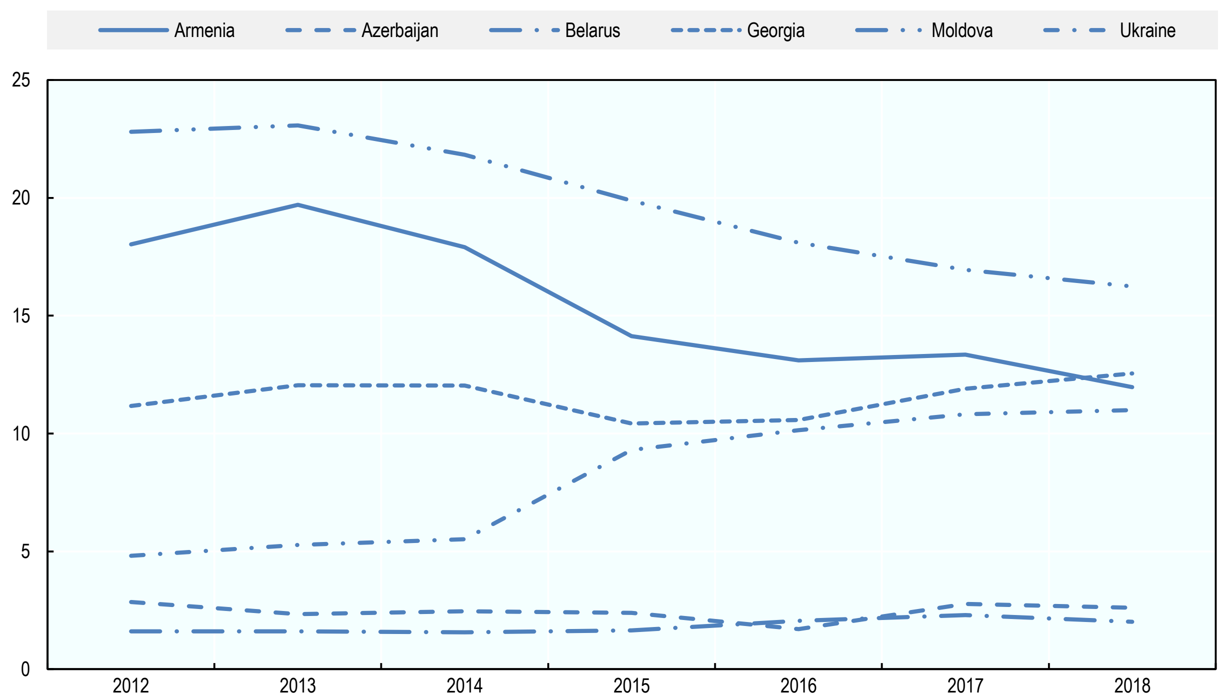
However, the factors that led to the shocks of 2014-15 are still present and leave the region vulnerable – particularly to slower growth in trading partners, commodity price fluctuations and uncertain geopolitical conditions.

Persistent cyclical and structural weaknesses

Trends in remittances inflow are an important determinant of domestic demand

The recent recovery was driven largely by domestic demand, supported in many countries by the recovery of remittance income from labour migrants. In 2017, total personal remittance flows to the region grew by 26.1%, rising by a further 13.7% in 2018. Moldova and Armenia remain the most dependent on remittances (respectively 17% and 13% of GDP in 2017) (World Bank, 2019[1]). In the EaP region, remittances from Russia represent nearly half of the remittances received (except in Moldova, where remittances from Russia account for 33% of total remittances) (World Bank, 2019c[3]). Remittances therefore act as a major transmitter of external shocks, leaving the EaP countries highly dependent on the economic development of Russia.

Figure 7. Personal remittances, received (% of GDP)



Source: OECD calculations based on data from the World Bank's (2019[1]) *World Development Indicators* Database.

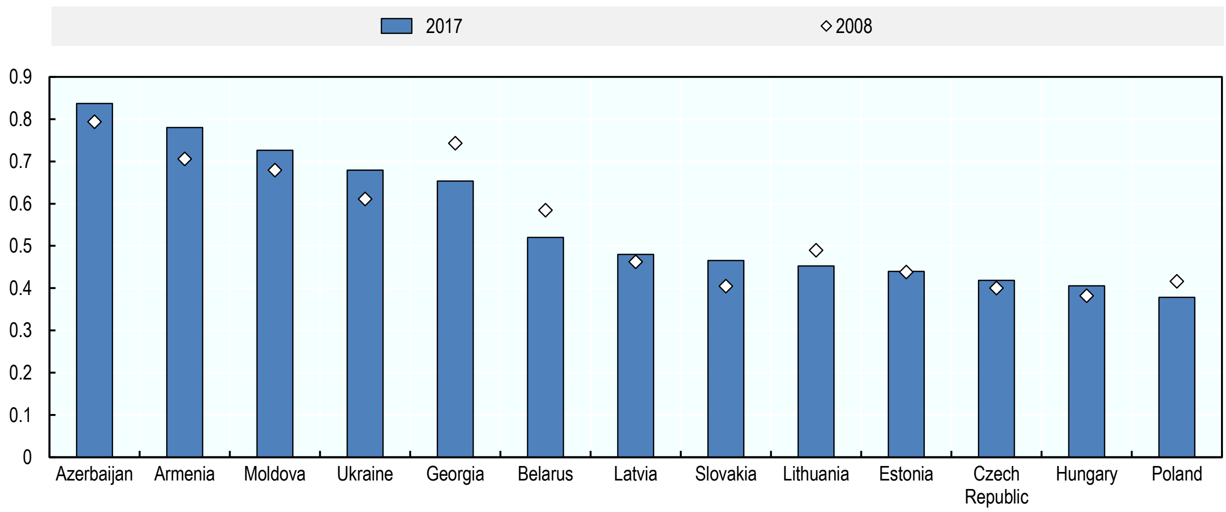
StatLink http://dx.doi.org/10.1787/888934086394

Despite some export diversification, competitiveness remains low and market concentration high

In addition, relatively low levels of competitiveness and limited diversification expose the region to fluctuating commodity prices and volatile demand from its main trading partners. All EaP economies are concentrated in terms of both products exported and trading partners. In 2017, all EaP countries had export baskets less diversified than comparable economies in the EU (Figure 8). Moreover, the majority of the EaP countries displayed a Hirschman Herfindahl Index (HHI) of product concentration higher than comparable economies in the EU. (Figure 9). Belarus's situation is of particular concern, with the highest market concentration in the region in 2017 – increasing since 2008, along with that of Armenia and Georgia.

Figure 8. Product diversification in Eastern partner countries

Product diversification index, 2008 vs 2017

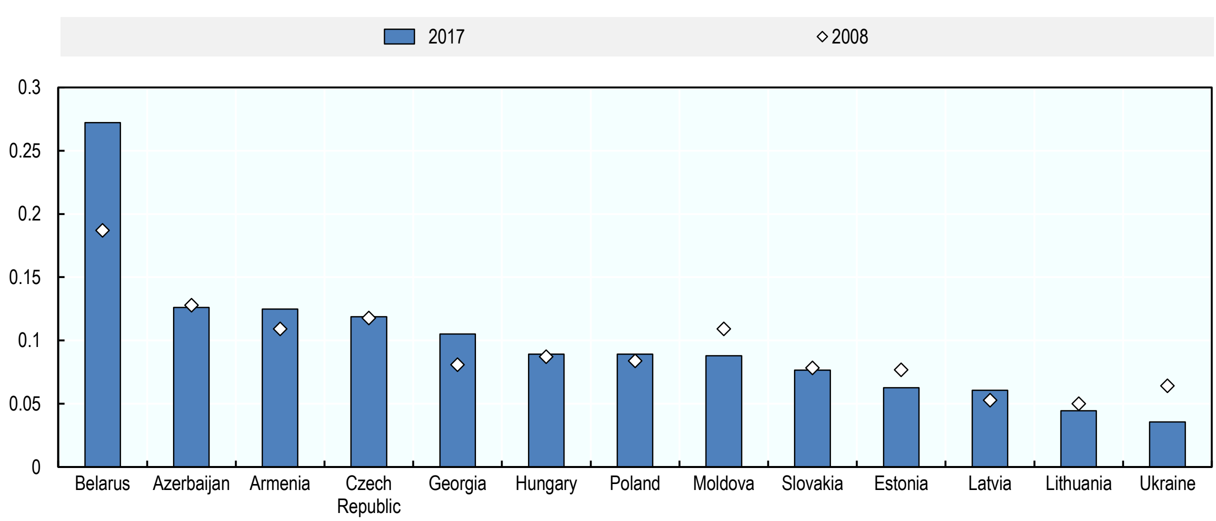


* The product diversification index is computed by measuring the absolute deviation of the trade structure of a country from world structure. It takes values between 0 and 1; a value closer to 1 indicates greater divergence from the world pattern.
Source: OECD calculations based on data from the United Nation's (2019[9]) UNCTAD database.

StatLink http://dx.doi.org/10.1787/888934086413

Figure 9. Product concentration in the Eastern partner countries

Hirschman Herfindahl* product concentration index, 2008-2017

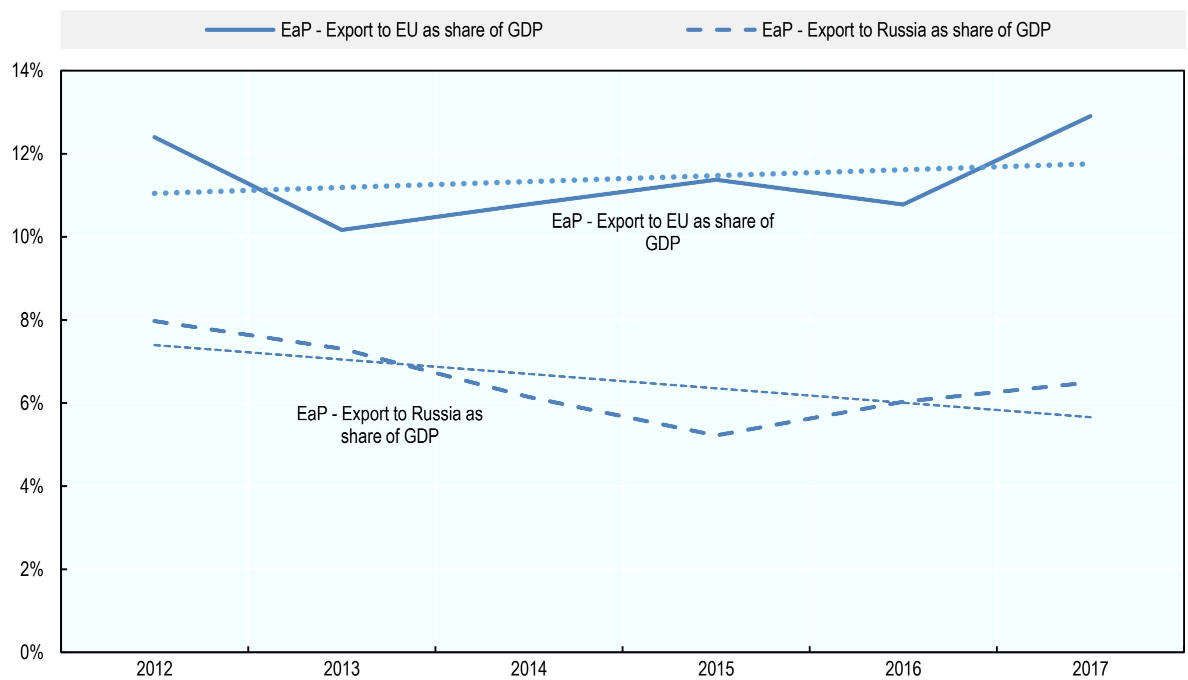


* The Hirschman Herfindahl (HH) index is a measure of dispersion of trade value across an exporter's partners. A country with trade (export or import) that is concentrated in a very few markets will have an index value close to 1. Similarly, a country with a perfectly diversified trade portfolio will have an index close to zero (World Bank definition).
Source: OECD calculations based on data from the World Integrated Trade Solution (WITS) software.

StatLink http://dx.doi.org/10.1787/888934086432

However, there is some evidence of long-term trade diversification across the EaP region, as countries redirect their exports towards the EU. In 2017, exports from the EaP countries to the EU increased by 40% compared to the previous year. In 2018, the EU was the destination of 69% of Moldova's exports, followed by Azerbaijan (54%), Ukraine (43%), and Belarus (30%) (ITC, 2019[2]). In a context of trade blockages in the east of Ukraine, many enterprises have been able to secure access to the EU market. As such, total Ukrainian trade with the EU reached 40% of total exports in 2017, up from 24% in 2009. Georgia's trade with the EU has also increased, but to a lesser extent (from 21% of total exports in 2009 to 22% in 2018).

Figure 10. Export to Russia and to EU, as share of GDP



Source: OECD calculations based on data from the United Nation's (2019[6]) Comtrade Database.

StatLink http://dx.doi.org/10.1787/888934086451

The Deep and Comprehensive Free Trade Areas (DCFTAs), which came into full force in July 2016 in Moldova and Georgia and in September 2017 in Ukraine, could reinforce the diversification of EaP economies. Under the agreements with the EU, the legislation and standards of these countries must move closer to the EU *acquis*. Further approximation of laws, standards and product safety regulations should remove the remaining barriers between these countries and the EU in the future.

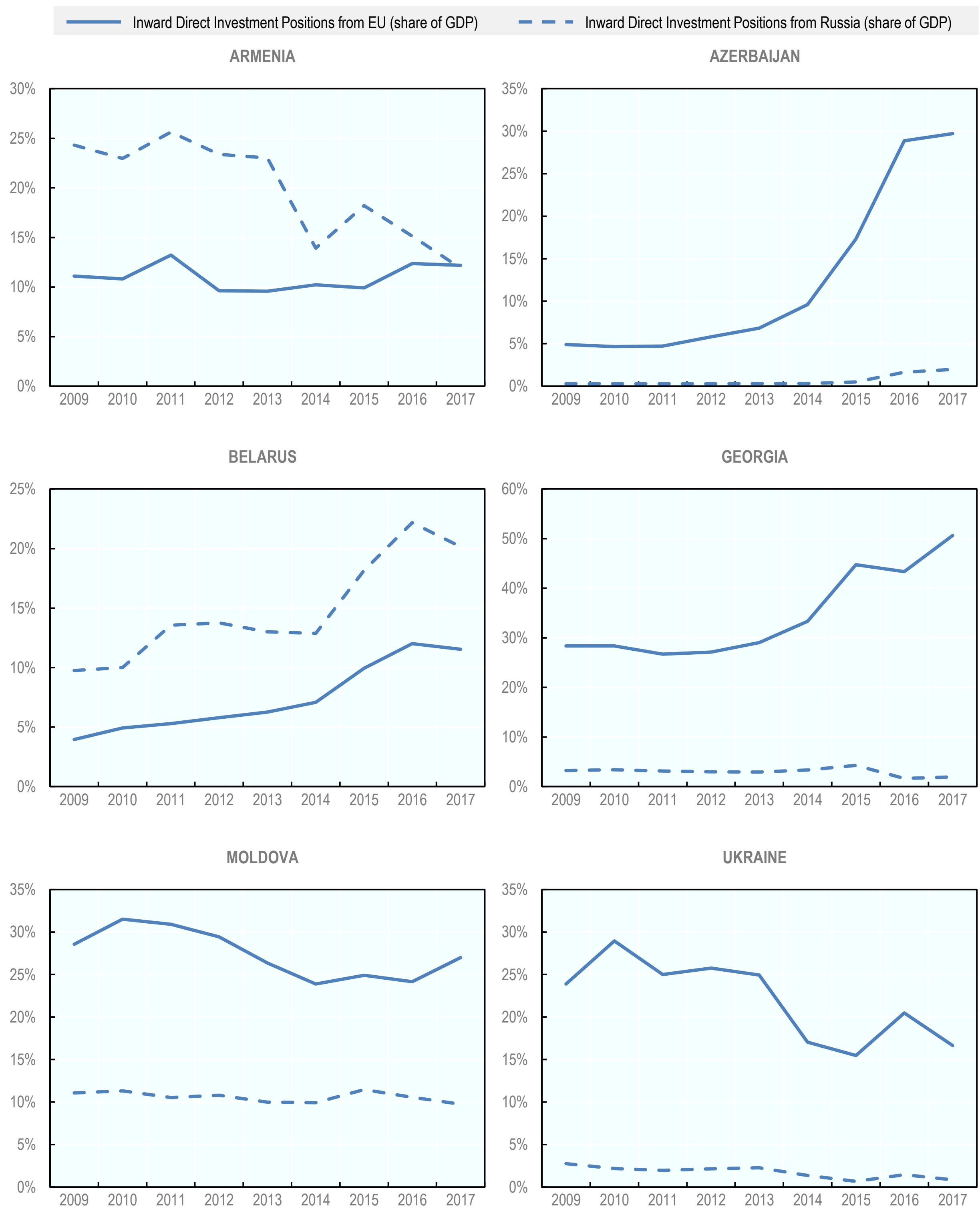
EaP countries are also gaining improved access to other large markets. Georgia signed a free trade agreement with China in 2018, and discussions with India are ongoing. These and other such agreements would reorganise trade flows across the region, leading to further trade diversification and improving countries' economic attractiveness to international investors. This would also affect the SME sector, as diversification of exports and improvement of production capacity are crucial to optimise SMEs international business strategies and increase their productivity to face a globally competitive environment.

The weak economic environment and the uncertain geopolitical outlook undermine investor confidence

Inflows of foreign direct investment (FDI) to EaP countries are recovering at a slower pace due to a challenging economic environment and the uncertain geopolitical outlook. They have yet to return to pre-crisis levels – especially in Ukraine, where FDI inflows in 2018 were only 23% of their 2008 values. Georgia is the only country where net FDI inflows have almost recovered to previous levels; they reached 7.3% of GDP in 2018 in the wake of the implementation of the DCFTA and energy-related projects, which boosted investors' confidence. In recent years the sources of FDI inflows have diversified, with an increased share of inflows coming from the EU at the expense of Russia, in each of the EaP countries except Belarus (Figure 11). As such, the stock of FDI from the EU represented 51% and 30% of Georgia and Azerbaijan's GDP, respectively, in 2017, up from 28% and 4% in 2009 (IMF, 2019c[10]).

However, the EaP countries face persistent structural weaknesses, including long-term demographic challenges and institutional problems such as opaque governance, weak judicial systems, and a lack of competitive neutrality due to the dominance of state ownership in key sectors of the economy. Political and geopolitical tensions, especially in the east of Ukraine, have undermined investor confidence. Economic and political instability in the region therefore remains a significant obstacle to increasing both domestic investment and FDI. Meanwhile, attracting investment remains crucial for the region – as a source not only of financing, but also of knowledge and as a potential catalyst for SME development.

Figure 11. Foreign direct investment from EU and Russia, as share of GDP, 2009-17



Source: OECD calculations based on data from the IMF's (2019c[10]) Coordinated Direct Investment Survey.

StatLink http://dx.doi.org/10.1787/888934086470

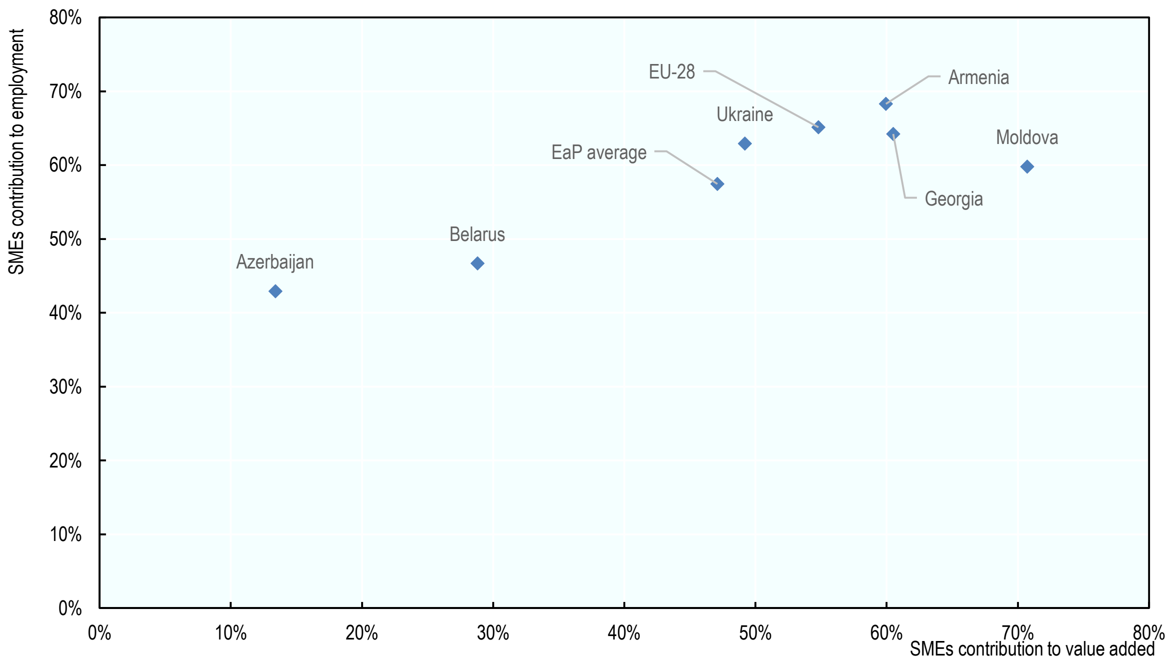
SMEs have not yet tapped their full potential for competitiveness and economic growth

SMEs are key components of a diversified and competitive economy. Small and medium-sized entrepreneurs are risk-takers and tend to be owners of innovative assets, with a large potential to grow; but they are also flexible enough to respond efficiently to changes in global demand. Allowing SMEs to start, grow and better integrate into global value chains (GVCs) – and thus to benefit from productivity gains from organisational and technological improvements – would result in greater diversification, and higher-quality job creation in EaP countries (OECD, 2019[11]).

SMEs represent the large majority of EaP countries' business population (about 99% in Armenia, Belarus, Georgia, Moldova and Ukraine in 2017). The large majority of SMEs in the EaP countries are microenterprises, which represented more than 90% of the total enterprise population across the region in 2017-18. The share of medium-sized enterprises in the total business population continues to decline relative to smaller enterprises across the region. In most EaP countries, SMEs' contributions to growth and job creation are comparable to those found in the European Union (Figure 12).

Figure 12. SMEs contribution to the economy in EaP countries is on par with EU levels

SMEs contribution to value-added and employment as share of total enterprises, 2018 or latest available



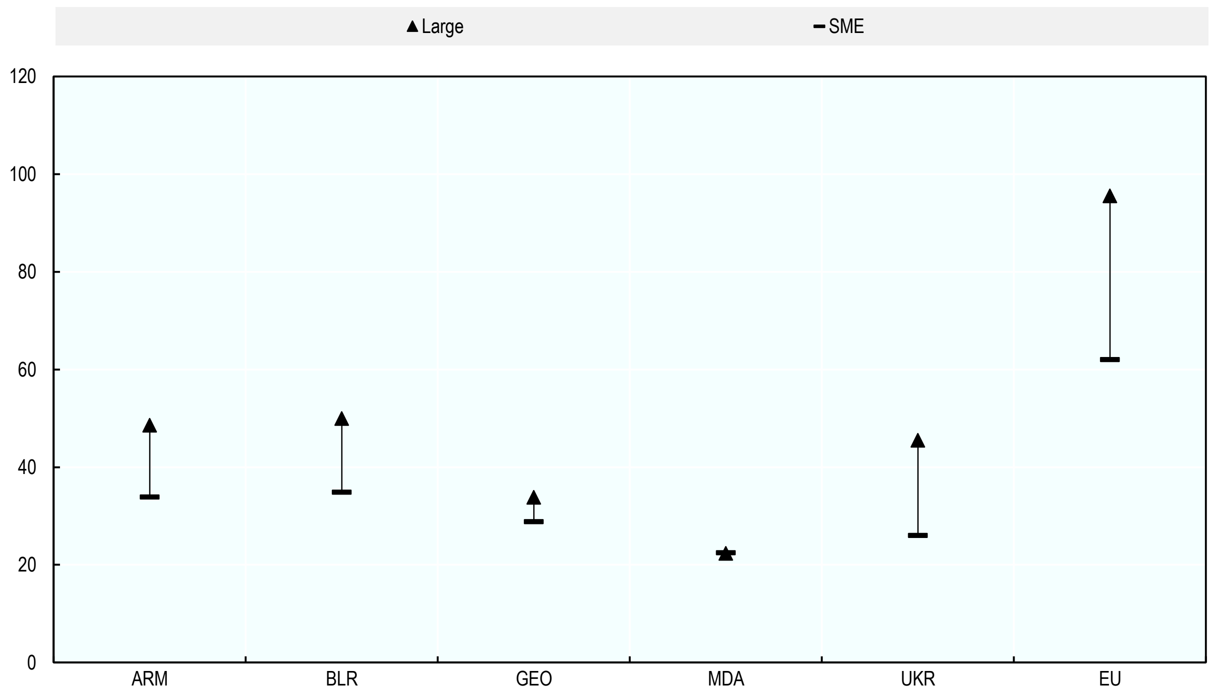
Notes: 2018 data for Armenia, Azerbaijan, Georgia, and Ukraine; 2017 data for Belarus, Moldova, and EU-28. Moldova value-added figures are estimated. EU-28, Ukraine and Armenia figures correspond to SMEs in the non-financial business sector. Belarus figures for microenterprises include individual entrepreneurs. Data on employment refer to number of employees for all the countries except for Ukraine, where data refer to number of employed persons.
Source: OECD calculations, based on data from national statistical offices and from Eurostat (2020[12]).

StatLink http://dx.doi.org/10.1787/888934086489

However, SMEs in the EaP region show low levels of labour productivity, especially relative to EU levels (Figure 13). This reflects primarily the SMEs' concentration in low-value-added sectors of the economy – the wholesale and retail trade sector, generally followed by the manufacturing sector – but also their low integration into global value chains.

Figure 13. Remaining gap in SME labour productivity in EaP countries vs. EU

Value added per employee, thousands of USD, current PPPs (2018 or latest available year)



Notes: Data do not include Azerbaijan because of statistical inconsistency. 2017 data for Belarus, EU, and Moldova. Data for EU, Armenia and Ukraine refer to the business economy (ISIC rev.4 sections B-N excluding K financial intermediation). Due to data unavailability, labour productivity is measured as value added per employee instead of value added per person employed, except for Ukraine where the number of persons employed is considered.
Source: OECD calculations based on data from national statistical offices and from Eurostat (2020[12]).

StatLink http://dx.doi.org/10.1787/888934086508

Table 29. SME sector statistics, 2018 or latest available

	ARM		AZE		BLR		GEO		MDA		UKR	
	Number	Share	Number	Share	Number	Share	Number	Share	Number	Share	Number	Share
Number of enterprises												
Micro	64,344	93.69%	-	-	338,749	95.6%	-	-	48,032	85.1%	1,520,293	95.5%
Small	3,686	5.4%	-	-	11,528	3.3%	122,858	98.3%	6,374	11.3%	59,642	3.7%
Medium	624	0.9%	-	-	2,237	0.6%	1,756	1.4%	1,299	2.3%	9,918	0.6%
Large	126	0.2%	-	-	1,742	0.5%	368	0.3%	757	1.3%	2,417	0.2%
SMEs	***68,654***	***99.8%***	***-***	***-***	***352,514***	***99.5%***	***124,614***	***99.7%***	***55,705***	***98.7%***	***1,589,853***	***99.8%***
Employment												
Micro	82.585	26.5%	35,014	5.3%	543,189	19.8%	-	-	99,311	18.8%	2,534	34.6%
Small	69,328	22.2%	76,052	11.5%	393,810	14.4%	276,969	40.8%	117,030	22.2%	1,076	14.7%
Medium	61,050	19.6%	172,366	26.1%	341,012	12.5%	159,299	23.4%	99,311	18.8%	989	13.5%
Large	99,042	31.7%	377,249	57.1%	1,460,701	53.3%	243,185	35.8%	212,281	40.2%	2,716	37.1%
SMEs	***212,963***	***66.3%***	***283,432***	***42.9%***	***1,278,011***	***46.7%***	***436,268***	***64.2%***	***315,652***	***59.8%***	***7,315***	***62.9%***
Value added (in local currency, million)												
Micro	-	-	4,468	6.1%	10,825	10.4%	-	-	12,023	19.6%	382,202	17.3%
Small	954,899	40.4%	1,236	1.7%	10,721	10.3%	7,159	34.5%	15,074	24.6%	310,227	14.0%
Medium	462,881	19.6%	4,133	5.6%	8,431	8.1%	5,375	25.9%	16,304	26.6%	395,930	17.9%
Large	946,557	40.0%	63,571	86.6%	n/a	n/a	8,193	39.5%	17,963	29.3%	1,123,834	50.8%
SMEs	***1,417,780***	***60.0%***	***9,837***	***13.4%***	***29,977***	***28.8%***	***12,534***	***60.5%***	***43,401***	***70.7%***	***1,088,360***	***49.2%***

Notes:
ARM: Micro enterprises are included in the small enterprises category for data on value added;
BLR: Individual entrepreneurs are included in the micro enterprises category;
GEO: Data on the number of enterprises refer to 2017, data for employment and value added refer to 2018;
MDA: Data for the number of enterprises and employment refer to 2018, data on value added refer to 2017;
Data on employment refer to number of employees for all the countries except for Ukraine, where data refer to number of employed persons.
Source: National statistical offices.

Stronger level-playing field is needed to unleash the potential of SMEs

The operational environment for SMEs has improved significantly…

Developing sound business conditions that allow SMEs to thrive is critical to promoting diversification in EaP countries. This requires creating business-friendly regulations, a robust strategic framework, effective and well-co-ordinated support institutions, and effective public-private dialogue.

All EaP countries have recognised the importance of reducing regulatory barriers and improving the business environment for SMEs. Georgia remains one of the world's top ten performers in the World Bank's *Doing Business* report (ranking 7th in 2020) (World Bank, 2019b[13]). While the other EaP countries are lower-ranked, they have shown substantial improvement since 2016 and several are among the fastest-improving countries in the ranking. Azerbaijan has raced upwards from 80th in 2014 to 25th in 2019. Belarus, Armenia and Moldova ranked 37th, 41st and 47th, respectively, in 2019; however, they still score poorly in the areas of paying taxes, getting credit and dealing with construction permits. Ukraine, despite significant improvements since 2014 (from 96th to 71st) still shows poor performance in the areas of getting electricity, protecting minority investors and resolving insolvency.

EaP countries have made continuous efforts to simplify business-related legislation, notably through guillotine-like programmes, the use of e-government services and the streamlining of barriers to trade or financial regulation and legal framework. Moreover, governments increasingly implemented targeted support mechanisms to enhance SMEs' access to finance, skills and innovation through instruments both financial (grants and tax incentives) and non-financial (training, business development services.

… but there is a need to make EaP economies more competition-friendly and to work on level-playing-field fundamentals

Despite formal improvements in the regulatory framework and institutions, the *de facto* practices of private actors and public authorities constitute strong barriers to SME growth. The momentum of key reforms and public support for business integrity, contract enforcement and competition should be strengthened in EaP countries.

First, the implementation of frameworks to prevent, detect and address corporate misconduct remains underdeveloped in EaP economies. Companies engaging in corrupt behaviours (e.g. bribery, favouritism in concluding contracts, money laundering) – whether by error, neglect or profit-driven risk-taking – undermine public and private efforts to do business according to the rules and erode trust in markets and institutions (OECD, 2015[14]).

Second, the cumbersome procedures required to enforce contracts, the lack of competent courts, and the long and costly resolutions of contractual disputes continue to hamper commercial practices. Effective institutional contract enforcement and the availability of alternative dispute settlement processes would enhance predictability in business operations and reduce uncertainty by assuring investors that their contractual rights will be upheld promptly and at reasonable cost (OECD, 2011[15]).

A third and prominent issue for SMEs is the competitive distortion that might result from the predominance of state ownership in the real economy. While the rationale for state ownership comprises a wide range of economic, social, political and strategic purposes, specific attention should be given to ensuring a level playing field and fair competition with privately owned businesses, as the anti-competitive conduct and dominant market power of state-owned enterprises (SOEs) can block market entry and expansion and facilitate cartels (OECD, 2018[16]). State-owned enterprises typically account for substantial parts of the economy and employment in EaP countries – for instance, enterprises fully owned by (or partially owned but controlled by) the State accounted for around one third of value added and total employment in 2016 in Belarus (IMF, 2019a[4]), while in Moldova they constitute 32% of GDP[2] (World Bank, 2017[17]) and 13% of employment (Ioniţă, 2016[18]). Although SOEs tend to participate in national strategic activities and operate in the infrastructure sector, they may also operate in sectors where SMEs can compete efficiently, such as agriculture or industry.

To help EaP countries reflect on these fundamental building blocks of the business environment, this SBA assessment introduces an analysis of three new policy dimensions: competition, contract enforcement and business integrity. This addition should enrich the understanding of overall economic policy making in the countries, complement the focused assessment of SME-specific aspects with an analysis of the broader determinants of business performance, and provide an indication of suitable reform areas for building healthy, productive and competitive economies in the EaP region.

References

Belstat (2019), *Statistical Yearbook 2018*, National Statistical Committee of the Republic of Belarus, Minsk, http://www.belstat.gov.by/en/ofitsialnaya-statistika/publications/statistical-publications-data-books-bulletins/public_compilation/index_12543/. [5]

EBRD (2018), *Economic Forecasts (Regional Economic Prospects)*, http://www.ebrd.com/what-we-do/economic-research-and-data/data/forecasts-macro-data-transition-indicators.html. [8]

Eurostat (2020), *Data Explorer - Annual enterprise statistics by size class for special aggregates of activities (NACE Rev. 2) (database)*, https://appsso.eurostat.ec.europa.eu/nui/submitViewTableAction.do. [12]

IMF (2019c), *Coordinated Direct Investment Survey (CDIS) (database)*, https://data.imf.org/?sk=40313609-F037-48C1-84B1-E1F1CE54D6D5. [10]

IMF (2019a), *Republic of Belarus : 2018 Article IV Consultation-Press Release; Staff Report; and Statement by the Executive Director for Republic of Belarus*, International Monetary Fund, Publication Services, https://www.imf.org/en/Publications/CR/Issues/2019/01/18/Republic-of-Belarus-2018-Article-IV-Consultation-Press-Release-Staff-Report-and-Statement-by-46526. [4]

IMF (2019b), *World Economic Outlook*, International Monetary Fund, Publication Services, Washington DC, http://dx.doi.org/www.imf.org/en/Publications/WEO (accessed on December 2019). [7]

Ioniţă, V. (2016), *State owned enterprises and their role in the national economy*, IDIS Viitorul, Chișinău, http://www.viitorul.org/files/State%20owned%20enterprises%20and%20their%20role%20in%20national%20economy.pdf. [18]

ITC (2019), *Trade Map - Trade statistics for international business development (database)*, http://www.trademap.org/Index.aspx. [2]

OECD (2019), *OECD SME and Entrepreneurship Outlook 2019*, OECD Publishing, Paris, https://dx.doi.org/10.1787/34907e9c-en. [11]

OECD (2018), *Ownership and Governance of State-Owned Enterprises: A Compendium of National Practices*, OECD Publishing, Paris, http://www.oecd.org/corporate/ca/Ownership-and-Governance-of-State-Owned-Enterprises-A-Compendium-of-National-Practices.pdf. [16]

OECD (2015), *Corporate Governance and Business Integrity: A Stocktaking of Corporate Practices*, OECD Publishing, Paris, http://www.oecd.org/daf/ca/Corporate-Governance-Business-Integrity-2015.pdf. [14]

OECD (2011), “Chapter 1. Investment Policy”, in *Policy Framework for Investment User’s Toolkit*, OECD Publishing, Paris, http://www.oecd.org/investment/toolkit/policyareas/investmentpolicy/41246110.pdf. [15]

United Nations (2019), *UN Comtrade | International Trade Statistics Database (database)*, http://comtrade.un.org/. [6]

United Nations (2019), *UNCTADstat (database)*, https://unctadstat.unctad.org/EN/. [9]

World Bank (2019), *World Development Indicators (database)*, World Bank, https://databank.worldbank.org/source/world-development-indicators (accessed on 4 December 2019). [1]

World Bank (2017), *The Republic of Moldova: Support to State-Owned Enterprises (SOE) Preminiary Diagnostics and Reform Assessment: Phase 1*, International Bank for Reconstruction and Development / The World Bank, Washington DC, http://siteresources.worldbank.org/EXTCENFINREPREF/Resources/Moldova_SOE_Diagnostics_EN.pdf. [17]

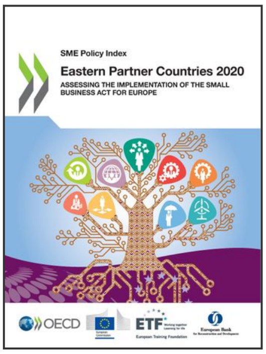
World Bank (2019b), *Doing Business Report 2020*, World Bank, Washington, DC, http://www.doingbusiness.org/en/doingbusiness. [13]

World Bank (2019c), *Migration and Remittances Data - Bilateral Remittances Matrices*, http://www.worldbank.org/en/topic/migrationremittancesdiasporaissues/brief/migration-remittances-data. [3]

Notes

[1] The economic rent of a natural resource equals the value of capital services flows rendered by the natural resources, or their share in the gross operating surplus; its value is given by the value of extraction. Resource rent may be divided between depletion and return to natural capital. https://stats.oecd.org/glossary/detail.asp?ID=2332.

2 This assets-to-GDP ratio is calculated on the basis of Ministry of Finance reports and GDP data for 2015.



From:

SME Policy Index: Eastern Partner Countries 2020

Assessing the Implementation of the Small Business Act for Europe

Access the complete publication at:

https://doi.org/10.1787/8b45614b-en

Please cite this chapter as:

OECD*, et al.* (2020), "Economic context", in *SME Policy Index: Eastern Partner Countries 2020: Assessing the Implementation of the Small Business Act for Europe*, OECD Publishing, Paris/European Union, Brussels.

DOI: https://doi.org/10.1787/8597c13a-en