

Obstacles of Small and Medium-Sized Enterprises Development in the Republic of Armenia

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Keywords: small and medium-sized enterprises /SMEs/, business and entrepreneurship, market economy, export potential of SMEs, governmental regulation of SMEs.

Հայաստանի Հանրապետության փոքր և միջին ձեռնարկությունների զարգացման խոչընդոտները

Բունդի Խաչատրյան

Երևանի «Գլաձոր» համալսարան, Ընդհանուր տնտեսագիտության ամբիոնի հայցորդ (Երևան, ՀՀ)

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Ամփոփագիր. Փոքր և միջին ձեռնարկատիրությունը յուրաքանչյուր երկրի տնտեսական և սոցիալական կայունության հիմնական երաշխիքներից մեկն է: Ոլորտի զարգացումը հնարավորություն է տալիս մեղմելու անցումային տնտեսություններին բնորոշ տնտեսական և սոցիալական դժվարությունները՝ ստեղծելով կայուն պայմաններ հետագա տնտեսական աճի համար: ՓՄՁ ոլորտը նշանակալի դեր ունի Հայաստանի ՀՆԱ-ի, գրավածության, հարկային եկամուտների ձևավորման, եկամուտների հավասարաչափ բաշխման և աղքատության հաղթահարման գործում: Այսպիսով, ՓՄՁ ոլորտի մրցունակության ամրապնդումը չափազանց կարևոր է տնտեսական զարգացման համար՝ նվազեցնելով արտաքին գործոններից կախվածությունը և ապահովելով կայուն տնտեսական աճ: 2012 թվականից Հայաստանը նախաձեռնել է իրականացրել է մի շարք բարեփոխումներ՝ ուղղված ՓՄՁ ոլորտի զարգացմանն ու աջակցությանը, այդ թվում՝ կարգավորող օրենսդրության պարզեցմանը, էլեկտրոնային կառավարման ընդլայնմանը, ձեռնարկատիրական կրթության և մշակույթի զարգացմանը, գործարար միջավայրի բարելավմանը և բիզնեսի աջակցության առաջադեմ ենթակառուցվածքների ապահովմանը: Չգալի աշխատանք է կատարվել նաև ՓՄՁ զարգացման քաղաքականության շրջանակն ապահովելու ուղղությամբ: Ակնհայտ է, որ փոքր և միջին ձեռնարկատիրությունը կարևոր դեր է խաղում յուրաքանչյուր երկրի տնտեսական և սոցիալական զարգացման գործում: Սույն աշխատությունը նպատակ ունի ուսումնասիրել Հայաստանի Հանրապետության փոքր և միջին ձեռնարկատիրության ոլորտը, բացահայտել ոլորտի զարգացման հիմնական միտումներն ու ուղղությունները, զարգացմանը խոչընդոտող հիմնական խոչընդոտները, ինչպես նաև կատարվել են մի շարք եզրակացություններ և առաջարկություններ, որոնք կարող են օգտագործել ոլորտի բարելավման և զարգացման համար:

Հանգուցաբառեր՝ փոքր և միջին ձեռնարկություններ /ՓՄՁ/, բիզնես և ձեռներեցություն, շուկայական տնտեսություն, ՓՄՁ-ների արտահանման ներուժ, ՓՄՁ-ների պետական կարգավորում:

Препятствия развитию малых и средних предприятий в Республике Армения

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Аннотация. Малые и средние предприятия являются одной из главных гарантий экономической и социальной стабильности каждой страны. Развитие сектора дает возможность смягчить экономические и социальные трудности, присущие странам с переходной экономикой, создавая стабильные условия для дальнейшего экономического роста. Сектор МСП играет значительную роль в формировании ВВП Армении, занятости, налоговых поступлений, обеспечении равного распределения доходов и преодолении бедности. Таким образом, усиление конкурентоспособности сектора МСП имеет решающее значение для экономического развития за счет снижения зависимости от внешних факторов и обеспечения устойчивого экономического роста. С 2012 года Армения инициировала и реализовала ряд реформ, направленных на развитие и поддержку сектора МСП, включая упрощение регулирующего законодательства, расширение электронного правительства, развитие предпринимательского образования и культуры, улучшение бизнес-среды и предоставление передовой инфраструктуры поддержки бизнеса. Также была проделана значительная работа по обеспечению основ политики развития МСП. Очевидно, что малые и средние предприятия играют важную роль в экономическом и социальном развитии каждой страны. В данной статье ставится задача исследовать сектор малых и средних предприятий в Республике Армения, выявить основные тенденции и направления развития сектора, основные препятствия, мешающие развитию, а также сделать выводы и предложить рекомендации, которые могут использоваться для улучшения и развития отрасли.

Ключевые слова: малые и средние предприятия /МСП/, бизнес и предпринимательство, рыночная экономика, экспортный потенциал МСП, государственное регулирование МСП.

1. Introduction.

In general, the main basis of a market economy system is SMEs as the most massive, dynamic and flexible form of business. Accordingly, small and medium enterprises are the main guarantee of economic and social stability of each country. Specifically, SMEs, as it can be derived from the name, is a type of business activity carried out by market economy entities under certain conditions, by criteria approved by state or other representative organizations, which define the essence of this concept. As a rule, the main criteria according to which the enterprise is considered an SME entity are the following:

1. Number of employees;
2. The amount of authorized capital;
3. The amount of assets.

The importance of small and medium enterprises development in the modern world is one of the main imperatives for the reconstruction and development of national economies. It is the main guarantee of the establishment of market relations and economic progress. Specifically, the SME sector covers an appropriately large sector of the economy; it represents manufacturing, processing enterprises, crafts, retail, wholesale, farms, services, services, etc. SMEs are the main driver of market economy development. It promotes private property and entrepreneurial skills, is flexible in a changing market economy, helps to diversify economic activity and can make a significant contribution to international trade, export promotion as well as jobs creation, as SMEs development is a unique, effective precondition for the improvement of population life. In this context, the significance of small and medium enterprises for the country's economy can be demonstrated by the following factors:

➤ SME development ensures strong and dynamic private sector formation;

➤ The development of SMEs ensures growing of the economically active part of the population, the incomes of the citizens increase, the disproportions of the welfare of different social groups are smoothed;

➤ The development of SMEs provides an opportunity to ensure economic growth in a short period of time, to stimulate the production of competitive products for foreign markets;

➤ SME sector creates a significant part of GDP;

➤ SMEs can provide a significant number of new jobs opportunities in a short period of time, by significantly improving the situation in the labor market and solving a number of serious social problems;

➤ New technologies and innovations are introduced in SMEs in relatively quickly and at low cost;

➤ SMEs use local resources more efficiently by reducing the dependence of the country's economy on imports; ➤ SME products compete with imported products and replace them with local ones;

➤ SMEs, due to their flexibility, adapt more quickly to market demands, mastering the production of new products;

➤ The development of SMEs in the regions significantly contributes to the implementation of targeted regional policy in the country, the development of SMEs is the guarantee of the formation of the middle class that forms the basis of modern society;

➤ Due to their strategic significance and opportunities for further development, SMEs contribute to the revitalization and resuscitation of all sectors of the economy, including the expansion of opportunities for large enterprises.

Taking on some of the production stages of large enterprises, it contributes making large productions more profitable and gives flexibility to the latter. It is worth to mention that in developed countries, small and medium enterprises make up 80- 99% of all enterprises. SMEs in these countries are considered a source of economic stability, innovation and dynamic growth of jobs. SME capacity and timeliness are evidenced by OECD data, which show that in 30 Member States the share of SMEs is 95% of the total share of enterprises, which includes 60-70% of the total workforce. According to the same source, 72% of employment in EU countries is provided by SMEs, where 66% of GDP is generated [7, p. 252]. It is to state that the bases of entrepreneurial activity in the Republic of Armenia, the rights and responsibilities of entrepreneurs, the organizational and legal forms of enterprises, the grounds for their creation, operation and termination of activity are defined by the RA Civil Code. Its main purpose is to make a profit from the use of property, the sale of goods, the performance of works or the provision of services. According to McIntyre, the synergistic relationship between SMEs and larger enterprises, is a critical factor [6, pp. 121-141]. Meanwhile, SMEs have a greater chance of succeeding in business than large enterprises due to the following conditions: the use of a strategy oriented to small market segments, the absence of strong competition, insurmountable barriers in the market, low level of production capitalization, direct contact with consumers, opportunity for direct contact with consumers, opportunity to penetrate to the market quickly,

opportunity to use the results of the work done in various ways, relative stability of economic conditions (raw materials, materials, energy, price stability, etc.), etc.

2. Literature review

Small and medium-sized enterprises (SMEs) are often seen as the backbone of economic employment in prosperous economies, as well as the driving force behind innovation and value-added production.

Over the past 2-3 decades, many OECD countries have gone through several generations of policies aimed at strengthening the role of SMEs. Many countries have succeeded due to decentralized SME development strategies, others, especially small countries, have been able to boost SME competitiveness more centrally.

Some countries have focused more on promoting large enterprises, where SMEs have become followers rather than growth leaders. Others have focused mainly on promoting SMEs, creating high entrepreneurial competitiveness (for example, the German Mittelstand with its famous "hidden pioneers", which are highly specialized, export-oriented SMEs) [13].

In general, the term "small business" has become widespread only in English-speaking countries. In Western European countries, in Japan are more commonly used "Small and Medium Enterprises", [10, p. 193] in India and in another Asian countries are used the terms "Small-Scale Industry" [5, p. 36].

The concepts of entrepreneurship were first used in the 18th century by the English economist Richard Cantillon. According to him, an entrepreneur is a person with uncertain, volatile incomes, whose main function is to match supply in different commodity markets with demand [9, pp. 126-128].

Joseph Alois Schumpeter (1883-1950) was an Austrian-trained economist, economic historian, and author. He is regarded as one of the 20th century's greatest intellectuals. Schumpeter is best known for his theories on business cycles and the development of capitalist economies, and for introducing the concept of entrepreneurship. For Schumpeter, the entrepreneur was the cornerstone of capitalism—the source of innovation, which is the vital force driving a capitalist economy [4, p.44].

3. Research Methodology

Without business statistics, it is impossible to obtain accurate quantitative characteristics of the market

situations and conduct their research and forecasting. Without understanding the statistical structure

indicators of business statistics and statistical studies of quantitative characteristics of the market, any business can suffer serious damage. Only application of methods processing of statistical indicators, various data on the business climate should become the basis in shaping and improving economic policies and better understand development processes firms to assess its prospects.

In modern economic conditions, the role of entrepreneurship in economic development, and the development of statistical methodology for measuring and researching entrepreneurship is becoming a priority for most statistical offices and international organizations. However, although the role entrepreneurship in economic development is a topic for active discussion, there is lack of scientific data on entrepreneurship, the factors that determine it, and the impact on economy due to the lack of reliable and reliable statistical information.

One area that has seen a boom in recent years is business statistics, especially business statistics. business demography, which is the statistics of births, deaths and survival businesses, is a relatively new area of statistical products based on information from commercial registers.

In most countries, despite the lack of targeted programs to collect statistics on entrepreneurship, statistics are available at the national level for the purpose of monitoring various aspects of the business environment (for example self-employment statistics, business demographics and, although rarely, indicators based on combined data on individuals and enterprises or about enterprises from various sources).

However, in many cases the data produced by countries are not comparable across international level. The two main reasons for this are as follows:

a) National definitions of vital events differ from international ones.

For example, the Australian Bureau of Statistics (OSA) produces business demographic statistics in to help analyze business dynamics in Australia. While the methodology and definitions adopted for calculating the birth and death rates of enterprises are close to those recommended in the Guide Eurostat and OECD, due to differences, Australian data are not fully comparable with business demographic indicators in the harmonized database of OECD and Eurostat;

b) Use for data collection as statistical units of "organizations" instead of "enterprises". Several countries, such as Mexico and Japan, have such traditions of collecting business data through surveys and censuses of establishments. These

countries are taking considerable effort to produce business demographic statistics that would be consistent with recommendations of the Eurostat and OECD Guidelines. However, to obtain internationally comparable data can only be obtained by using the same accounting units.

4. Analyze

SMEs are one of the key factors in increasing the competitiveness of the Armenian economy, ensuring inclusion and sustainable development. The 2019 program of the Government of the Republic of Armenia largely uses SME development, which is considered a precondition for inclusive economic growth. The following strategic directions are prioritized by the Government of the Republic of Armenia to strengthen the SME sector

and increase competitiveness in the Republic of Armenia:

- Increasing the availability of financial resources;
- Capacity building of SMEs and development of business culture;
- Ensuring market access for SMEs;
- Providing a favorable institutional and legal environment for SME development.

In 2011, the definition of SMEs in the Republic of Armenia in terms of the average number of employees was defined in accordance with the definition of SME in the EU member states, according to which SME enterprises are classified for administrative purposes according to the following criteria:

Table 1. Definition of small and medium enterprises in Armenia [14].

	Average payroll number of the employees	Revenue generated from the previous year activities	Or the book value of assets as of at the end of the previous year
Micro	0-9	< 100 million AMD	< 100 million AMD
Small	10-49	< 500 million AMD	< 500 million AMD
Medium	50-249	< 1.5 billion AMD	< 1.0 billion AMD

In 2020, the number of SMEs operating in the Republic of Armenia was 68 780, of which only 126

(about 0.18%) were classified as large businesses. 52.1% of SMEs operate in Yerevan.

Table 2. Number of economic entities according to Economic Activity Classification Categories (EACC) and sizes of economic entities in 2020 [12, p. 6].

	Total	Micro-small		Small	Medium	Large
		Total	Don't have hired employees			
Mining and open pit operations	314	267	49	35	5	7
Manufacturing	6741	5837	1372	691	167	46
Supply of electricity, gas, steam and high-quality air	249	132	2	107	4	6
Water supply, Sewerage, Waste Management and Processing	83	63	14	17	-	3
Construction	1517	1120	85	313	75	9
Wholesale and retail trade, car and motorcycle repair	44093	42940	25917	998	133	22
Transportation and storage	1739	1489	514	205	34	11
Accommodation and public catering	4053	3444	796	532	72	5
Information and communication	2161	1817	444	288	45	11
Real estate-related activities	1764	1144	157	109	11	-
Professional, scientific and technical activities	3607	3369	1103	208	29	1
Administrative and auxiliary activities	1971	1747	452	171	48	5
Other services	488	475	241	12	1	-
TOTAL	68780	64344	31146	3686	624	126

As it can be seen from the table, in 2020 in the Republic of Armenia out of 68780 entities, only 3686 are small enterprises and 624 are medium

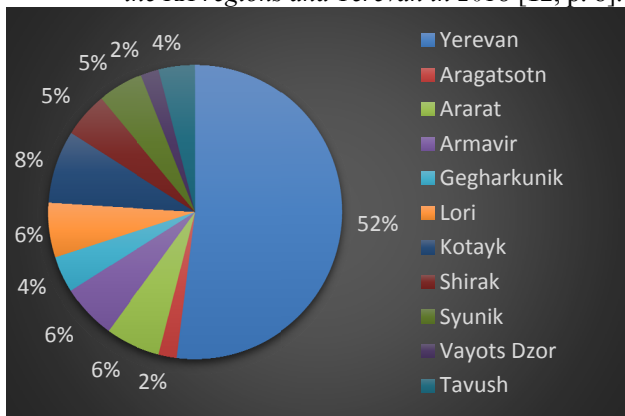
enterprises. Micro-small enterprises are much greater in number, particularly, 64344 out of 68780.

Table 3. Number of business entities by RA regions and Yerevan by size of business entities in 2020 [12, p. 7].

	Total	Micro-small	Small	Medium	Large
		Total	Don't have hired employees		
Yerevan	35753	32799	12967	2411	452
Aragatsotn	1780	1707	998	66	7
Ararat	4229	4043	2410	167	13
Armavir	3946	3780	2187	147	16
Gegharkunik	2764	2670	1577	89	4
Lori	4261	4087	2306	149	18
Kotayk	5901	5540	3088	284	66
Shirak	3237	3099	1263	121	15
Syunik	3179	3025	1707	133	18
Vayots Dzor	1228	1174	719	46	7
Tavush	2502	2420	1564	73	8
TOTAL	68780	64344	31146	3686	624

As it is demonstrated in the table, more than the half of the SMEs operate in Yerevan, particularly, 35753 entities out of 68780. As for the regions, the larger number of SMEs are located, appropriately, in Kotayk, Lori, Ararat and Armavir.

Figure 1. Structure of the number of business entities in the RA regions and Yerevan in 2018 [12, p. 8].



The need to develop small and medium enterprises in the modern world is one of the main imperatives for the reconstruction and development of national economies. It is the main guarantee of the establishment of market relations and economic progress. SMEs are the main driver of market economy development. It promotes private property, entrepreneurial skills, flexibility in a changing market economy, helps to diversify economic activity, can make a significant contribution to international trade, export promotion, and, of course, job creation. As a result, sustainable economic growth and the formation of a middle class are ensured. Developments in the high-tech market in recent years indicate that SMEs operating

in this field have a strong potential for cooperation with large corporations, even competing, forcing them to review their own management systems and policies to innovate. However, in current modern conditions, the development of SMEs activities in Armenia is affected by a number of obstacles. One of the first problems for the development of SMEs is the instability of legal framework. The instability of the legal framework forces to constantly change the activities of small and medium enterprises. For example, in all tax laws and in the instructions for their application, there are constant changes and entrepreneurs must always follow them independently and be aware of new changes at any time. In other words, entrepreneurs today are not sufficiently informed about the legal acts related to business, the changes that have taken place in them. Thus, it is necessary to intensify the work to raise the level of awareness of laws among entrepreneurs. Furthermore, frequent changes in tax legislation, incompleteness of tax system and systematization, existence of different forms of tax administration, ambiguity of tax legislation, short and inflexible tax payment deadlines, high costs of tax consulting are the main reasons for obstacles for high costs of the tax system for SMEs.

Meanwhile, the process of registering companies is easy, but there is a lack of information on the organization's legal status, the choice of tax regime, as well as the documents submitted to the State Revenue Committee. The following areas were identified as problem areas for tax administration (including high income tax rates) according to the research done by Armenian Business Coalition [1]:

- The extent of income tax and vacation payments;
- Difficulties regarding to developing and submitting tax reports;
- Difficulties of cooperation between VAT paying and turnover tax paying enterprises;
- The same norms related to personnel policy and work formulations.

It is to state that the formation of a favorable legal framework is slow but stable in Armenia and there are some positive trends in this regard. Nevertheless, according to the reports of "Doing Business" by World Bank, in 2020 Armenia ranked 47th among 190 countries in terms of freedom of doing business [3], which is a downturn compared to the previous year (Armenia ranked 41st among 190 countries). It is worth to emphasize that ensuring access to finance, particularly borrowings in terms of loans, is a prerequisite for SMEs development. Banks avoid SMEs lending due to lack of guarantees. However, business lending is very important for the development of the economy. Banks consider this group of borrowers to be relatively high-risk, inefficient, and provide them with mainly short-term loans with high interest rates, in case that they have collateral. That is why SME lending is mostly done through international programs. Difficulty of getting loans, high guarantee and collateral requirements make the lending process simply impossible, especially for start-ups, micro and small organizations. In this regard, availability of financial resources is one of the important preconditions that allows SMEs to expand their activities, introduce new technologies, which will lead to operational efficiency, will allow to produce competitive products, and in case of export, to be competitive in international markets. In the case of foreign currency loans, SMEs are vulnerable to foreign exchange risk, as long-term loans are mainly provided in foreign currency. Awareness of the products offered by banks is not high, which can lead to the entrepreneur choosing an inaccessible product. Acquiring equipment through leasing from the primary market alone is an unnecessary financial burden for SMEs, as is the need for collateral for leasing in the event of interest rate subsidies.

In Armenia, SMEs have significant obstacles regarding to export procedures. According to the research done by Armenian Business Coalition the respondents need the following kind of support related to export:

- Assistance in establishing contacts with business partners and representatives in foreign markets;
- Assistance in participating in business forums, exhibitions and other events;

- Co-branding (combining products of several small manufacturers under one brand);
- Certification for the exporting country or compliance with the legal requirements of the exporting country;
- Assistance in cargo transportation and other logistics services;
- Receipt / collection of payments for the sold product;

It is worth to highlight that capacity and skills of SMEs are considered to be the factors that determine the opportunity for enterprise development and growth. Necessary knowledge and skills can be acquired through appropriate consulting or training, if the latter are really the reflections of the needs of the business, thus, ultimately, they enable the entrepreneur to develop their own businesses. The unavailability of consulting services for the given subject limits the enterprise's ability to develop skills, the latter will depend mainly on the free courses offered. In this context, it is worth adding that entrepreneurial capacity is generally assessed as unsatisfactory by start-ups. The enterprises engaged in high-tech, implementing innovative investments and using information technologies are considered priorities for the Armenian economy. However, for some small businesses, such activities are almost inaccessible. Other problems of SME development can be considered exchange rate fluctuations, unpreparedness of those wishing to establish SMEs, insufficiency of material base, finding customers and partners both local and international, high prices of raw materials, unprofitability of production, unfair competition, market imperfection, distrust of foreign partners, difficult to enter foreign markets, etc.

5. Conclusion

The aim of this paper was to examine the current trends of small and medium enterprises in the Republic of Armenia. To achieve this aim, we have investigated from two standpoints. In terms of this, both quantitative and qualitative approaches are used. The quantitative approach was used by analyzing the statistics of small and medium enterprises in the Republic of Armenia, in order to identify the main trends and directions SMEs development. In terms of qualitative research, the case of "EU4Youth: Employability and Stability in Armenia, Belarus and Ukraine" project's "Entrepreneurship" component was used to identify the extent regarding to some constraints the businesses face, such as access to finance, entrepreneurial knowledge and skills, ongoing consulting and coaching, etc.

In this regard, it was identified that most SMEs need necessary entrepreneurship education, capacity building, especially, when it comes to new approaches and technologies, marketing and financial management and optimal use of financial instruments. This problem is one of the most common causes of many companies shutting down. Business capacity building companies, associations, NGOs, and other donor-funded organizations often have a local, narrow and temporary budget. Most of the services are not sufficiently tailored to the business needs of the customers, in other words, they are general in nature, which reduces the effectiveness of such support. In other cases, when such services are provided on a paid basis, they are often simply not available, especially for companies with small and still very limited cash flows. Furthermore, inclusive and equal access to state-sponsored education services for all SMEs, is still problematic. Inclusiveness and equal access to education services are important for all SMEs. It is noticed that the educational programs are implemented effectively, but they are incomplete in terms of inclusion, as such courses are attended mainly by the same entrepreneurs. It is worth to mention the contrary side of this such as some SMEs participate in training only formally to benefit from grants at the end of the course. On the other hand, business plans written as a result of trainings are not important for entrepreneurs in terms of further planning of their businesses and are only aimed at attracting loans or grants. In developed countries, the SME sector is financed not only through banks, but also through alternative financing through venture capital institutions, networks of "business angels", etc. Venture capital companies and business angels in Armenia are not sufficiently developed. International experience shows that a well-designed and well-established legislative framework is particularly important for the effective use of alternative SME financing tools. Specifically, the collection of statistical data on the SME sector by gender segregation is incomplete, which does not allow to get an idea of the involvement and role of women in this sector. Most women's businesses are not just individual or micro-level enterprises, but they also occupy certain areas, focusing on trade, services and small-scale production, often home-made products. Despite the work done and the progress made, the women entrepreneurship sector still remains vulnerable and there are a number of areas that need to be addressed when developing a new SME development strategy. Specifically, science and private market connection is also poorly developed. Scientific knowledge remains in the theoretical realm and does not become a product. This problem

is more or less solved only in the IT sphere. There are scientific institutes - private and unique cases of private sector cooperation, but the systemic approach is still lacking. It is worth to mention that the introduction of new technologies, which can increase the competitiveness of SMEs, is not available as on the one hand, the introduction of such technologies requires financial resources, the involvement of which at the expense of credit means is expensive due to the high interest rate, on the other hand, the sector is risky. Some banks provide leasing funds for the introduction of such technology. Importing technologies is not available for SMEs and in this case large entrepreneurs can mainly afford it. State support for the introduction of innovative technologies was assessed as insufficient. The small size of the market also hinders the introduction of innovative technologies. At the same time, there are grant programs for the introduction of innovative technologies, which are implemented by the EU, donor organizations and other stakeholders through grant programs which are still few and insufficient. Particularly, improving the business environment, increasing access to finance and significantly increasing the efficiency of companies by reviewing tax/customs regulations, payment volumes and administration, eliminating unjustified privileges of individual companies/monopolies in the import/export sector can be significant for internal and external competitiveness of SMEs. Of particular importance are investments in ensuring the high quality of products/services, and especially the collection of regular and reliable information on foreign markets. In fact, the efforts made in this regard, including by the state, are still insignificant as awareness of SMEs on export procedures and work in this area is incomplete. It is important to improve SME policy framework by making additional efforts to boost exports to major economic blocs (including the EU) and to take advantage of trade opportunities in regard to Armenia's membership in the Eurasian Economic Union (EEU). On the other hand, in the context of the development of the SME sector, significant improvements have been made to the operating environment by simplifying company registration processes and expanding e-government services

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Сдана/Հանձնվել է՝ 06.07.2022

Рецензирована/Գրախոսվել է՝ 20.07.2022

Принята/Ընդունվել է՝ 27.07.2022