

3. The business environment for SMEs and entrepreneurship in the Slovak Republic

This chapter describes the strengths and weaknesses of the business environment for SMEs and entrepreneurs in the Slovak Republic. It first considers macroeconomic conditions in the Slovak Republic, and then provides a description of the regulatory environment, followed by the innovation system. This chapter also describes education and skills that are relevant for SMEs and entrepreneurship, and investigates issues related to infrastructure policy, as well as the tax system for SMEs and the access to finance environment. The chapter also describes the environment for foreign direct investment and trade. It concludes with policy recommendations related to the business environment.

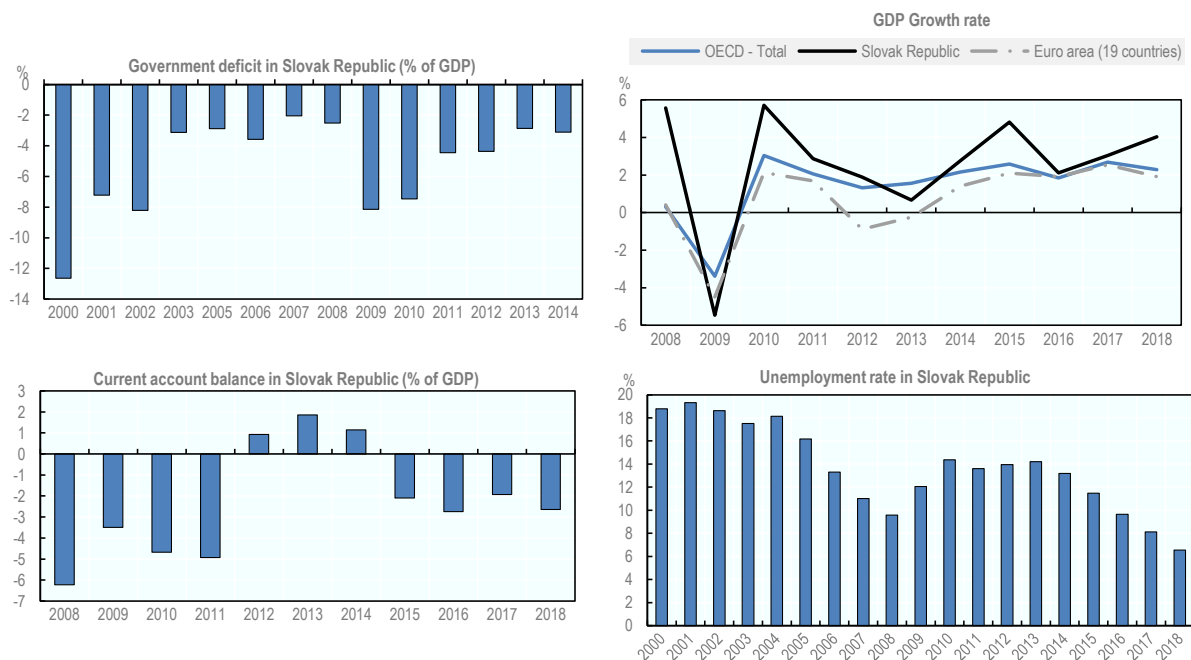
Macro-economic conditions

Pre-COVID-19 macroeconomic conditions were favourable to SME growth

Macroeconomic conditions during the pre-COVID-19 period were broadly favourable to SME and entrepreneurship development. GDP growth in the Slovak Republic stood at 4% in 2018 and had been positive since 2009, with average yearly growth rates of over 3%. Furthermore, GDP per capita increased by 80% over the two decades to 2018. The government deficit reached only 1% of GDP. The current account deficit was 2.6% of GDP in 2018 (Figure 3.1).

Unemployment stood at an all-time low in the history of the Slovak Republic going into the COVID-19 crisis, with an unemployment rate of 6.1% in 2019, which had steadily decreased since 2013 (Figure 3.1). However, low unemployment levels revealed significant skills shortages and skills mismatches in the labour market, with adverse impacts especially for SMEs, which are often unable to invest in workforce training or match the wage rates of their larger counterparts. One possible remedy is to attract Slovak emigrants. Almost 10% of Slovaks lived abroad in 2016, twice the average share across OECD countries (OECD, 2019a).

Figure 3.1. Macroeconomic conditions in the Slovak Republic



Source: OECD (2020) National Accounts database; OECD (2020), Balance of Payments databa; and OECD (2020), Employment database

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COVID-19 represented a big shock to the Slovak economy

The economic impact of the COVID-19 pandemic has been severe with GDP shrinking by some 6.3% in 2020, despite forceful public measures to contain the spread of the virus and mitigate the damage done to the economy (see Box 3.1 for an overview of the most pertinent measures aimed towards SMEs and entrepreneurs). Recovery is anticipated, with recent OECD growth forecasts of 2.7% in 2021 and 4.3% in 2022.

Box 3.1. Measures to assist SMEs in the aftermath of the COVID-19 crisis

After declaring a state of emergency on 15 March 2020, the Slovak government adopted legislation to defer income taxes on 18 March. The government announced a further set of measures to help companies and the self-employed on 29 March. The measures include;

- The state will pay 80 percent of the employee's salary in companies that have had to close during the pandemic health crisis;
- State financial contributions will be made to the self-employed and employees in companies that recorded a drop in revenues. In April, the state will contribute EUR 180 per employee for salaries in companies whose revenues dropped by more than 20 percent. Companies with a more than 40-percent drop in revenues will receive EUR 300 per employee from the state. Those whose revenues dropped by 60 percent will receive EUR 420 per employee, and those with more than 80 percent drop will receive EUR 540;
- EUR 0.5 billion will be made available to guarantee bank loans to employers to be able to finance their businesses;
- Employees in quarantine and parents who are at home with their children will receive 55 percent of their gross salary from the state;
- The payment of payroll taxes will be delayed for firms whose revenues drop by more than 40 percent;
- The deadline for paying income tax advance payments for those with a revenue drop of more than 40 percent will be postponed. Entrepreneurs will start paying the advance payments as of October, and;
- Companies will be able to include loss carry back since 2014 if they have not yet used a loss carry back.

On 14 April, the government announced further measures, including the introduction of a short-time work scheme to support workers' pay at companies that have suspended operations or whose revenue has dropped. The state will pay up to 80% of wages of employees, but not more than EUR 880 per employee per month, to companies affected by the crisis.

On 28 April, the government approved the use of EUR 1.2 billion from unspent EU funds to compensate for the COVID-19 outbreak, EUR 330 million of which would be for small businesses.

In addition, the Act on Temporary Protection of Entrepreneurs became effective from June 2020 providing temporary protection from bankruptcies consisting of:

- Temporary protection for bankruptcy petitions for companies hit by the COVID-19 crisis;
- The possibility of postponing the obligation to file for bankruptcy;
- Suspension of executions started after 12 March 2020 (in the case of commitments arising from business activities);
- The impossibility of commencing the exercise of a lien belonging to the undertaking;
- Prohibition on offsetting related receivables;
- A ban on contracting by contractors for delays between 12 March and 12 May 2020 related to the spread of Covid-19 and non-threatening contractors;
- Extension of the time limits for enforceability by legal acts and for the exercise of the right against an entrepreneur under temporary protection;

- The possibility to give priority to liabilities related to the maintenance of the company's operations;
- Support for fresh capital financing.

The government has also introduced new temporary protection for entrepreneurs from the beginning of 2021 to create room for "informal" corporate restructuring, lowering the cost and duration of the procedure.

Source: OECD 2020b and written correspondence from experts from the Ministry of Justice

The regulatory environment

Frequent regulation changes increase the administrative burden on smaller firms

Slovak small firms spend on average 221 hours per year handling bureaucratic requirements, according to estimates by the Institute of Economic and Social Studies in the Slovak Republic. Furthermore, surveys by the Slovak Business Agency (SBA) show a large majority of business owners (86% in 2018) reporting that frequent changes and amendments to the legislation influence their functioning and future growth. Each year, Slovak entrepreneurs must keep track of approximately 50 amendments to the key 15 business laws. In 2018, there were nearly 500 regulation proposals, with one-third of them affecting the business environment (Table 3.1). Impact assessment procedures are frequently by-passed, and a commenting period, along with the introduction of an ex-post evaluation procedure could improve the quality of future regulatory proposals.

Table 3.1. Business environment regulation in 2018

	Frequency and size in 2018
Regulation proposals	499
Documents with impact on business environment	143
Documents with calculated costs for business	22 (15%)
Total costs for the business environment	EUR 216.2 million

Source: SBA (2019).

The Slovak Republic is well ranked across the OECD countries in the EU on engaging stakeholders in the regulatory management of primary laws and subordinate regulations (OECD, 2019b). The relatively good ranking comes from the introduction of a standardised procedure, which involves publishing all legislative drafts and their impact assessments on the governmental portal www.slov-lex.sk. There, the general public can submit written comments, and ministries are obliged to provide written feedback. The authorities have made significant efforts to involve businesses (and SMEs in particular) in early stage consultations (OECD, 2020). Although not always successful, it is an example of good practice among OECD countries.

The introduction of a regulatory impact assessment procedure (RIA) in 2008 aimed to improve the regulatory environment by requiring assessment of the impact of regulatory proposals. Under the procedure, the government should assess the estimated economic impacts on a wide range of economic actors, including government, business, environment, and competition authorities in the country. However, the process still lacks proper implementation in practice. The ministries have few

incentives to comply with better regulation policies and regulatory proposals are often evaluated only once they are developed. In addition, only 15% of the regulation proposals in 2018 included estimated cost on businesses (Table 3.1).

In 2018, the government of the Slovak Republic adopted the Better Regulation Strategy (RIA 2020) Act, which aims to improve the quality of laws, eliminate redundant regulation, improve the process of introducing and reviewing regulations, and decrease bureaucratic complexity by eliminating a regulation with each new regulation (one-in-one-out method) (SBA, 2019). The outcomes of the measures will depend on the implementation and adoption of the targets proposed by this strategy. The Slovak Republic founded the Better Regulation Centre in 2015 as a further effort to reduce the disproportionate regulatory burden on businesses and improve the overall business environment. As a stand-alone unit within the SBA, the Regulation Centre builds on the EU Small Business Act for Europe initiative.

The implementation of the Better Regulation Strategy crucially hinges on the administrative and analytical capacity of key ministries and government bodies, including from the subnational level. This could be achieved by streamlining and centralising oversight and providing training to improve regulatory management practices (OECD, 2020c).

The Slovak Republic lags behind in ex-post evaluation of regulations (OECD, 2019b). Proper assessment of outcomes after implementation of regulations on different types of firms and other economic actors would help policy makers understand the behaviour and size of the impact over time, evaluate what works, and generate rigorous and better-tailored regulations in the future.

Gold-plating increases administrative burden

Gold-plating refers to the incorporation of costly and unnecessary rules and regulatory obligations above the requirements of the European Structural and Investment Funds (ESIF) or EU regulations. High administrative burden can then result in lower attractiveness of the ESIF funds, discouraging potential applicants, and raise costs for firms. In practice, it can be difficult to differentiate gold-plating from bureaucracy that originates in existing structures and gold-plating can be involuntary (Böhme et al., 2017). Often, countries might choose to interpret the regulatory framework more narrowly to protect themselves from a possible misunderstanding of the regulations.

In a government assessment, almost in one-third of evaluated directives (120 out of 400) the Slovak legislation introduced additional regulatory measures on the top of EU requirements. Most of the additions concerned more ambitious and progressive regulatory attempts, but in 30 of the cases, the increased requirements were unfounded (Ministry of Economy of Slovak Republic, 2019).

In another example of gold-plating prevalence in the Slovak Republic, anti-fraud investigations by the European Anti-Fraud Office (OLAF) detected that the financial impact of irregularities during the 2014-2018 period in EU countries related to EU ESIF expenditures was by far the highest in the Slovak Republic, concerning nearly 20% of all EU funds (Table 3.2). Irregularity refers to any infringement of a provision of Community law coming from an act or omission and is reported by national authorities in the Member States that oversee the ESIF Operational Programmes to be then investigated by the OLAF.

Table 3.2. Irregularities in the European Structural and Investment Funds and their financial impact

Number of irregularities and their financial impact, 2014-2018.

Member State	Member States		OLAF	
	Detected fraudulent and non-fraudulent irregularities	Financial impact as % of payments	Investigations closed with recommendations	Financial recommendations as % of payments
Spain	10995	3.31	7	0.43
Romania	5563	3.23	66	0.4
Poland	5103	1.89	22	0.12
Italy	4117	1.33	21	0.35
Hungary	2886	1.31	52	3.84
Portugal	2723	2.04	10	0.42
Czechia	2665	2.86	7	0.06
United Kingdom	2596	0.57	6	0.05
Greece	2206	2.5	17	0.31
Slovakia	1649	19.29	14	2.29
Germany	1567	0.31	4	0.37
France	1291	0.3	10	0.1
Ireland	1120	1.88	0	0
Lithuania	1110	2.05	3	0.11
Bulgaria	1072	1.92	27	0.42
Netherlands	777	0.79	4	0.04
Latvia	517	2.36	1	0.01
Estonia	412	1.58	0	0
Austria	370	0.37	2	0.02
Belgium	315	0.46	1	0.02
Slovenia	261	1.59	1	0.14
Croatia	189	0.95	2	0.34
Sweden	175	0.2	0	0
Finland	155	0.12	0	0
Denmark	144	0.27	0	0
Malta	91	2.53	0	0
Cyprus	82	0.74	0	0
Luxembourg	2	0.02	0	0
Total	50153	2.01	277	0.45

Source: European Anti-Fraud Office (2018), https://ec.europa.eu/anti-fraud/about-us/reports/olaf-report_en.***Improvements can be made in administrative procedures to start a business***

The Slovak Republic ranked 45th among 190 economies in the World Bank's "Ease of Doing Business" index in 2020. Despite its score improving, the Slovak Republic fell from its 42nd position in 2019, failing to progress in business regulation reforms as fast as some other countries.

Among individual indicators making up the overall score, the Slovak Republic ranked among the top ten countries for ease of administration on trading across borders (1st) and registering property (8th place). One of the most problematic areas of business regulations concerns starting a business (118th place) (Table 3.3). The Slovak Republic requires 7 procedures for new business start-up as compared to an average of 4.9 in OECD high income countries, while the process lasts over 21 days, as compared

to 9 days across the OECD (World Bank Group, 2020). The Slovak Republic's performance remains weak in this area despite some recent reforms, such as abolishment of the requirement to obtain and submit information on tax arrears in 2019, which speeds up the business registration process.

Table 3.3. Easy of Doing Business in the Slovak Republic

Ranking and scores for business regulations and their enforcement in 2020

Topics	DB 2020 Rank	DB 2020 Score	DB 2019 Score
Overall	45	75.6	75.4
Starting a Business	118	84.8	82.0
Dealing with Construction Permits	146	59.4	59.3
Getting Electricity	54	83.3	83.2
Registering Property	8	90.2	90.2
Getting Credit	48	70.0	70.0
Protecting Minority Investors	88	56.0	56.0
Paying Taxes	55	80.6	80.6
Trading across Borders	1	100	100
Enforcing Contracts	46	66.1	66.1
Resolving Insolvency	46	65.5	66.9

Source: World Bank Group (2020).

Insolvency procedures are costly in terms of time and money, disincentivising second chance entrepreneurship

Business failure is increasingly seen as offering learning a learning process on which entrepreneurs build their experience. Giving entrepreneurs a “second chance” quickly after they go bankrupt is therefore one of the principles of dynamic entrepreneurship policy. The insolvency procedures in the Slovak Republic are the longest in the EU, leaving ample space for policy initiatives that would facilitate early restructuring of SMEs in difficulties and improve the regulations affecting the re-start possibilities of entrepreneurs facing bankruptcy.

The Slovak Republic has one of the least favourable environments for resolving insolvency among EU countries and has seen only limited progress over the past ten years on second-chance entrepreneurship indicators (European Commission, 2019). For example, Slovak insolvency procedures can take up to 4 years, compared with an EU average of approximately 2 years. Furthermore, the cost of recovering the debt can amount to up to 18% of the value of the debtor's estate; the second highest value among the EU countries, where the average is 10%. Recent reforms have been made to the insolvency regime, as highlighted in box 3.1, and their impact on second chance entrepreneurship need to be closely monitored and readjusted if necessary.

The innovation system

Weak academic research performance and academic-business cooperation holds back innovation

The Slovak Republic is classed as a moderate innovator on the European Innovation Scoreboard, and its innovation system performance ranks among the tail end of EU countries on many measures (Table 3.4). There are some areas where the Slovak Republic performs relatively well, in particular on

“Sales impact” (with a high shares of technologically advanced and innovative products in total exports) and “Employment impacts” (with a high share of total employment in high growth enterprises). However, the Slovak Republic ranks well below the EU average values on a range of other innovation system performance measures, especially in terms of academic research performance, the involvement of public innovative activities with the private sector, and innovation within SMEs. Investments in R&D also lag behind. Currently, manufacturing, dominated by multinational firms, is the major source of R&D in the business sector, indicating a lack of diversification of innovative activities (European Commission, 2019b).

Table 3.4. Innovation performance in the Slovak Republic and the EU

	EU (28 countries)	Slovak Republic	EU	Slovak Republic
	Actual values		Values normalised to 2011 EU levels	
FRAMEWORK CONDITIONS				
Human resources				
New doctorate graduates	2.1	2.0	145.2	138.5
Population completed tertiary education	39.8	36.4	119.4	94.0
Lifelong learning	10.9	3.4	102.1	24.0
Attractive research systems				
International scientific co-publications	1070	648	145.4	84.1
Scientific publications among top 10% most cited	11.5	4.7	109.5	34.9
Foreign doctorate students	20.3	8.7	95.6	40.5
Innovation-friendly environment				
Broadband penetration	18.0	13.0	200.0	144.4
Opportunity-driven entrepreneurship	3.6	1.4	129.5	54.4
INVESTMENTS				
Finance and support				
R&D expenditure in the public sector	0.68	0.40	92.5	40.2
Venture capital investments	0.149	0.011	129.3	9.3
Firm investments				
R&D expenditure in the business sector	1.36	0.48	114.6	39.1
Non-R&D innovation expenditure	0.86	0.75	116.8	105.4
Enterprises providing ICT training	23.0	18.0	126.7	93.3
INNOVATION ACTIVITIES				
Innovators				
SMEs with product or process innovations	34.3	19.5	97.1	42.8
SMEs with marketing or organisational innovations	35.6	20.0	85.3	32.3
SMEs innovating in-house	28.1	16.8	90.0	38.4
Linkages				
Innovative SMEs collaborating with others	11.8	8.2	106.8	70.1
Public-private co-publications	81.7	28.5	117.3	38.4
Private co-funding of public R&D expenditures	0.05	0.02	96.0	62.2

Intellectual assets				
PCT patent applications	3.53	0.63	90.9	16.3
Trademark applications	7.85	4.43	111.4	66.6
Design applications	4.17	1.76	92.2	38.9
IMPACT				
Employment impacts				
Employment in knowledge-intensive activities	14.2	10.6	109.0	62.8
Employment fast-growing firms innovative sectors	5.2	7.3	101.2	149.8
Sales impacts				
Medium & high-tech product exports	56.3	67.3	107.9	138.7
Knowledge-intensive services exports	68.4	38.3	103.2	41.9
Sales of new-to-market and new-to-firm innovations	12.96	20.27	97.0	169.3

Note: Normalised values related to an EU average in 2011 normalised to 100.

Source: EU (2019), European Innovation Scoreboard 2019 dataset, <https://data.europa.eu/euodp/en/data/dataset/european-innovation-scoreboard-2019>.

In particular, low R&D spending and weak business engagement with higher education institutions (HEIs) are holding back the commercialisation of research in start-ups and knowledge transfer to SMEs. Despite programmes dedicated to incentivise innovation spending and create linkages between HEIs and businesses, such as the Ministry of Economy's innovation vouchers programme, current programme funding levels are limited. In addition, SMEs often find it difficult to apply for such support.

Innovation and R&D policies are fragmented and are not well implemented

Public action on innovation in the Slovak Republic is guided by the country's Smart Specialisation Strategy. The first Smart Specialisation Strategy covered the 2014-20 period, and is now in the process of renewal for 2021-2027. The 2014-20 Strategy focused on four key areas of economic specialisation: (1) Automotive and mechanical engineering industries; (2) Consumer electronics and electrical equipment; (3) Information and communication technologies and services, and (4) Production and processing of iron and steel. It also sought to introduce the following key innovation policy reforms: (1) Merge eight R&D&I government agencies into two, (2) Reverse shares of support to basic and applied research to 1:2 by 2020, (3) introduce a mandatory indicator of state support to R&D as a share of GDP in the State Budget Law, and (4) re-organise HEIs and transform the Slovak Academy of Sciences. However, despite being among the first EU member states to develop its smart specialisation strategy, administrative delays have postponed its implementation, and the allocated budget has been only partially spent and there has been little demonstrable impact on overall change in innovation system performance (Balaz, Frank and Ojala, 2018). These issues need to be addressed in the implementation of the 2021-2027 strategy.

In addition, the innovation policy support landscape is fragmented across different government Ministries and agencies. The Ministry of Economy has multiple mechanisms in place to spur innovation, including financial support of innovative projects, innovation vouchers to develop cooperation between firms and universities and research institutes, industrial cluster support, and start-up visa support that grants temporary residence permits to those foreign entrepreneurs who intend to develop an innovative product on the Slovak market. The need to improve coordination is exemplified by the competition (rather than cooperation) among different public bodies to access EU structural and investment funds. In somewhat similar fashion, the government collaborates with a large number of research entities in

the country, which leads to a dilution of limited resources. Public-private cooperation would benefit from the establishment of wider research units spanning different universities (OECD, 2019a).

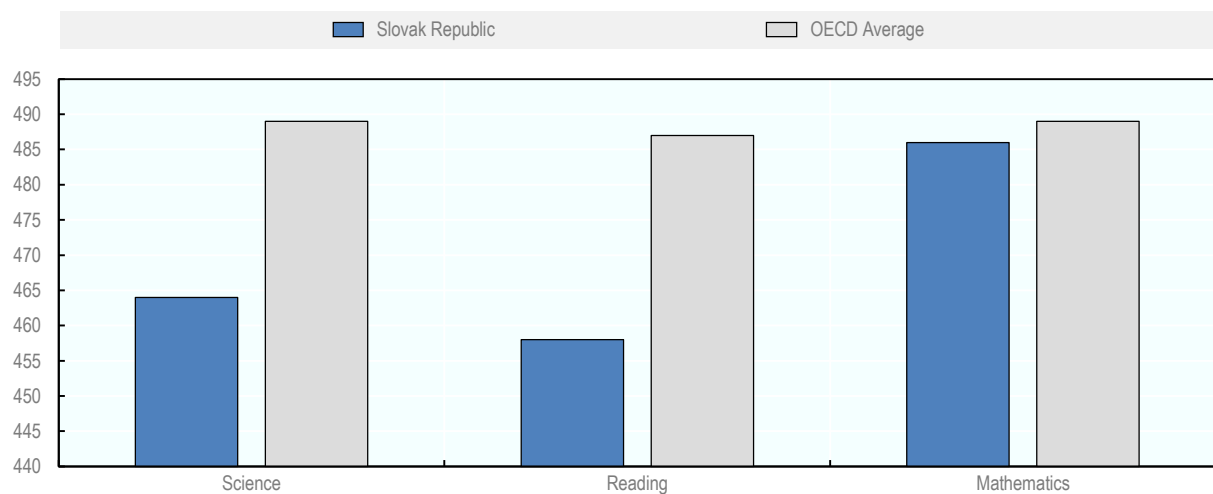
Educational attainment and skills

Slovak pupils score below the OECD average in science and reading

Slovak 15-year olds lag behind the OECD average in their competences in science, reading and mathematics, as measured by the OECD programme for international student assessment (PISA), and the gap is especially high in science and reading (Figure 3.2). The Slovak Republic displayed the largest deficit with respect to the OECD average in reading scores, only ahead of Greece and the OECD countries in Latin America in 2018.

Figure 3.2. Performance of 15-year olds in science, reading, and mathematics

Mean PISA score in each subject in 2018.



Source: OECD (2021c), Science, Reading, and Mathematics performance (PISA) (indicator). doi: 10.1787/91952204-en

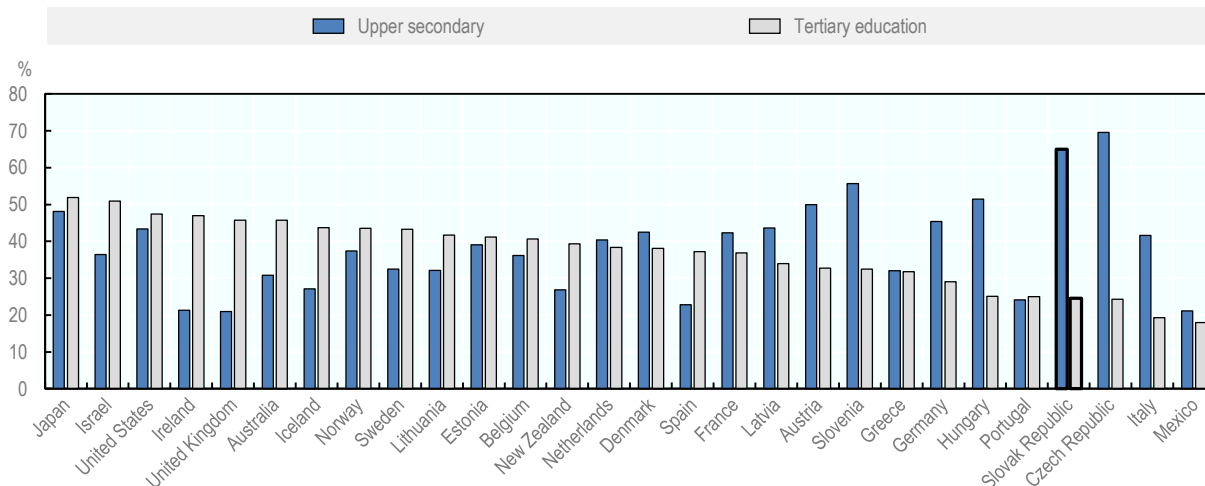
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The Slovak Republic has a low share of the workforce with a university education

Only approximately one-quarter of adults in the Slovak Republic have a university degree, compared to about 37% across the OECD countries (Figure 3.3). On the other hand, the younger generations are closer to the OECD average.

Figure 3.3. Educational attainment of adults

Percentage of 25-64 year olds by educational attainment in 2018.



Source: OECD (2020d), Education at Glance database.

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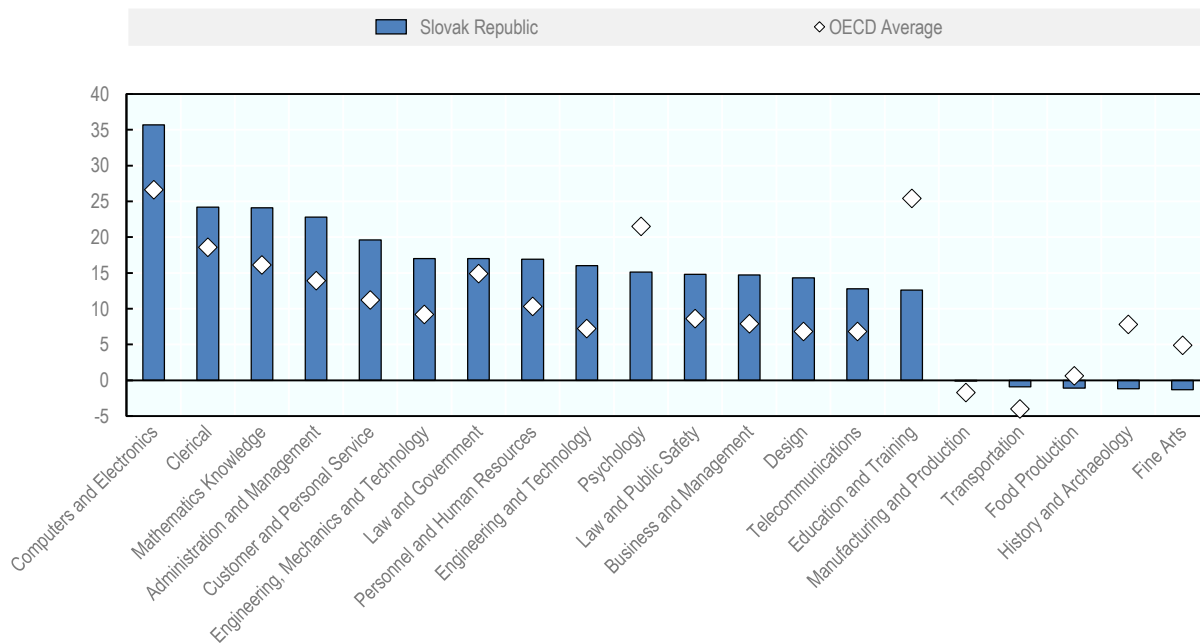
The relatively low skill levels are associated with a relatively high risk of job loss through automation. More than 60% of jobs in the Slovak Republic can be considered as being at risk of being automated, the highest share among the OECD countries (Nedelkoska and Quintini, 2018). The Slovak Republic has built its economic success in part on automobile and electronic industries, and these will likely undergo automation of large parts of the production process, reducing employment of the less-skilled workforce. Upgrading skills that can be used across a variety of tasks and jobs, promoting flexibility, teaching soft skills, and investing in increasing managerial capability will help prepare the workforce for the future automation challenges and build additional strength in diversifying the labour market.

Many sectors face significant skill shortages, especially in ICT and electronics

The Slovak labour market suffers from skills shortages in specific areas, which will affect SME development. In particular, Slovak skills shortages in computer sciences and electronics are greater than the OECD average. Technical knowledge in other areas is in short supply as well: the Slovak job market needs more employees with knowledge and expertise in mathematics, but also engineering, mechanics, and technology, as well as employees with clerical, administrative and management knowledge (Figure 3.4). A shift towards science-based study programmes, and especially training in computer sciences, and business administration programmes could help to cover the shortages and prepare the Slovak Republic for future labour market needs. The skills shortages could also be addressed, at least to some extent, by retaining talent in the country and attracting back the emigrated workforce and attracting in foreign talent.

Figure 3.4. Skills shortages and surpluses in the Slovak Republic and the OECD

Score of shortage or surplus by knowledge area, 2015.



Note: Only the first 15 highest skill shortages and 5 highest skill surpluses in the Slovak Republic are displayed out of a total of 39 categories. Positive values indicate skill shortage while negative values point to skill surplus. The larger the absolute value, the larger the imbalance. Results are presented on a scale that ranges between -100 and +100. The maximum value reflects the strongest shortage observed across OECD (31) countries and skills dimensions.

Source: OECD (2017a), Labour: Skills for Jobs dataset.

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SMEs also suffer from gaps in the availability of soft skills, in particular in oral and written comprehension. Many employees have insufficient verbal abilities, oral expression, and deductive reasoning skills. This holds especially true in the information and communication sector, professional, scientific and technical activities sector, and administrative and support service activities, but is less of a problem in the manufacturing sector (Table 3.5).

Table 3.5. Missing skills in the largest SME sectors in the Slovak Republic

Score of skill shortage (positive) or surplus (negative) in 2015.

Skills	Wholesale and Retail Trade	Manufacturing	Construction	Prof., Scientific and Tech. Activities	Admin. and Support Service Activities	Transportation and Storage	Accommodation and Food	Information and Communication
Oral Comprehension	4.2	-1.7	2.6	10.3	7.4	4.9	9.9	23.0
Written Comprehension	3.8	-0.9	2.8	9.7	6.9	4.4	7.7	22.5
Verbal Abilities	3.9	-1.0	2.8	9.7	7.1	4.5	8.6	21.3
Oral Expression	4.1	-1.4	2.7	9.9	7.0	4.7	10.0	21.4
Deductive Reasoning	3.6	-1.0	2.6	8.9	7.5	4.2	7.7	21.2
Written Expression	3.5	0.2	3.0	8.7	7.1	3.9	6.7	18.4
Inductive Reasoning	3.2	-1.1	2.4	8.1	7.4	3.9	6.7	19.4
Reasoning Abilities	3.1	-1.0	2.2	7.6	5.7	3.6	6.9	18.2
Information Ordering	3.2	-1.8	2.1	7.8	4.7	3.9	7.3	19.9
Near Vision	3.5	-3.0	1.8	8.3	4.6	4.3	7.9	19.4
Speech Recognition	3.3	-1.3	1.7	7.7	5.2	3.7	8.3	16.0
Cognitive Abilities	2.7	-1.0	1.9	6.6	5.3	3.2	6.0	15.3
Quantitative Abilities	2.4	0.2	1.8	6.1	3.0	2.7	4.4	14.3
Flexibility of Closure	2.2	-1.7	1.7	5.5	6.4	2.8	5.0	13.3
Attentiveness	2.2	-1.6	1.1	5.0	5.6	2.9	5.7	11.6

Note: The sectors displayed are the largest in terms of employment in SMEs. Positive values indicate skill shortage while negative values point to skill surplus. The larger the absolute value, the larger the imbalance. Results are presented on a scale that ranges between -100 and +100. The maximum value reflects the strongest shortage observed across OECD (31) countries and skills dimensions.

Source: OECD (2017a), Labour: Skills for Jobs dataset.

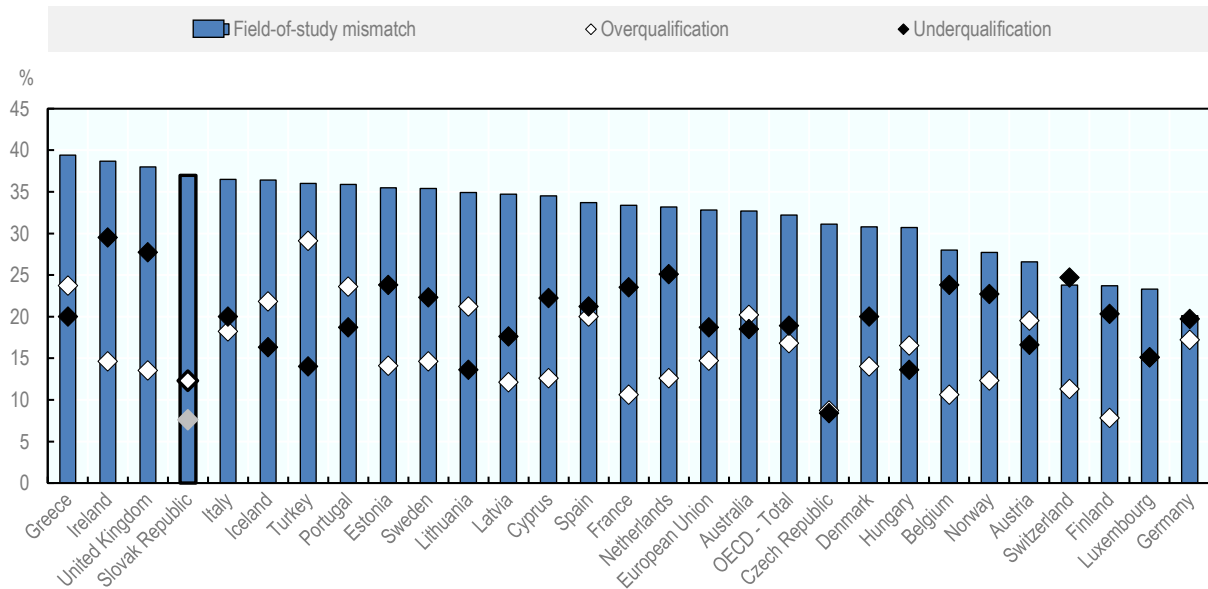
Graduates in the Slovak Republic are less likely to find job in the field of their studies

There appears to be a mismatch between skills produced through the education system and labour market needs. In 2016, 37% of adults worked in fields different from their educational qualification (Figure 3.5). On the other hand, only 8% of adults worked in positions for which they were underqualified, and only 12% were overqualified, both among the lowest qualification level mismatches in the OECD area. This suggests a need for more and better university study programmes in areas including business administration, IT, communication and engineering, as well as greater offers of specialised courses within existing study programmes.

Closer cooperation between universities and the private sector could help achieve a better match between university skills output and labour market needs. Business inputs could help align curricula to business needs. In addition, internship programmes for university students in enterprises are relatively uncommon and in practice largely reserved for larger enterprises. More internships in SMEs would give the opportunity to students to get practical experience and create connections with employers before graduation.

Figure 3.5. Mismatch between skills and employment, Slovak Republic

As a share of workforce in 2016

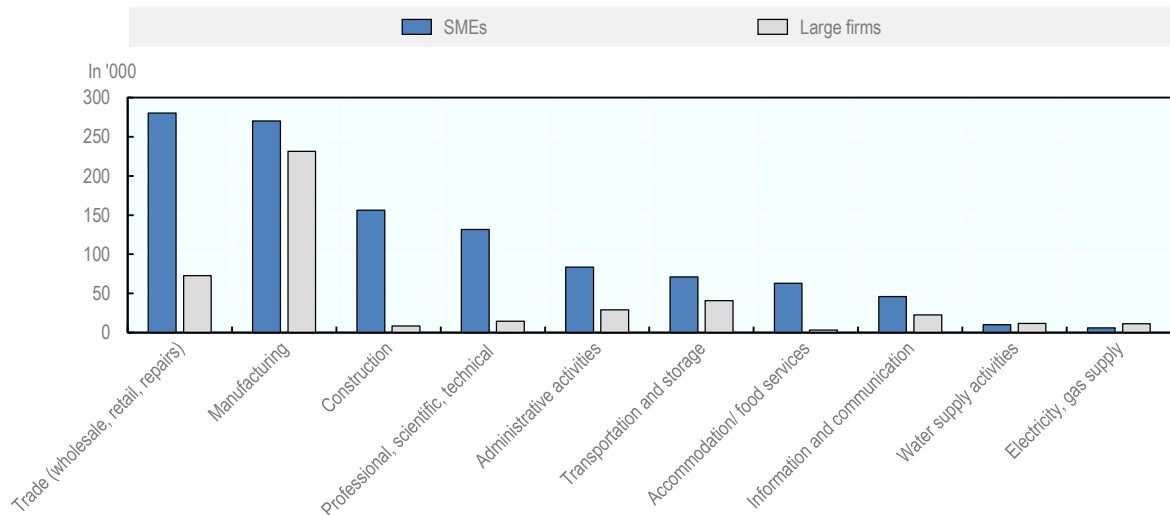


Source: OECD (2017a), Labour: Skills for Jobs database

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Figure 3.6. Fields of study in tertiary education in the Slovak Republic and OECD

Share of 25-34 year-olds by field of study in 2018



Source: OECD (2020d), Education at a Glance database.

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Several countries have a dedicated body to keep track of the supply and demand of skills in the (regional) labour market, such as skills councils. These bodies can be helpful in minimising the skills mismatch. Australia's Industry and Skills Committee is an example (Box 3.2). A skills council at a

national level in the Slovak Republic could help build cooperation between the government, trade unions and entrepreneurs and expand their engagement in skills policies. It could serve as a platform to understand the future skill needs and construct a coordinated and possibly cross-sector approach to vocational education and training. Its possible establishment could build on the legislation introduced in 2018, Act on Quality Assurance in Higher Education, which brings employers, graduates and research institutions together to review the content of study programmes (OECD, 2020e).

Box 3.2. Skill councils can reduce the skill mismatch: example from Australia

Skill councils or committees are employer-led organisations, often organised within specific industries or regions, which support employer participation in the implementation and direction of vocational education and training. Among the objectives of a skills council or committee are minimising skills shortages and supporting productivity growth.

Description of the approach

The Australian Industry and Skills Committee (AISC), composed of nominated industry leaders, ensures that the training system responds to the needs of industry in a timely fashion. The Committee relies on specific Industry Reference Committees in communicating industry skills requirements and supporting the development and review of training packages. Currently, the AISC operates through eight cross-sector projects to address common skills needs and optimise efforts of individual industries.

The AISC's mission is to reduce complexity in the vocational education and training (VET) system, improve mobility through recognition of qualifications between occupations and address the issue of low enrolments in some courses. In addition, the Committee coordinates the development of new training products that would help trainees to acquire new or emerging skills needed by industries. The AISC also creates space for different industries to exchange on the issues of opportunities that new technologies bring and consider the implications of technology change for new competency requirements for their sectors. They also generate case studies about good practices in the VET system that can then serve as a dissemination tool on good practices.

The eight cross-sector projects are as follows:

- **Automation and Digital Skills:** VET's role in responding to digital change across industry and its impact on the workforce;
- **Big data:** development of training in Big Data as a cross-sectoral skill in capturing, interpreting and taking advantage of data that are too large to process through traditional database and software methods;
- **Cybersecurity:** development of skills in cyber security where professionals in different industries can cope with advanced threat response, risk management and other emerging cyber challenges;
- **Supply chains:** development of skills and competencies sets for industry employees in order to support mobility across industries, increasing efficiency and productivity across diverse industries;
- **Environmental sustainability:** adjustments to VET programmes to ensure that the workforce is equipped with skills focused on environmental sustainability;
- **Teamwork and communication:** generating skills in teamwork and communication among the workforce across industries;
- **Inclusion of people with disability:** addressing poorer education and employment outcomes for people with disability through VET;

- **Consumer engagement through social media:** identifying, updating and developing training packages to ensure the provision of skills for a wide range of industries for consumer engagement through online and social media.

Relevance to the Slovak Republic

A functioning skills council in the Slovak Republic would serve as a communication tool between industry and ministries developing skills policies and would provide timely requests, suggestions, and cooperation to influence the direction of vocational training. It would serve as an opportunity for the direct participation of entrepreneurs in the discussion on skill needs. Skill councils should have representation from enterprises of all sizes, including small firms.

The skills council could function in such way that it would consider current needs and give advice for designing and reshaping vocational training for each industry, but should also take into future skill needs, similar to the AISC's approach. This would allow for intra-industry skill creation, greater flexibility of the labour force and possibly foster closer cooperation and linkages between sectors.

Source: (Australian Industry and Skills Committee, 2020)

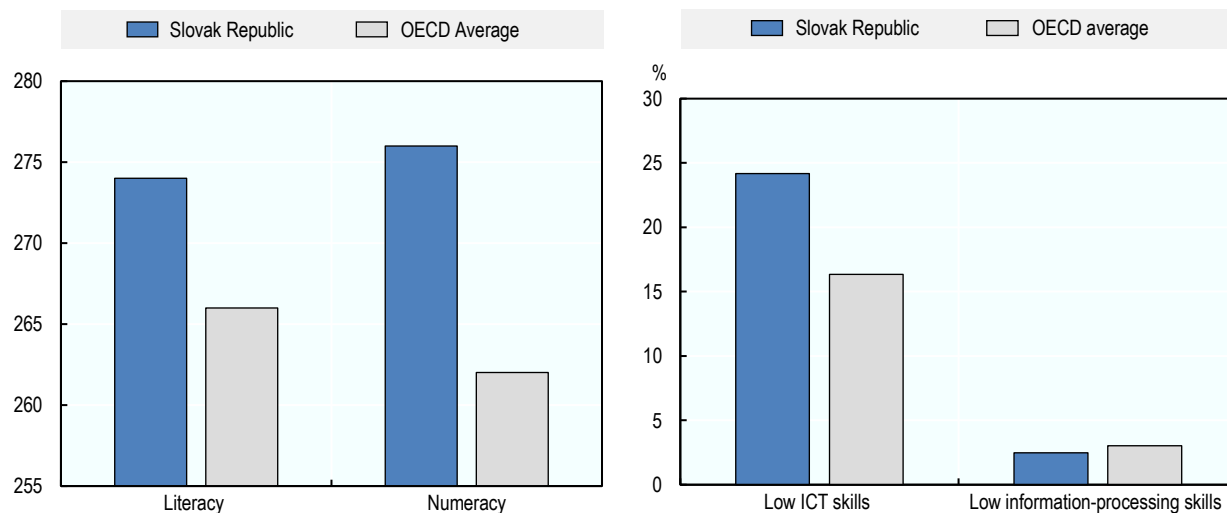
The Slovak Republic operates a dual education system based on the template of the vocational education systems in Austria, Germany, and Switzerland. It functions on the principle of closer cooperation between employers and vocational schools, with the goal of combining theoretical and practical education and enabling young people to acquire skills that match employer needs. In 2018, 490 employers and 85 vocational schools were participating in the system of dual education, but only about 200 employers participated actively (SBA, 2018). The Act on Vocational Education and Training, adopted in 2015, aims to increase the motivation of entrepreneurs to participate and have a voice in the training system. This should support the coordination of vocational training in line with labour market needs and increase the employability of VET graduates. Tax incentives aim to stimulate employer participation in the programme. However, as the SBA concluded in a study in 2018, employers often remain reluctant to participate in the dual education system. The firms cite financial, personnel-related, administrative difficulties that prevent them from entering (SBA, 2018).

Compared to other OECD countries, adults are less likely to participate in education

In contrast to the relatively weak competence levels of Slovak 15-year olds, adults score above the international averages on literacy and numeracy in the OECD Programme for the International Assessment of Adult Competencies (PIAAC) (Figure 3.7). Slovak adults perform particularly well in numeracy skills, with fewer adults falling in the lowest level of the numeracy test than the OECD average, and 12.6% scoring in the highest level (level 4 or 5) compared to a 10.9% across the OECD countries in 2018. The area where Slovak adults underperform compared to the OECD average is ICT skills. A quarter of Slovak adults have low ICT skills, 8 percentage points more than across the OECD, although most adults pass the information-processing skill test (Figure 3.8). This underlines the missing ICT knowledge demanded by SMEs, and could be improved by the provision of targeted adult training courses.

Figure 3.7. Adult skills

Scores in literacy and numeracy among adults and percentage of adults with low ICT skills, in 2018



Source: OECD (2018), Survey of Adult Skills (PIAAC).

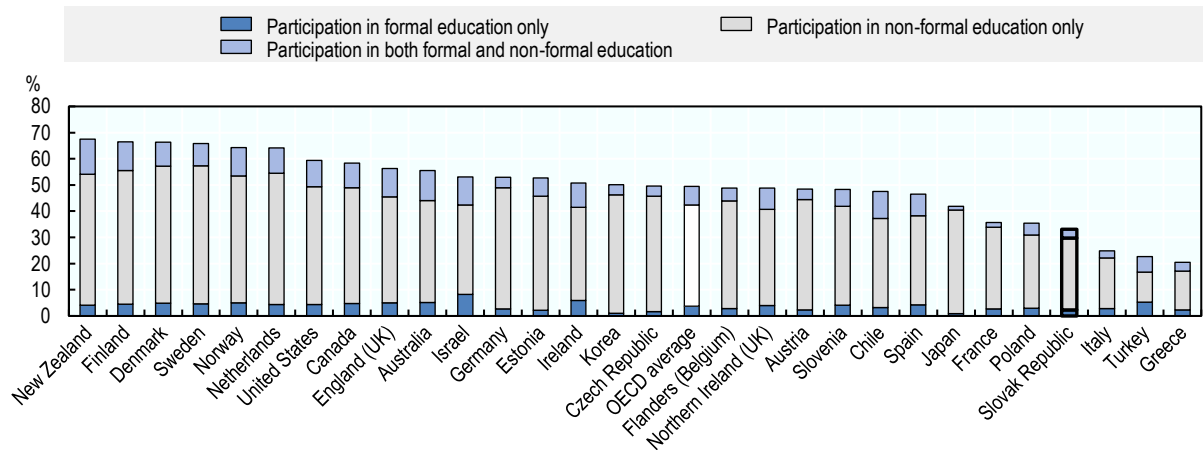
StatLink  <https://doi.org/10.1787/888934247647>

There is ample space for the government to improve the governance of adult learning, build a coherent long-term vision of adult learning, and make clear connections between goals and policies to create a well-functioning system of adult education. Despite an effort to define and establish a national life-long learning strategy, such as the Lifelong Learning Strategy initiative introduced in 2011, many support mechanisms do not exist or are not fully implemented. Achieving the goals formulated by the strategy requires strengthening the governance system and greater involvement of national government and ministries, as well as local administrations. Currently, general public also places limited importance to life-long learning and measures to raise awareness of the importance of lifelong learning and the opportunities for training among the population also need to be taken (OECD, 2020e).

About one-third of adults in the Slovak Republic continue their education, mostly in form of non-formal education, which is a relatively low proportion in an international context. Furthermore, those adults in the Slovak Republic who do engage in adult learning mostly follow foreign language courses and there are significant gaps in ICT training and training for soft skills such as management and customer relation skills.

Figure 3.8. Adult learning

Share of adults participating in education, 2012/2015



Note: The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

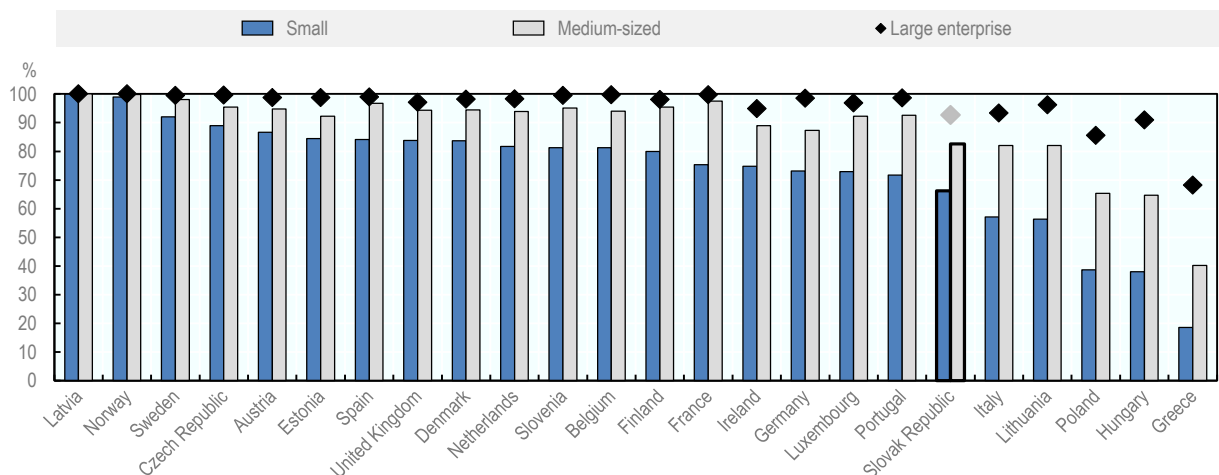
Source: OECD (2020e), Skill Strategy Slovak Republic.

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The most frequent reason reported by enterprises for not providing continuous training is that they do not have any (additional) skill needs (reported 82% of SMEs that do not provide any training) or because they hired new staff that matches the skill needed (reported by almost half of non-training firms in the Slovak Republic). One-third of enterprises not offering training report that the reason is their high workload and lack of time allocated to participate in training, followed by cost reasons. In the Slovak Republic, 30% of firms have no time for staff to participate, and 31% cite high cost of training courses.

Figure 3.9. Enterprises providing continuous vocational training

Share of firms by size class in 2015



Source: Eurostat (2020), Education and Training in the EU database

StatLink  <https://doi.org/10.1787/888934247685>

Vocational training is not well developed in the Slovak Republic. SMEs might not be fully aware of the importance of training and upgrading skills and competencies that help to improve productivity and adaptability to changing environment. Two-thirds of small firms in the Slovak Republic provided training in 2015, in contrast with 75% in the OECD. A higher share of medium-sized firms train their workforce in the Slovak Republic; 83% as compared to 88% across OECD countries (Figure 3.9). In addition to a lower occurrence of training, the intensity of training is lower. Employees in Slovak small firms spent about 4 hours in CVT courses per 1 000 hours worked, whereas in medium-sized firms the training intensity was about 5.5 hours per 1 000 hours worked. This contrasts with countries such as Ireland, where 13 hours in small and 10 hours in medium-sized firms are dedicated to training. The Slovak Republic performs better, however, than countries such as Greece or Hungary where SMEs dedicate only up to 0.2% of worktime to training (or less than 2 hours per each 1 000 hours) (Eurostat, 2020).

Entrepreneurship education receives only marginal attention in the educational system

The education system can contribute to developing entrepreneurial attitudes and entrepreneurial skills such as the ability to build teams, communication and motivation skills, mentoring and development, but also engagement in entrepreneurial activities. However, the formal education system in the Slovak Republic provides little entrepreneurship education and the country lacks a specific entrepreneurship education strategy, even if it addressed the topic extensively in the National Youth Strategy 2014-20. Non-profit educational organisations have tried to fill in the gap left by the formal curriculum. As an example, Junior Achievement Slovakia organises practical training programmes in schools to support entrepreneurial and economic thinking and support youth employment. In addition, both the Ministry of Economy and the SBA are planning to introduce schemes that would develop activities focused on improving entrepreneurial education (OECD, 2020d). Already in 2018, the SBA had about 30 projects to help create new business ideas and educate the general public on business-related topics.

Attracting Slovak migrants living abroad could bring back skills and support entrepreneurial activities

Returning migrants are a potential source of qualified workforce, networks and capital, which could contribute to entrepreneurship activity and help tackle the skill deficit. Close to one in ten Slovaks live abroad, one of the highest proportions among OECD countries (OECD, 2019a). Various diaspora programmes could increase cooperation with Slovak communities abroad, encourage return migration, exchange knowledge and promote networking. Other countries with large diaspora communities have often pursued policies in this area. For example, Lithuania organises labour market information fairs abroad, organises visits to scientific institutions to highly qualified researchers or facilitates return by offering services to returning migrants through a one-stop-shop portal.

In 2015, the Ministry of Education introduced a grant scheme for experienced professionals returning to the Slovak Republic, but this has been discontinued. LEAF, an NGO, runs the Slovak Professionals Abroad programme in the absence of government programmes at scale.

Infrastructure

Transport infrastructure investment is unevenly distributed across the territory

The Slovak share of GDP spent on total transport infrastructure investments exceeds most other OECD countries at about 1.2% in 2017 (OECD.stats). Since the 1990s, infrastructure investments have focused on developing high-speed motorways in the western and northern part of the country. This has

been important in development of industrial activity and attracting foreign investments in these regions. Indeed, research finds clear correlations between local economic indicators such as lower unemployment and transport investments in the districts (Habrman and Žúdel, 2017).

While infrastructure investment has focused on the motorways, the remaining road network has deteriorated for the past two decades and the transport infrastructure remains uneven or incomplete, contributing to significant disparities between regions, with the Eastern and Southern regions lagging behind. The perception of road infrastructure quality is among the lowest among OECD countries. Similarly, rail transport provides inadequate quality and is underused. An uptick in car ownership and use has led to decline in rail travel, and fewer resources for maintenance and upgrade are dedicated to rail infrastructure (OECD, 2019a).

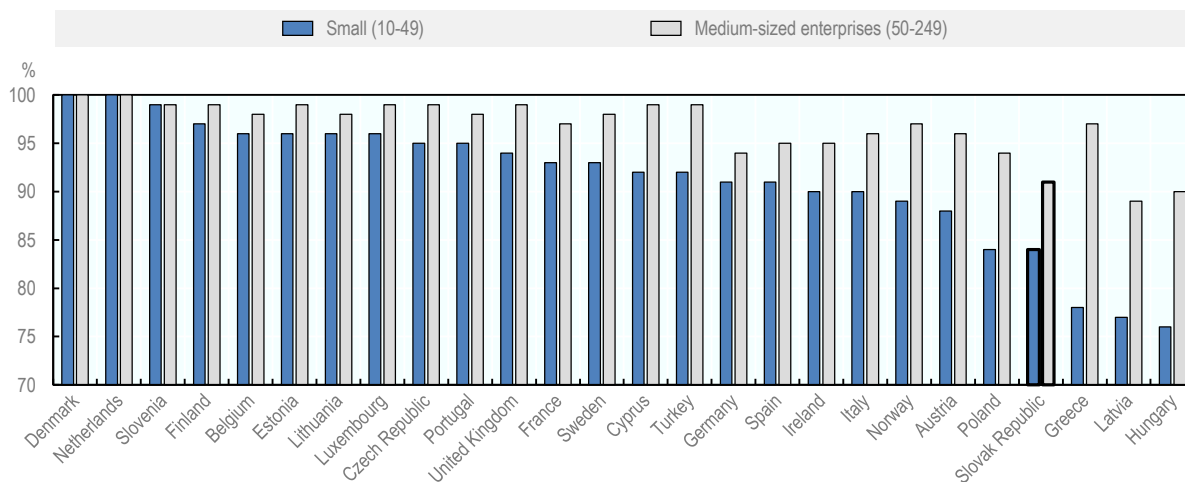
Broadband connectivity among SMEs is low, and few small firms use a fast connection

Digital infrastructure, along with human capital and a supportive regulatory framework, is one of the necessary drivers for digital transformation, as set out in the digital strategy of the Slovak Government for 2019-30. However, the Slovak Republic has one of the lowest levels of investments in ICT as a share of GDP in EU countries. Over time, insufficient investments lead to lagging availability and speed of broadband connections. In 2019, 84% of small firms and 91% of medium-sized firms used a digital subscriber line (DSL) or other fixed broadband connection, as compared to 91% for small firms and 97% of medium-sized firms across European countries as a whole (Eurostat). In addition, the share of SMEs with a broadband connection has stagnated in recent years.

Only a small share of SMEs use a fast internet connection: 13% of small firms and 17% of medium-sized firms had a connection with a download speed of at least 100 Mb/s in 2019, despite high adoption of cloud services among SMEs, which ideally require higher download speeds. For medium-sized firms, this is the lowest value among European countries (Figure 3.10).

Figure 3.10. Enterprises with broadband connection by size

Percentage of enterprises that use DSL or other fixed broadband connection in 2019



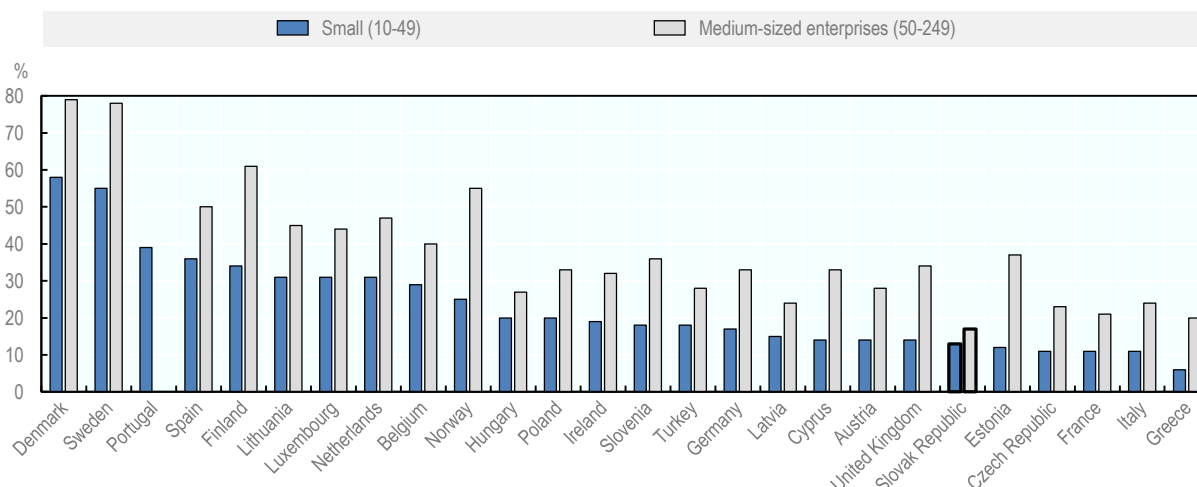
Note: Only the non-financial sector is considered.

Source: Eurostat (2021), Digital Economy and Society: ICT Usage in Enterprises Database, <https://ec.europa.eu/eurostat/web/digital-economy-and-society/data/database>.

StatLink  <https://doi.org/10.1787/888934247704>

Figure 3.11. Enterprises with fast internet connection by size

Share of enterprises with contracted download speed of the fastest fixed internet connection is at least 100Mb/s in 2019



Note: Only firms from the non-financial sector are considered.

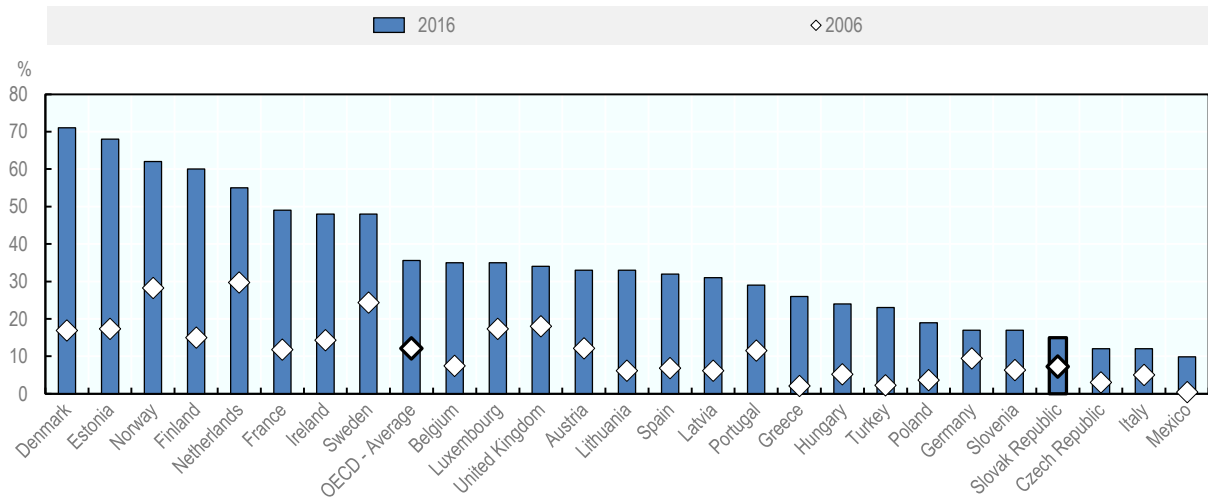
Source: Eurostat (2021), Digital Economy and Society: ICT Usage in Enterprises database, <https://ec.europa.eu/eurostat/web/digital-economy-and-society/data/database>.

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The Slovak Government could do more to harness the full potential that digitalisation offers. In 2016, 15% of individuals had used the internet to send completed forms to public authorities within recent months. In contrast, over 60% of individuals used internet for forms with public authorities in Nordic countries (Estonia, Denmark, Finland, Norway) (Figure 3.12). However, the Slovak Government has shown that progress in e-government practices can be achieved in relatively short time. In 2018, only 20% of firms were registered to fill their tax online, but following an awareness-raising campaign and assistance offered to individuals at the tax centres, the tax authorities were able to collect nearly 100% of tax filings online in the following year.

Figure 3.12. Digitalisation of government in the Slovak Republic

Percentage of individuals who used the internet for sending completed forms to public authorities in the last 12 months



Source: OECD (2021d), Government at a Glance database.

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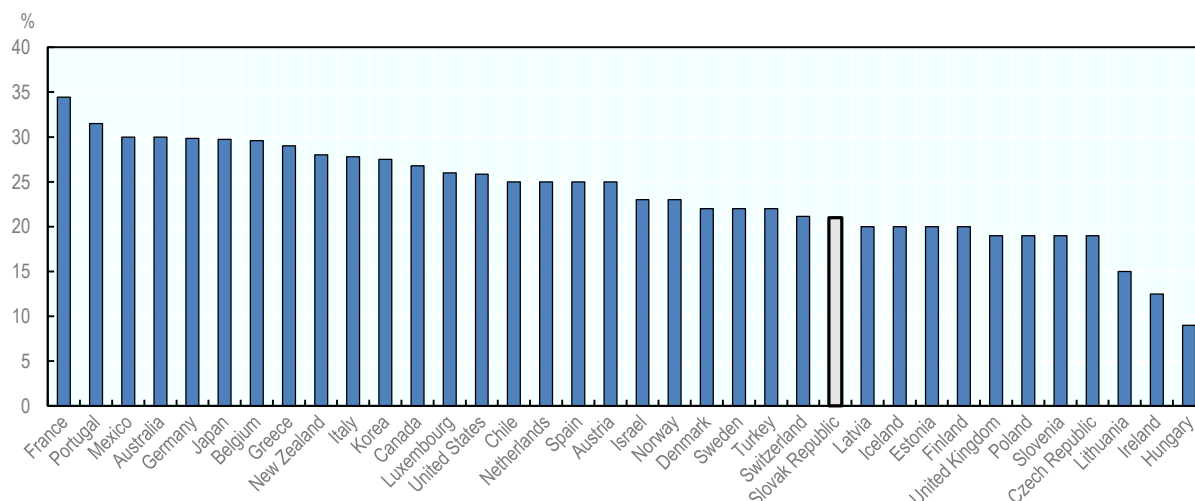
Taxation affecting SMEs

Corporate taxation is low and a lower rate regime has been introduced for the smallest firms

Corporate taxes are generally low in the Slovak Republic. The standard corporate income tax rate in the Slovak Republic was 21% in 2020 for corporate taxpayers with taxable revenues above EUR 100 000. This is lower than in most OECD countries, where the average was 24% in 2018 (Figure 3.13). A major tax reform in 2004 introduced a flat tax rate, replacing a system of corporate, income, dividend, and VAT tax rates between 10 to 38 per cent. This reform lowered the corporate tax rate from 25% to 19% on average, and broadened the tax base by eliminating most exemptions, for example for newly established firms. In the following years, the tax rates underwent multiple adjustments, reaching a rate of 21% in 2017 (Remeta et al., 2015).

Figure 3.13. Statutory corporate income tax rates

Combined corporate income tax rate in 2018



Note: This figure shows 'basic' (non-targeted) central, sub-central and combined (statutory) corporate income tax rates for resident corporations. Where a progressive (as opposed to flat) rate structure applies, the top marginal rate is shown. Tax rates targeted to specific industry or income types are not shown in the table.

Source: OECD (2020f), Public Sector, Taxation and Market Regulation: Corporate Tax Statistics database.

StatLink  <https://doi.org/10.1787/888934247761>

In addition, the Slovak Republic introduced a lower tax rate regime for the smallest firms in 2020. This involved a reduced corporate income tax of 15% for all self-employed people, entrepreneurs and corporations with income revenues less than EUR 100 000. Lowering the tax rate for micro firms can potentially increase their retained earnings, resulting in higher investment, growth and productivity. However, imposing tax breaks can also incentivise entrepreneurs to stay small. Research has shown that firms tend to keep their size under the threshold set by size-contingent policies. For example, the distribution of French firms shows that employment regulations for firms with 50 and more employees, represents a possible barrier to firm growth: the number of firms with 50 employees is half of the count of number of firms with 49 employees (Garicano, Lelarge and Van Reenen, 2016). It is therefore possible that the introduction of the lower tax rate will incentivise the self-employed and micro firms to remain small and report earnings under the threshold of EUR 100 000, even if they have higher growth potential. The impact of the reduced Slovak Republic tax rate for the smallest firms should therefore be carefully evaluated.

Only a handful of other countries have preferential rates for very small enterprises, and these schemes have had mixed results. The United Kingdom abolished its preferential rate in 2015 and introduced instead more targeted measures such as support to cover financing gaps for start-up businesses. A less distortive alternative to the recently established rate in the Slovak Republic could be a preferential tax rate for the first part of the business income, and a higher level after a threshold, as described in an example from Canada in Box 3.3.

Box 3.3. Corporate tax rate reduction for smaller profits firms: An example from Canada

Description of the approach

The federal small business tax rate, also called the Small Business Deduction (SBD), is a special tax regime for Canadian small firms. The eligibility and tax rate imposed depend on the tax capital of the firm and the level of business income. The special regime applies to firms with taxable capital of less than CAD 15 million and is applied on the first CAD 500 000 of active business income. The tax rate rises progressively with income, and the portion of income it is applied on reduces progressively with taxable capita, as shown below.

Taxable capita	Tax rate
Less than CAD 10 million	<ul style="list-style-type: none"> First CAD 500 000 of active business income: small business tax rate of 9% (after the small business tax deduction of 19%, in combination with a federal tax abatement of 10%) Over CAD 500 000: general business rate (15%)
CAD 10-15 million	<ul style="list-style-type: none"> Small business tax rate on a portion of the income, which gets proportionally smaller as the amount of taxable capital increases. The rest is taxed at the general business rate (15%)
More than CAD 15 million	<ul style="list-style-type: none"> General business rate (15%)

Factors of success

The goal of the SBD is to provide small firms with more after-tax income for reinvestment and expansion. The preferential tax rate for small business can also cover some of the regulatory compliance costs that small businesses bear disproportionately. The actual impact is difficult to evaluate for lack of a suitable control group.

Obstacles and responses

There are concerns about the cost efficiency of the measure. Spending that currently goes towards the SBD could be allocated to measures that might possibly be more effective in encouraging job creation and increases in economic activity, such as tax credits and deductions for business expenditures by small business, reduction in payroll taxes, and improved access to financing for small businesses.

Relevance to the Slovak Republic

Using the Canadian system of tax deductions, small firms would lose the incentive to keep their income under the threshold in order to qualify for the exemption. Only the first part of the income would be taxed at a lower rate, while remaining income can be taxed at the standard corporate tax. However, the challenge of defining the qualifying business threshold remains. A careful evaluation of the impact of the current incentives will give policy makers information about the cost and benefits of the preferential tax rate at varying thresholds. More targeted assistance should also be considered if the goal of the tax measures is to generate job creation, business growth, or assist in covering the financing gap for the most dynamic firms.

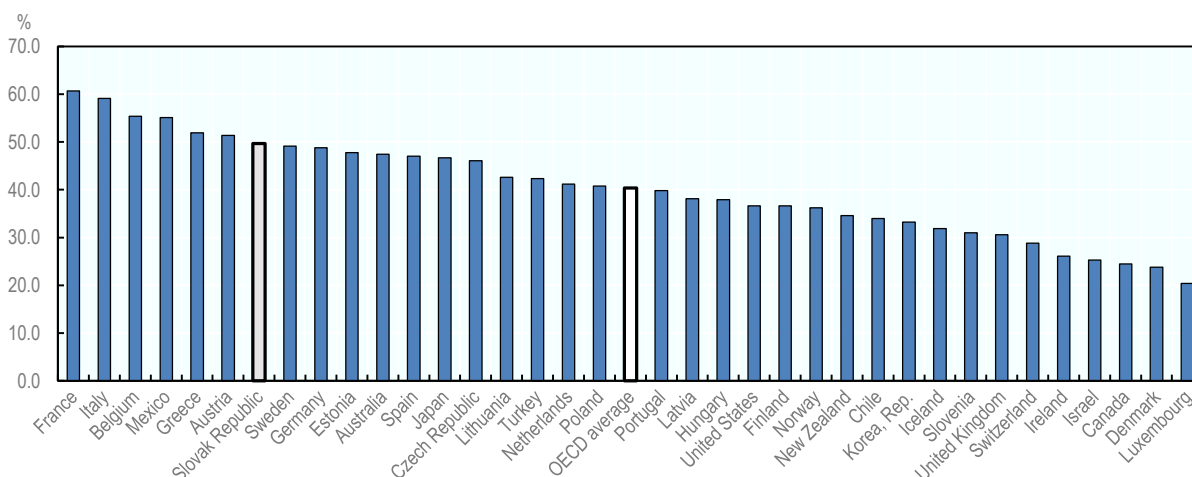
Source: (OECD, 2016)

The tax structure relies heavily on social security taxation, possibly discouraging firms from hiring

Despite comparatively low corporate tax rates, Slovak firms pay about half of their profit as taxes and other contributions in 2019, about 10% more than OECD average (Figure 3.14). This is mainly due to the high rate of social security charges. Contributions into social security system represent 44% of the total tax receipts in the country, compared to about one-quarter in the OECD. In contrast, taxes on personal income, profits and gains represent only 10% of profits (where the OECD average is 24%) (OECD, 2019a). The heavy dependence of tax revenues on employment taxation in the Slovak Republic may be a factor in the high share of micro firms without employees in the Slovak Republic.

Figure 3.14. Total tax and contribution rate

As percentage of profit in 2019



Note: Total tax rate measures the amount of taxes and mandatory contributions payable by businesses after accounting for allowable deductions and exemptions as a share of commercial profits. Taxes withheld (such as personal income tax) or collected and remitted to tax authorities (such as value added taxes, sales taxes or goods and service taxes) are excluded.

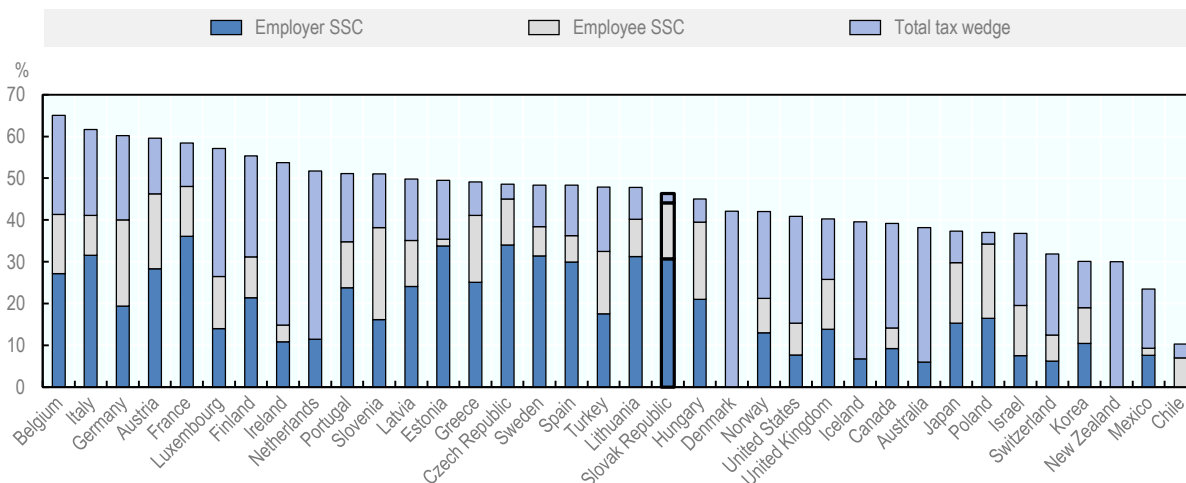
Source: World Bank (2019), Doing Business database, <http://www.doingbusiness.org/>

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Employee social security deductions and income taxes, including any local and central-government income taxation, added up to 46% of total labour costs in 2018, with the Slovak Republic ranked around the median of OECD countries (Figure 3.15).

Figure 3.15. Taxation on labour

Total tax wedge (income taxes and social security charges) as a share of labour cost of an average wage in 2018



Note: The tax wedge is the combined central and sub-central government income tax plus employee and employer social security contribution taxes, as a percentage of labour costs defined as gross wage earnings plus employer social security contributions. The tax wedge includes cash transfers.

Source: OECD (2020e), Public Sector, Taxation and Market Regulation: Tax Database.

StatLink  <https://doi.org/10.1787/888934247799>

Policy makers could consider reforms that would make employment as attractive as subcontracting. Until recently, the tax wedge for the self-employed was about 25% lower than for employees. The Slovak Government introduced measures in 2013 to reduce the discrepancies between the labour taxation of the self-employed and employees. However, as the self-employed can deduct their costs from taxable income and can choose other advantageous tax opportunities, employees continue to be interested in becoming independent contractors for their firms, which might be a factor in the high share of the self-employed in the economy (Remeta et al., 2015).

Tax incentives for employment are focused on marginalised workers

Slovak enterprises can benefit from employment tax incentives for hiring marginalised workers. The tax incentives are provided to firms in areas with a high local unemployment rate. In 2020, they amounted to up to 40% of the labour cost of marginalised workers for between three months and two years. Other employment incentives include hiring support in regions with high local or regional unemployment and incentives for employing workers with a disability. These tax incentives serve mainly in support of reintroducing the long-term unemployed to the labour market. Analyses are required to identify the effectiveness and efficiency of these measures.

Tax credits for innovative investments doubled between 2018-20, likely making R&D support more appealing to small enterprises

Tax credits are also offered to firms for investments in R&D. Between 2018 and 2020, the volume of R&D tax credits doubled. In the fiscal year 2020, these tax credits amounted to the double of the R&D costs incurred in this period. Spending on R&D, while still small compared to other OECD countries,

has risen over the past decade and policies are increasingly inclusive with about 17% of small firms and 16% of medium-sized firms investing in R&D as shown in Chapter 2. Some 150% of R&D costs incurred in 2019 could be deducted from the tax base, up from 100% in 2018. Before 2018, the deduction was capped at 25% for the qualifying R&D expenditure and 50% for labour costs. In 2015, a hybrid R&D tax allowance was introduced that extended the R&D support from grant recipients to tax incentive support, increasing total business R&D expenditures (OECD, 2019c).

Such incentives will likely help increase R&D investments, on condition that information is disseminated on the application process and requirements, especially to smaller firms, as well as ensuring that procedures are administratively accessible. The design of the scheme is discussed in more detail in chapter 6.

There is potential for a tax break for equity investments in small firms

The Slovak Republic could consider introducing tax breaks for equity investments to help fast growing firms obtain necessary capital. The take-up of equity finance in the Slovak Republic is very low, especially among SMEs (with none of the surveyed enterprises according to SAFE survey in 2019 using external equity). At the same time, there are few tax incentives that would spur equity investments. At the corporate level, tax systems often favour debt financing over equity financing due to the deductibility of the costs of debt finance against the income of the corporation, in contrast with non-deductible equity finance. The difference of the tax rates in the Slovak Republic on the equity and top corporate bonds is 14%, (Harding and Marten, 2018). Equity investments could be encouraged in a form of tax credit, which would make equity investments comparable in terms of after-tax returns with investments in bonds.

SME access to finance

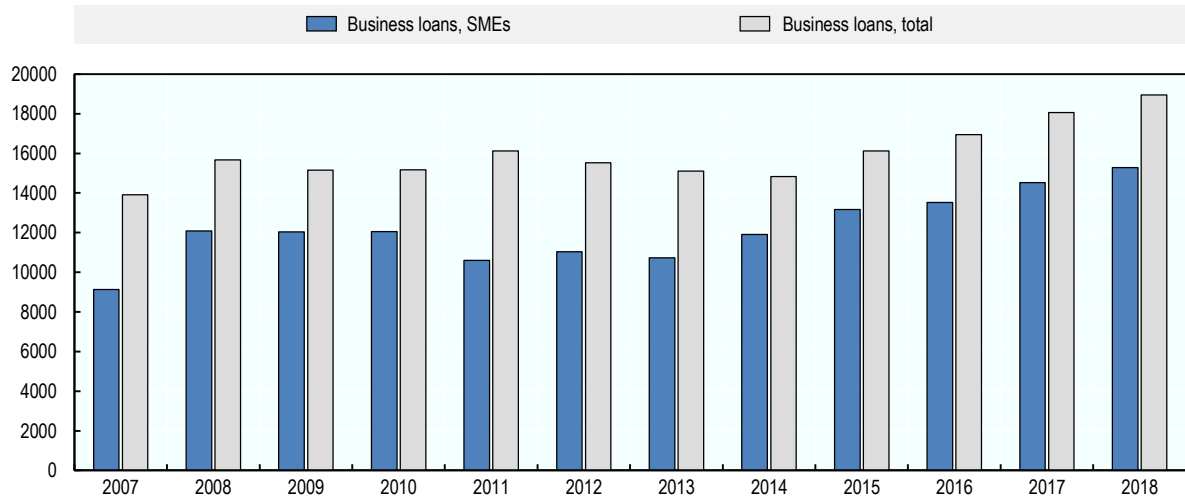
There is a strong reliance on straight debt

Slovak entrepreneurs rely heavily on traditional means of financing, including savings, family funds, reinvested capital, bank loans, bank and credit overdrafts, debt securities and factoring. In 2019, 81% of SMEs used traditional financing methods to obtain credit, with 35% using a credit line, bank overdraft or credit overdraft within the last 6 months and another 20% more than 6 months ago (EC, 2019).

Business loans to SMEs increased by 4.1% between 2017 and 2018, following the trend of the previous years, although they declined in 2019 for the first time since 2014 (Figure 3.16). The long run increase has been driven by greater long-term loans. About 40% of SMEs report taking on a bank loan.

Figure 3.16. Business loans by SMEs in the Slovak Republic

Total amount, in millions of EUR



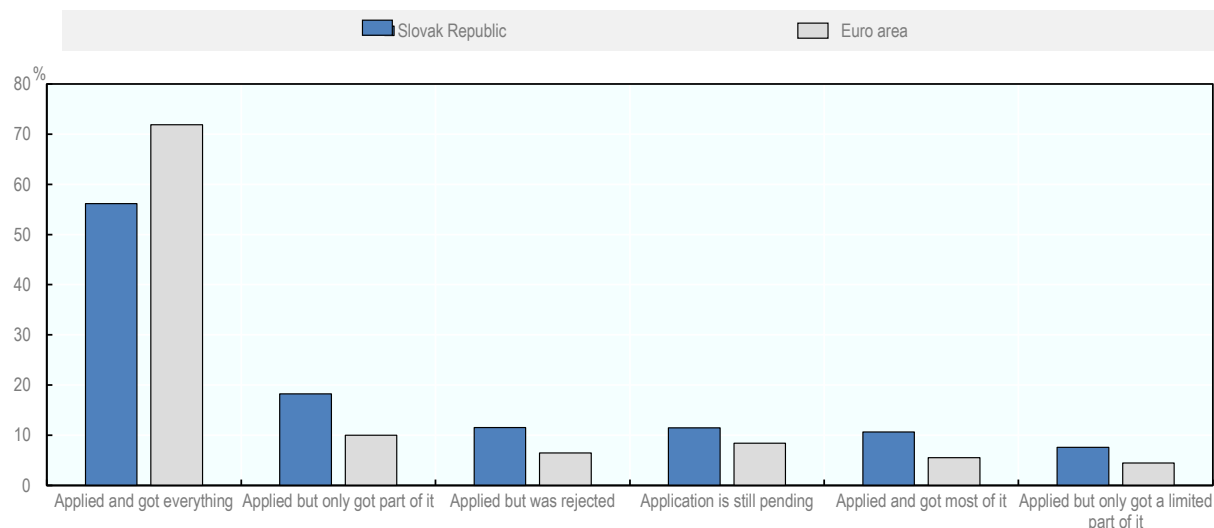
Source: Data from Financing SMEs and Entrepreneurs 2020: An OECD Scoreboard (OECD, 2020).

StatLink  <https://doi.org/10.1787/888934247818>

Approval rates for bank loans are low in the Slovak Republic as compared to other EU countries. In 2019, only 56% of Slovak entrepreneurs who applied for a loan received the full amount requested, in contrast with 72% of firms across the Euro area. Slovak applications are also more frequently rejected. In addition, the rejection rate of 12% in the first half of 2019 was double the rate in the Euro zone (Figure 3.17). Despite lower loan approval rates, entrepreneurs tend to report access to bank financing as being satisfactory. By 2019, interest rates on loans for SMEs had fallen to their lowest level for the past decade, to 2.9%, down from 5.5% in 2007 (National Bank of Slovakia).

Figure 3.17. SME approval rate for bank loans in the Slovak Republic and Euro area

Weighted percentage of responses in the first half of 2019



Note: Remaining responses: "Do not know" and "Applied but refused because cost too high" are the least frequent answers among surveyed firms, with 0% to 2.6% share.

Source: European Central Bank (2020), SAFE - Survey on Access to Finance of Enterprises, https://www.ecb.europa.eu/stats/ecb_surveys/safe/html/index.en.html.

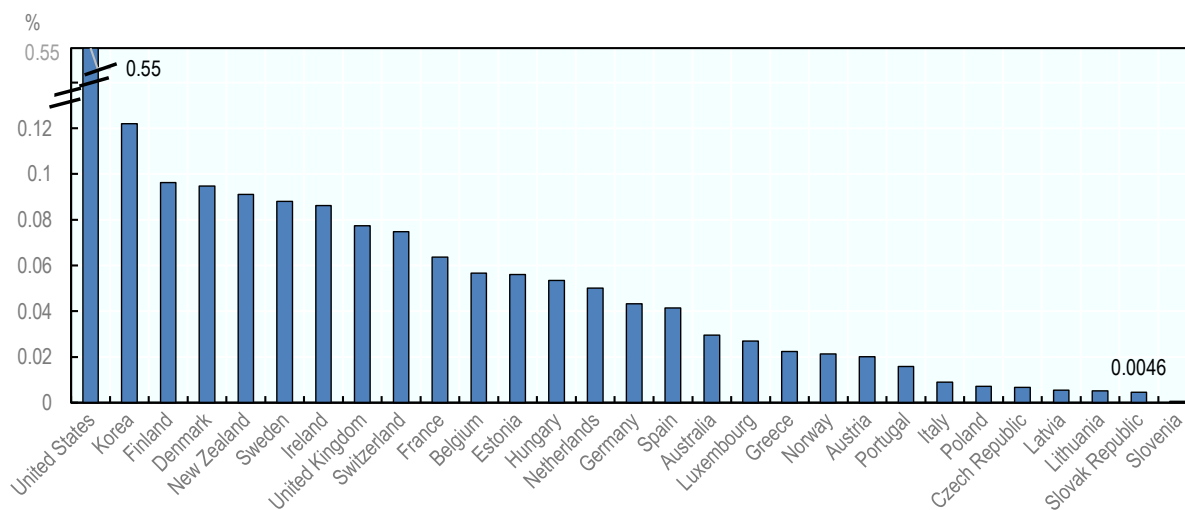
StatLink  <https://doi.org/10.1787/888934247837>

Alternative forms of financing to debt are generally underdeveloped. For example, 95% of SMEs do not use equity capital, 10% more than the EU average. This contrast with 57% of SMEs that were not using bank loans, and 43% not using bank overdrafts (51% and 46% in the EU, respectively). The share of venture capital investments in GDP in the Slovak Republic is among the lowest in the OECD. Venture capital investments amount to 0.0046 of GDP in the Slovak Republic, only ahead of Slovenia among OECD countries, where venture capital stands at 0.06% of their GDP on average (Figure 3.18). There were only six transactions in 2018 (3 by the Slovak Investment Holding and 3 by the Slovak Business Agency via the National Holding Fund). In 2019, 15 transactions were realised in a total volume of EUR 30 650 000.

A comparative study of SME market gaps and market failures among EU member states indicates that, while the debt finance gap is relatively limited, there appear to be significant market failures at play when it comes to equity finance markets. While additional policy interventions on the supply side would support innovative SMEs to access more equity financing, there is also a clear need to improve the quality of projects that can be presented to equity funds. Only 3% of the Slovak SMEs consider equity financing as a relevant form of financing, in contrast with one-quarter of SMEs in Croatia or Slovenia. A combination of demand and supply side factors restrict equity markets (EC/EIB, 2019).

Figure 3.18. Venture capital investments

In US Dollars as a share of GDP in 2018



Note: Venture capital is made up of the sum of early stage (including pre-seed, seed, start-up and other early stage) and later stage venture capital. As there are no harmonised definitions of venture capital stages across venture capital associations and other data providers, original data have been re-aggregated to fit the OECD classification of venture capital by stages.

Source: OECD (2020g), Enterprise Statistics Database.

StatLink  <https://doi.org/10.1787/888934247856>

Volumes of venture capital funding declined significantly in 2017, following the closure of funding support of the EU and European Investment Bank Group's initiative "Joint European Resources for Micro to Medium Enterprises" (JEREMIE) for the 2007-2013 programming period. Venture capital investments recovered in 2018, almost doubling the size of the funding of the previous year, but remaining below the level of previous decade. The majority of the investments supported development in established SMEs, including expanding production capacities, developing market potential, or product and service development. Supporting start-up activities and seed investments represented about 40% of the total venture capital investments over past decade (Table 3.6).

Table 3.6. Venture capital investments in SMEs in the Slovak Republic

In millions of Euros

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Seed	0.22	3.85	2.1	0.66	0.87	1.19	0.06	1.2	1.69	4.45	0.2	0	1.1
Start-up	0.05	0.45	3.9	10.9	4.8	0.2	0	1.72	5.65	9.63	1.3	0.4	2
Development	6.77	3.69	8.37	0.46	5.8	5.59	8.93	6.05	3.5	3	1.5	5	27.6
Total	7.04	7.99	14.37	11.42	11.47	6.98	8.99	8.97	10.84	17.08	2.91	5.4	30.65

Source: OECD (2020h). Report on the state of SMEs in the Slovak Republic.

A well-functioning angel network or syndicate can bring large benefits to the early stage finance ecosystem by enabling investors to diversify their risks by investing in a (potentially wide) portfolio of projects. While no reliable data exists, interviews with key stakeholders indicates that business angel activities are modest in the Slovak Republic, co-investment relatively rare and the angel network has a low profile. The country still lacks a dedicated governmental business angel funds programme that

would generate more early-stage financing sources. The Slovak Business Angel Network, established in 2011 by the Young Entrepreneurs Association of Slovakia, the Slovak Venture Capital and Private Equity Association, and the Slovak Business Agency, aimed to fill this gap. Its aim was to offer matchmaking services between viable projects in need of equity and (potential) angel investors, provide networking opportunities for investors in the Slovak Republic, organise events and forums, and pre-select potential business projects on their merits and investment-readiness, yet their activity has stalled.

The government may want to consider (re)introducing measures to strengthen the angel network as a cost-effective and non-distortive way to stimulate the early stage equity market. This could take the form of tax incentives or credits for investors in start-ups. It could be accompanied by logistical and financial support for the angel investment network, which would help match finance demand and supply.

A 2017 study on tax incentives, commissioned by the European Commission, finds that these often positively impact equity investments for start-ups and SMEs and play an increasingly important role in the policy mix among EU governments and beyond. The Slovak Republic does not have such a tax relief in place, and could reconsider piloting one. The Seed Enterprise Investment Scheme (SEIS) in the United Kingdom is considered as a best practice example considering its scope, qualifying criteria and administration (See Box 3.4).

Box 3.4. Seed Enterprise Investment Scheme in the United Kingdom

Description of the approach

The Seed Enterprise Investment Scheme (SEIS) is an investment incentive initiative designed to boost economic growth in the United Kingdom by stimulating equity investments in new enterprises with growth potential. It also includes a platform linking start-ups and (potential) investors, allowing new firms to promote their company to potential investors and offering investors a convenient way to search for investee companies.

Besides its start-up and investor matching potential, SEIS supports investments through tax incentives. The scheme provides the investors with an upfront tax credit for investments in young companies, a capital gains tax deferral for reinvestment, a capital gains tax exemption for chargeable gains realised on disposal, and loss relief on more favourable terms than the baseline tax system for capital losses realised on disposal. Targeting entrepreneurial firms, SEIS combines age, size and specific sector exclusions.

Factors for success

The particularity of the Seed Enterprise Investment Scheme as compared to similar schemes across different countries, lies in its combination of tax incentives, its well-targeted qualifying criteria, administrative procedures, and stability, earning the highest score in a study on effectiveness of tax incentives for venture capital by European Commission. Evidence on the impact of the SEIS states that about one-quarter of the investments in EIS would not be made in its absence.

Important factors of success are:

- Government investments are indirect, as the investments are made by the private sector, which avoids the problematic of the government “picking winners”.
- The tax relief is generous and widely advertised in the financial press, resulting in a high level of investor awareness and participation.
- The scheme is reviewed and adjusted periodically to keep up with the evolving needs of its beneficiaries.

Potential difficulties

The complex rules of the investment scheme may dissuade its use in some instances. Some investors are deterred by the complexity of the rules or by the maximum equity stake limit that they are allowed to take in the SEIS companies under the eligibility rules.

Relevance for the Slovak Republic

Given the limited size of the early-stage investments and underdeveloped business angel investor community in the Slovak Republic, the government could establish a scheme that would offer tax credits for investments in new firms with high potential so as to de-risk these investments. Another support mechanism to new firms is establishing a platform where new firms could obtain visibility and potential investors could browse project proposals. To motivate the equity investors, the restrictions and procedures should be straightforward and proportionate.

Source: (European Commission, 2017)

Raising financial literacy among entrepreneurs can improve their ability to obtain funding

In addition to barriers on the supply side of the finance market, financial literacy of the population is lagging behind other countries. The OECD's PISA scores evaluating financial literacy of 15-year olds ranks Slovak Republic among the lowest performers, only ahead of Chile, Peru and Brazil.

Furthermore, the offer of financial education for Slovak entrepreneurs remains fragmented. Financial literacy programmes are currently on offer by both non-government and government bodies, including the Financial Literacy Support Strategy of the National Bank of Slovakia, adopted in 2019. In schools, financial education was incorporated into curriculum of existing courses in primary and secondary schools since 2009, and teacher training on financial education has been carried out by non-profit organisations. The current training programmes follow a one-size fits all approach providing basic education with a focus on the needs of consumers. There seems to be a paucity of relevant programmes targeting (potential) entrepreneurs and small business owners.

While no specific comprehensive data exist about the financial skills and acumen of entrepreneurs and business owners, there appears ample room for improvement. Research indicates that many innovative SMEs across the globe with a solid business model encounter difficulties in presenting their case to (potential) outside investors in a transparent and reliable way, and this situation is probably no different in the Slovak Republic. Investment readiness programmes are a relatively well-established policy response to such demand-side barriers in equity markets for SMEs (Boschmans and Pissareva, 2017). These programmes involve a combination of individualised training, mentoring and coaching for a relatively limited number of "high-potential" ventures, often in combination with other support measures such as innovation vouchers and grants. Enterprise Ireland is a case in point of a government body that takes a comprehensive approach to raising the number of companies that can successfully attract private equity (See Box 3.5). The Slovak Republic could set up a similar scheme.

Box 3.5. Boosting entrepreneur investor readiness and funding in Ireland via high-potential start-ups support

Enterprise Ireland offers numerous programmes targeted to support "high potential start-up" (HPSU) companies. HPSUs are identified as start-up businesses with the potential to develop an innovative product or service that can then be sold on international markets. They can be at feasibility stage, investor ready stage or growth stage.

Description of the approach

At each of the firm development stages, Enterprise Ireland assists entrepreneurs in acquiring skills and knowledge for further development.

- **Feasibility stage:** Support to develop the business idea or proposal to the "investor ready" level.
 - HPSU feasibility grant to support the development of an innovative start-up and development of an investor-ready business plan by covering costs such as salaries, consultancy fees, foreign travel, or trade fair costs.
 - Innovation voucher to work with a local college to solve a technical problem.
 - New frontiers entrepreneur development programme offers mentoring, incubation space, or scholarship payment to accelerate the growth, develop skills, and create contacts needed to start and grow a company.
 - Mentor grant matches a new entrepreneur with an experienced business mentor.

- **Investor Ready Stage:** Support to raise investment.
 - Competitive Start Fund: Investment of EUR 50 000 of equity designed to accelerate the development of the company by supporting achievements in commercial and technical milestones (evaluating international market opportunities, building prototype).
 - Innovative HPSU Fund: Equity investment to HPSU entrepreneurs on a co-funded basis to support the implementation of company's business plans.
- **Post-investment stage:** Support focused on exploring new international opportunities and continued development of the management team:
 - Numerous funds and vouchers: Market discovery fund, mentor grant, innovation voucher.
 - Workshops: Excel at export selling.

Over a period of 10 years, Enterprise Ireland assisted about 1 000 HPSUs. It supported investments of more than EUR 122 million between 2015 and 2019. The success underlines the organisation's goal of development of the next generation of business leaders and making the country a suitable place to start and scale up a business.

Relevance to the Slovak Republic

Adopting a combined approach of training and matching with equity co-investors could help Slovak entrepreneurs throughout the early stages of their life cycle. This approach may be more efficient than individual programmes that prepare the entrepreneur for the investment stage, which are separated from raising the funds to finance the company. In the first stage of conception of the idea and creating links with universities or technology centres, specialised training or consultations could guide the entrepreneur to generate a solid business plan, understand its potential and develop skills necessary to raise funding. This would prepare entrepreneurs for raising investments at each stage of company growth, and recognise and act upon the opportunities of markets, better understanding the potential. Such a programme could also develop networks and generate entrepreneurial culture.

Source: (Enterprise Ireland, 2020a) and (Enterprise Ireland, 2020b).

Trade and foreign direct investment

Business environment conditions are supportive of Slovak SME exports

Over the past two decades, the openness of the Slovak economy has increased steadily, with exports and imports reaching over 90% of GDP (Giorno, 2019). Business conditions are supportive of trade. The Slovak Republic had one of the best performances among 190 economies on the "Trading across Borders" indicator of the World Bank Doing Business index, alongside other Central-European countries (the Czech Republic, Hungary, Poland, and Slovenia). Slovak exporters and importers face zero costs to comply with documentation and border restrictions take only about one hour, to the benefit especially of SMEs. Slovak SMEs are nonetheless less likely to export than their counterparts in many other OECD countries.

Success in attracting FDI fails to translate into productivity spillovers for SMEs

The Slovak Republic has been very successful in attracting foreign direct investment (FDI). By 2016, foreign-owned firms in the Slovak Republic employed more than one in two manufacturing workers, despite not being numerous (only 1.6% of all Slovak manufacturers). This share was larger than in any other OECD country, where an average of approximately one-third of the manufacturing workforce is employed by a multinational firm (OECD, 2020a). Most of the investors come from Germany and other European countries, although FDI from Japan and the United States increased between 2010 and 2016.

Similarly, investors from other countries contributed to a 24% growth in employment in multinational manufacturing firms and a 54% growth in MNE employment in service sectors between 2010 and 2016, or about 105 000 jobs in total (Table 3.7). Furthermore, it is estimated that more than 80% of the total value of exports and imports is generated by foreign-owned exporter accounts in the Slovak Republic (OECD, 2015).

Table 3.7. Origin of largest foreign direct investments in the Slovak Republic

Number of multinational enterprises (MNEs) and employment in MNEs in 2016 and MNE employment growth by sector 2010-2016.

	Manufacturing			Services		
	Number of MNEs	Employment in MNE	Growth 2010-2016, %	Number of MNEs	Employment in MNE	2010-2016, %
Germany	244	76496	52.9	329	46856	91
United States	53	31121	78.1			
Austria	98	12978	-2.8			
Czech Republic	103	11956	30.7	487	15950	N/A
France	59	11514	37.8			
Italy	91	11158	2.3			
Japan	18	8368	112.9	30	996	N/A
Netherlands	48	7513	-61.9			
Switzerland	51	6611	8.4			
United Kingdom	42	5720	-7.2			
Belgium	40	5691	52.8			
Total	1113	249935	23.6	2372	163905	53.6

Note: Top countries with FDI that employed at least 5 000 employees in the Slovak Republic in 2016.

Source: OECD (2017b), AMNE database.

Inward foreign direct investment (FDI) may raise the productivity of domestic firms through knowledge spillovers. However, knowledge spillovers largely rely on supply relationships between domestic companies and multinationals. These supply relationships are relatively limited in the Slovak Republic, as measured by the value-added content from domestic firms in MNE exports. For example, transport equipment, the main exporting industry in the Slovak Republic, generates over one-quarter of gross exports, but adds only 40% of value locally, placing the Slovak Republic on the bottom of the distribution of domestic value added in the OECD (OECD, 2019a). It is not only local manufacturing SMEs that fail to participate in the creation of value added of foreign firms. Multinational firms and exporters also rely on foreign services at a greater intensity than in other countries. For example, domestic services value added contributed only 26% of gross exports, in contrast with an average of almost 40% in small OECD economies in 2014 (OECD, 2019a)..

One reason is the type of FDI that locates in the Slovak Republic. Many multinational firms in the Slovak Republic are focused mostly on the assembly of imported intermediate goods, which can be achieved with minimal interaction with local suppliers. The Slovak Republic could target investments higher up the value chain that would engage in more local content in their product, foster the development of local enterprises, and could help to diversify the economy.

Another issue is perceived weaknesses of potential domestic suppliers related to product quality, production efficiency, and workforce skill. Raising the availability of skilled labour through education and on-the-job training and improving management skills could help address these issues.

Conclusions and policy recommendations

Macroeconomic conditions in the pre-COVID-19 period have been favourable to business growth in recent years. However, the current crisis that has resulted from the COVID-19 pandemic is creating new short-term vulnerabilities for SMEs and start-ups. The Slovak Government has introduced a strong policy response to support small firms to survive this crisis.

The regulatory environment for SMEs and entrepreneurship in the Slovak Republic is strong in many areas when compared with OECD averages, including the system of regulatory impact assessment. However, there are also areas of weakness, in particular concerning relatively burdensome business start-up regulation. Another concern for Slovak small firms is the issue of frequent changes and amendments to small business legislation.

In terms of innovation, the Slovak Republic is labelled only as a moderate innovator by the European Innovation Scoreboard and ranks at the tail of the OECD rankings on various measures of innovation intensity among SMEs. Innovation spending has been increasing over past decade and R&D tax credits represent a key support mechanism introduced recently. However, lack of innovation spending and business engagement with higher education institutes holds back the commercialisation of research by SMEs and start-ups.

The availability of a skilled workforce remains a central challenge for SMEs in the Slovak Republic. Skills shortages relate to digital and business services skills and to soft skills such as management and oral expression. Improving the availability of these skills sets among university graduates and the existing SME workforce via on-job training, can lead to higher productivity and innovation among SMEs. The government could also step up efforts to attract skilled workers from abroad, especially the large Slovak diaspora living in other countries.

The transport network has improved substantially in recent years, although the infrastructure is stronger in the west of the country, which has had an impact on the location of some business investments. Increasingly, digital infrastructure is an additional key requirement for SME and entrepreneurship development and further investments are required across the country.

Revenue generation through the Slovak tax system is relatively weighted to social security contributions compared with property taxes and taxes on personal income and profits. The relatively high tax on labour might be connected to the relatively large share of firms without employees in the Slovak Republic. Corporate taxes are generally low and a lower regime for the smallest firms was introduced in 2020.

Slovak entrepreneurs rely heavily on traditional means of financing their capital, including savings, family funds, reinvested capital and bank loans. Slovak firms make little use of alternative sources of financing. Equity markets are largely undeveloped. To support investments (especially for innovative activities) and entrepreneurial dynamics, the Slovak Republic could consider introducing tax breaks for equity investments to help fast growing firms obtain necessary capital. Financial literacy among the Slovak population is generally low, and there are indications of a decline in recent years.

Trade and foreign direct investments have played a major role in development of the economy of the Slovak Republic. Foreign direct investment can domestic firm productivity through knowledge spillovers in particular. However, this will require additional efforts for domestic companies to create supply relationship with multinationals.

The following recommendations are proposed based on the assessment of the business environment for SME and entrepreneurship development.

Box 3.6. Key policy recommendations on the business environment for SMEs and entrepreneurship

Regulatory environment

- Fully implement the RIA 2020 Strategy to improve the overall culture of evaluation of regulations.
- Streamline and centralise regulatory oversight and provide training facilities to improve regulatory management practices.
- All governmental proposals, including initiatives of members of parliament, should undergo the same legislative procedures and involve engagement with stakeholders, allowing enough time for discussion and collection of comments.
- Review existing regulations and their usefulness on a systematic basis.
- Adopt simplification procedures to decrease administrative burden by continuing to upgrade electronic documentation procedures.
- Carefully monitor the impact of the recent modifications to the insolvency procedure and consider taking additional action to reduce the time required and cost of bankruptcy.
- Limit gold-plating by ensuring all new legislation introduces only the necessary amount of regulations.

Innovation and R&D

- Improve the coordination of the various public stakeholders active in the innovation sphere.
- Pool different academic research initiatives and create larger research units, which could act as focal points for public-private innovation partnerships.

Education/skills

- Establish skills councils to assess skills needs, ensure the representation of SMEs within them, and create a mechanism for SMEs to influence the curriculum to address skills shortages.
- Increase SME participation in apprenticeship programmes.
- Minimise costs and barriers to participation of SMEs in vocational education and training programmes and boost the variety of course offerings to include digital skills training, management capabilities training, and improving soft skills such as communication.
- Engage with diaspora communities and develop outreach programmes to attract back skilled Slovaks living abroad.

Taxation

- Carefully review possible unintended consequences of lower corporate tax rates for micro firms.
- Reduce the tax incentive for self-employment by ensuring a similar tax burden from social security contributions on self-employed income as on employment income.
- Assess the impact of the recent expansion of the R&D tax credit and adjust if necessary, increase awareness among SMEs of available R&D tax credits and ensure administrative clarity in the application and follow-up process for the tax credits.

SME access to finance

- Establish investment readiness programmes to prepare entrepreneurs to access finance at all stages in the development of their firm.
- Introduce tax incentives or exemptions for early stage equity investors to support the development of alternative forms of financing for innovative and growth potential SMEs and start-ups.
- Improve financial education in the population with appropriate financial training initiatives.
- Support co-funding of early-stage equity investments.

Trade and foreign direct investment

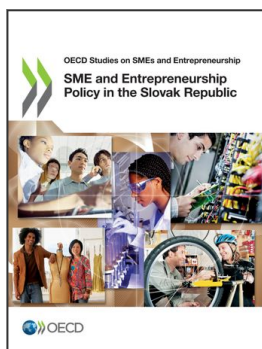
- Strengthen the emphasis of FDI attraction efforts on more knowledge- and skill-intensive investments with greater potential for domestic innovation spillovers.
- Increase the capacity of domestic firms to participate in global value chain networks by ensuring the availability of a qualified workforce and strengthening management capabilities in SMEs.

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