



**SME SUPPORT POLICIES IN TURKEY AFTER 1990
(REVIEW, EVALUATION AND SUGGESTIONS)**

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This study, which was presented at the 2009 “Turkey Small and Medium Enterprises Development Conference” held in Istanbul on the 9th and 10th of April 2009, is aimed at catalyzing the debate on the issues relevant to the SME sector in Turkey.

The views expressed in this publication are those of the author and do not necessarily reflect the official policy or position of the French Development Agency (AFD).

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LIST OF ABBREVIATIONS AND ACRONYMS

EU	European Union
AFD	<i>Agence Française de Développement</i> / French Development Agency
EIB	European Investment Bank
CEB	Council of Europe Development Bank
SPO	State Planning Organization
DTM	Undersecretariat of Foreign Trade
GEM	Global Entrepreneurship Monitor
IBRD	International Bank for Reconstruction and Development
İGEME	Export Promotion Center
ILO	International Labour Organization
IRC	Innovation Relay Centre
JBIC	Japan Bank of International Cooperation
KfW	German Development Bank
KGF	Credit Guarantee Fund
SME	Small and Medium-sized Enterprise
KOSGEB	Small and Medium Sized Industry Development Administration
KSEP	SME Strategy and Action Plan
KSS	Small Industrial Estate
KÜSGET	Directorate General of Small Industry Development Organization
MEKSA	Foundation for the Promotion of Vocational Training and Small Industry
NUTS	Nomenclature of Territorial Units for Statistics
OECD	Organization for Economic Co-operation and Development
OSB	Organized Industrial Zone
SDTŞ	Sector specific Foreign Trade Company
NGO	Non-governmental Organization
TEKMER	Technology Development Centre
TKB	Turkish Development Bank
TSKB	Turkish Industrial Development Bank
TUİK	Turkish Statistical Institute
TUSİAD	Turkish Industrialists and Businessmen Association
TEYDEB	TÜBİTAK Technology and Funding Programs Directorate
TOBB	Union of the Chambers and Commodity Exchanges of Turkey
TOSYÖV	Turkish Foundation for Small and Medium Businesses
UNDP	United Nations Development Programme
YOİKK	Coordination Council for the Improvement of Investment Environment in Turkey

I. INTRODUCTION

I.1. Introduction, objective and scope

In the historical process, any incident or development that occurs in the economic, political, social or cultural fields shows its impact in the other fields sooner or later, like the acceleration of the globalization process with the influence of technological progress.

The World economy is changing into a different structure in this process. On one hand we are suffering from financial crises that is gradually encompassing all the world economies due to the integration of financial markets, and on the other, we can witness that the attitudes of consumers and producers are changing constantly on the real economy side. People living in one part of the world are now able to get information about the people and incidents in the rest of the world thanks to the development of communication tools. Thus the consumers' demands become diversified day by day and can change at any moment.

This transformation in consumer demands naturally makes its presence felt in the supply side of the markets. Today, the producers should be able to have more flexible structures of production and respond simultaneously to changing market conditions. Therefore we can see that small and medium enterprises are increasing their dominance in the world economy against large enterprises whose scales are suitable for mass production alone.

In short, small and medium sized enterprises (SMEs) have positive impacts on the development of a country's economy on the regional basis not only by immediately adapting to changing conditions, but also by positively affecting competition with their dynamic structures and creating employment opportunities and added value.

SMEs in Turkey suffer from many problems in spite of their undeniable size in the Turkish Economy with respect to macro economic indicators. The most important of them are the financial problems. If SMEs can have a greater and more effective share in the banking and total financial systems, their contribution to the economy will certainly increase.

SMEs have been selected as The theme of the Conference to be held by the French Development Agency (AFD - Agence Française de Développement) in collaboration with Dünya (daily newspaper) on April 9th and 10th, 2009. Such issues as SME-large enterprise linkages, examples of good practice aimed at supporting SMEs, corporate social responsibility and integration of SMEs within regional economies will be discussed at different sessions of the conference.

This report aims to present a broad range of opinions which will support the theme of the Conference. The main issue to be discussed in this respect will be the Public Policies and State Aids for SMEs in Turkey after 1990. The report provides an analytical summary of these policies and presents policy and strategy recommendations based on the results of this analysis towards sustainable development of SMEs in Turkey.

I.2. Approach and methodology

Country-level policy and strategy documents and action plans together with related laws and regulations were taken as the basis for making a historical and analytical examination on SME support policies in Turkey after 1990. Implementation data were also utilized to the extent that they were available for evaluation. The reference documents which were examined for this purpose are as follows:

- A) Policies and strategies
 - Five-year and eight-year development plans
 - SME Strategy and Action Plans (KSEP)
 - European Union pre-accession plans
- B) Action Plans and implementation documents:
 - SME Strategy and Action Plans
 - State Aid regulations
 - Supports provided by KOSGEB and other relevant institutions
- C) Implementation and evaluation reports
 - Analysis reports prepared by such institutions as the World Bank, OECD, UNDP and ILO
 - The "investment environment" reports, prepared by various national and international institutions
 - European Union Progress Reports
 - SME incentive statistics

The lack of systematically established data and monitoring and impact assessment studies to facilitate an analytical examination of the policies and supports for SMEs in Turkey after 1990 is the most important constraint of this study. Therefore this study examines the change and development of policies and supports in the course of time and presents evaluations and recommendations in the light of these observations which are further supported with international comparisons and personal experiences.

In order to facilitate the comparison with international practices, a general picture of SME support policies (based on the world and EU practices) is introduced in Chapter II. Whereas Figure 1 provides a general framework, subsequent paragraphs show more detailed information about certain categories of support policies.

It has become apparent that it is impossible to make a detailed analysis for Turkey with respect to all of these categories within the limits of this study. For this reason, while screening the above-listed references, the focus was placed on the investment incentives and SME development supports. Chapter III consists of the findings and evaluations on these issues.

Chapter III includes general SME statistics for Turkey, a list of major support institutions, activities of these institutions and the policies and aids implemented after 1990. Chapter IV lists our policy and strategy recommendations.

As mentioned in Chapter II.1, this study deals with the policies aimed at developing the existing SMEs only. Prospective entrepreneurs with the potential and willingness to build up their own businesses have been excluded from this study. It is thought that it would be necessary to carry out a separate evaluation work on the SME policies and supports which are not covered by this study and the policies and supports directed at potential entrepreneurs who, we believe, are a very important group for the economic and social development of Turkey.

II. GENERAL SME SUPPORT FRAMEWORK

II.1. Economic growth and SMEs: GEM Dynamic Approach

The entrepreneurship conceptual model adopted by the Global Entrepreneurship Monitor (GEM) is shown schematically in the diagram below. This model considers that national economic growth is the result of two parallel sets of interrelated activities: those associated with established firms, and those related directly to the entrepreneurial process. The below diagram shows that these two groups of activities are interrelated, and it summarizes the conditions necessary for the development of these activities. Policy actions towards this aim are listed in the boxes numbered 1, 2 and 3 which summarize the macro policies, infrastructure conditions and support programs required for developing SMEs.

As mentioned above (see Chapter I.2 Approach and Methodology), the subject of this study is limited to the box numbered 2. But the issues mentioned in the boxes numbered 1 and 3 have also been referred to in the stages of examination, evaluation and recommendation.

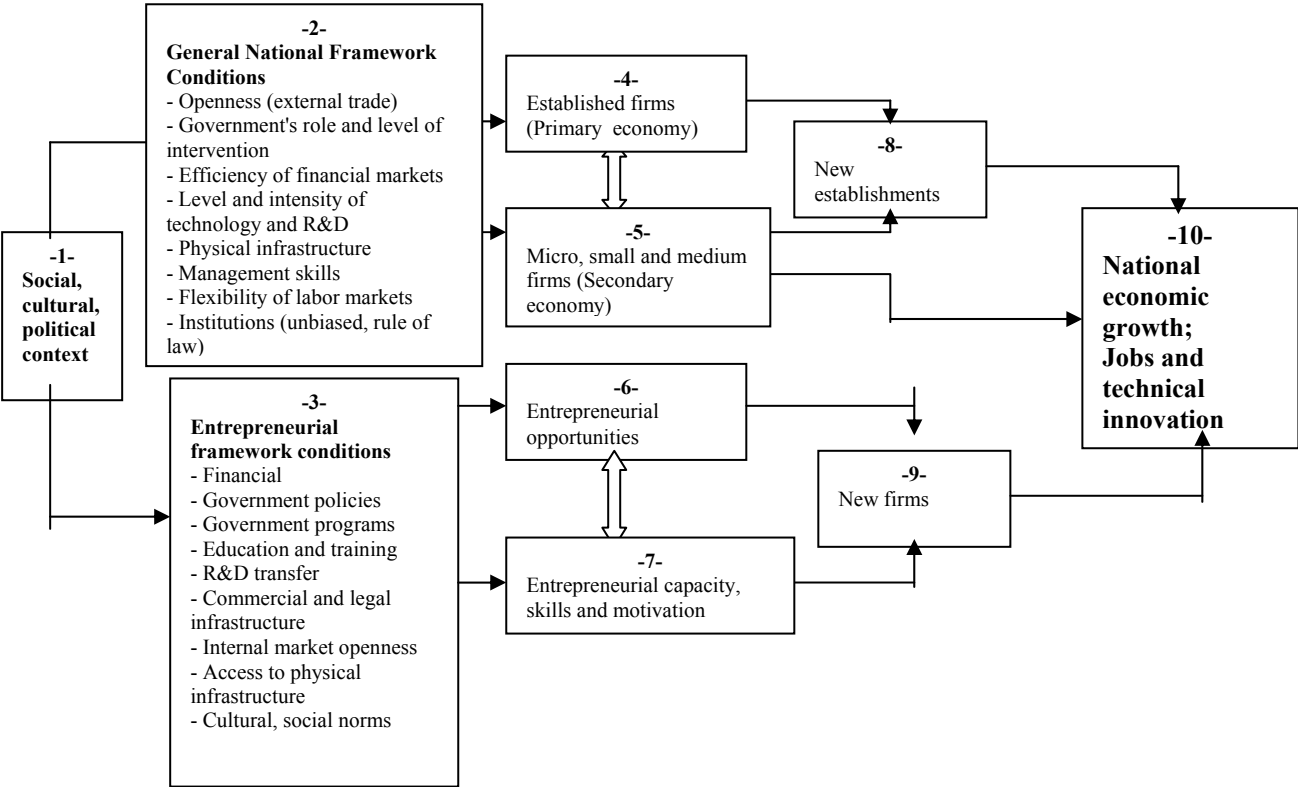


Figure1. GEM Conceptual Model (see GEM 2004, Executive Report page16)

II.2. General Classification of SME policies and supports

After examining the European Union's approach (the Bologna Charter, Small Business Act, etc.), along with the general framework which is shown by the box numbered 2 in Figure 1, it is possible to make the following general classification of SME policies and supports.

- A) Improving the environment conditions in which SMEs operate
 - Legislation
 - Competition policies
 - Tax policy
- B) Developing the human resources
 - Life-long education
 - Harmonizing education with labour market needs
 - Encouraging entrepreneurship
- C) Facilitating the growth and development of SMEs
 - Promotion of investments
 - Access to finance
 - Support for technology, R&D and innovation
 - Access to technology and market information
 - Widespread use of electronic trade
 - SME Clusters
 - Environment and energy

II.3. General Framework of SME policies in the EU

The number of small and medium sized enterprises which are considered to be the most important source of sustainable development and employment in the European Union is nearly 23 million, constituting 99% of entire enterprises. EU SMEs provide jobs for nearly 100 million people. The following table shows the EU definition criteria for SMEs (the quantitative criteria).

Table1. EU Definition of SMEs

	Definition Criteria	Micro Sized Enterprise	Small Sized Enterprise	Medium Sized Enterprise
EUROPEAN UNION	Number of employees	≤10	≤50	≤250
	Annual Turnover	≤2 Million Euros	≤10 Million Euros	≤50 Million Euros
	Annual Balance Sheet Total	≤2 Million Euros	≤10 Million Euros	≤43 Million Euros

In addition to the quantitative criteria mentioned above, there is an “independence criterion” according to which an SME can have a 25% maximum holding of the capital in one or more enterprises and/or an outsider can have a 25% maximum stake of in an SME.

The political leaders of the EU, during the Lisbon Meeting which was held in 2000, adopted a strategy to become the most competitive economy in the world within 10 years. The strategy aims to create more and better employment opportunities to ensure sustained economic growth. In line with this strategy, the EU and member countries are trying to establish certain measures which would make it attractive to set up new enterprises, and they are improving the environment conditions in which enterprises operate. In addition to this, they are implementing various mechanisms to develop the creativity of SMEs. Consultations with SME stakeholders are held in order to involve them in the policy making process. The "Think Small First" principle envisages that potential effects of plans, policies and legislation on SMEs must be evaluated before taking an action. The Commission adopted the Small Business Act (SBA) in 2008. The Act, which is planned to be implemented

following the summit in December 2008, is actually a comprehensive document of policy and action. This document covers the following principles concerning the establishment and implementation of SME policies:

- Create an environment in which entrepreneurs can thrive and entrepreneurship is rewarded.
- Ensure that honest entrepreneurs, who have faced bankruptcy, can quickly get a second chance.
- Decrease administrative burden.
- Develop e-government and one stop shop models.
- Facilitate SMEs' participation in public procurement and increase their use of State Aids.
- Facilitate SMEs' access to finance.
- Help SMEs to benefit more from the Single Market.
- Promote the upgrading of skills in SMEs and all forms of innovation.
- Enable SMEs to turn environmental challenges into opportunities.
- Encourage SMEs to benefit from the growth of markets in the emerging countries.

Articles Numbered 87 and 88 of the European Community (EC) Treaty constitute the legal basis of the state aids for SMEs in the EU. According to Article 87(1), state aids are incompatible with the concept of a "Common Market" in essence. Nevertheless, it doesn't prohibit the aids completely, but allows the exercising of state aids in accordance with Articles Numbered 87(2) and 87(3) in certain cases (exceptions). These exceptions are as follows:

- (a) Regional aids
- (b) Other horizontal rules
- (c) Sector specific rules
- (d) Specific aid instruments

(a) Regional Aids: Article 87 (3) (a) of the Treaty applies to State aid to promote the development of "areas where the standard of living is abnormally low or where there is serious underemployment". The NUTS-2 regions, where Gross National Product (GNP) per capita is lower than the EU-25 average by 75%, are covered by this category. For the period 2007-2010, regions with less than 75% of the EU-15 average GDP/capita are also eligible under this article.

(b) Other Horizontal Rules: The Commission's frameworks or block exemption regulations are applied to the following categories of aid:

- State aids for SMEs
- Aid for R&D and innovation
- Aid for climate change and environmental protection
- Aid for risk capital
- Aid for the rescue of firms in difficulty
- Aid to employment
- Training aid
- Aid for services of general economic interest

SME policies and supports within the EU countries are prepared and implemented by considering the above-mentioned acts, rules and approaches.

III. GOVERNMENT POLICIES AND SUPPORT SCHEMES AIMED AT SMEs IN TURKEY AFTER 1990 (REVIEW AND EVALUATION)

III.1. General Information on SMEs in Turkey

Turkey's definition of SMEs which was aligned with the EU definition is given below.

Table 2. Turkey's definition of SMEs

	Definition Criteria	Micro Sized Enterprise	Small Sized Enterprise	Medium Sized Enterprise
TURKEY	Number of employees	0-9	10-49	50-249
	Annual turnover	≤1 Million TL	≤5 Million TL	≤25 Million TL
	Annual Balance Sheet total	≤1 Million TL	≤5 Million TL	≤25 Million TL

In order to align the SME definition of Turkey with the EU definition, the quantitative criteria of the Union were taken as the basis. Whereas the same criteria for the head-count were adopted, annual turnover and balance sheet limits were reduced to nearly one-fourth of the limits set by the Union. Regarding the qualitative criteria (independence) the word “large enterprise” of the EU definition was replaced by “public institution” in the Turkish version. In our opinion, it would be better if “large private enterprises” were added to the restricted category beside the public institutions. It would also be more convenient to use Euros for identifying the turnover and balance sheet limits which is the official currency of the EU. In fact, it would have been more suitable for Turkey, which has just started the process of EU membership, to use exactly the same EU criteria in its official SME definition. We believe that this would have been more beneficial both in terms of harmonization with the EU policies and adhering to the idea of EU membership in Turkey.

The EU definition is quite flexible since it is an umbrella definition under which various other definitions can be made for specific purposes. It is clearly indicated in the official documents that the SME definition of Turkey is also an umbrella definition.

According to TÜİK data (2002)¹, SMEs in Turkey have a share of 76.7% in total employment, 26.5% in investments and 38% in the value added. A share of 76.7% in employment against a share of 38% in the value added indicates that employee productivity level of SMEs is very low in Turkey. As the size becomes smaller, this situation gets worse. The table below shows the distribution of enterprises in Turkey with respect to their size (TÜİK 2002).

Table 3. Classification of enterprises with respect to size (TÜİK 2002)	Number of Enterprises (All Enterprises)	%	Number of Enterprises (Manufacturing Industry)	%
Only the enterprise owner	23,762	1.38	1,509	0.61
1-9	1,633,509	94.94	220,030	89.12
10-49	53,246	3.09	20,325	8.23
50-99	5,080	0.30	2,453	0.99
100-150	1,804	0.10	946	0.38
151-250	1,387	0.08	719	0.29
251+	1,810	0.11	917	0.37
Grand Total	1,720,598	100.00	246,899	100.00

¹ Latest officially published data

The above table shows that the share of large enterprises is only 0.11% when all the enterprises are counted and it is 0.37% when the manufacturing industry is taken as the basis. The largest share, on the other hand, belongs to the 1-9 employee group.

III.2. Main problems suffered by SMEs in Turkey

The problems suffered by SMEs in our country can be summarized as follows. Recommendations for eliminating these problems are presented in Chapter V.

- Integration of entrepreneurship, management and ownership functions in one person: it is only a coincidence that a person having the required financial resources has, at the same time, good entrepreneurial and managerial skills.
- Lack of research and planning work: Lack of strategic plans and market surveys based on specific targets, ignorance of the real needs of the clients and widespread belief that “whatever is produced can be sold” are the main reasons for SME failures. This has its roots in the long lasting import substitution policy of Turkey which has only recently been abandoned.
- Lack of information about innovations: In this respect, cooperation of SMEs with universities and other research institutions is vitally important.
- The process of growth: within their life cycle, SMEs pass through the start-up, survival, growth and maturity phases. It is observed that especially in the second and third phases of this cycle, SMEs have very high rates of failure. The value of consultancy, especially for micro enterprises, is very high during these phases.
- Institutionalization: This is an important bottleneck of Turkish SMEs, the problem being more severe for the micro and small enterprises. Enterprise owners have recently gained a deeper awareness of the issue. This is reflected by the prevalence of “family business related topics” in recent meetings and conferences. Almost all the enterprises in Turkey aged over 100 years have remained in the small size bracket. This evidently shows the existence of problems related with institutionalization and the difficulty of involving second and third generations in the business.
- Partnership relations: Another important bottleneck suffered by the Turkish SMEs concerns the issue of partnership relations. There are rare examples of smoothly running partnership relations in Turkish SMEs. The main reason behind this is that partnerships are generally established among siblings, relatives, friends and fellow citizens. Also the cooperation potential among SMEs which can create complementary synergy for them is not utilized to the required extent.
- Lack of qualified employees: This problem needs to be tackled through necessary arrangements and active labour programmes.
- Financing: The most important factors complicating the access of SMEs to financial resources are the lack of information and the difficulties encountered in finding sufficient collateral. Innovative models aimed at solving these problems need to be implemented urgently.

III.3. Policies and plans aimed at fostering the SME sector in Turkey

Five-Year Development Plans

When we examine the economic history of Turkey, we can see that two five-year plans which were prepared before 1960 (during 1930s) were prepared only to discipline the public investments in a rational way. Moreover, as there were no specific programs towards the implementation of these plans, it can be hardly said that this period in Turkey was a "Planned Period." In this period, public investments were used as a tool to cover the areas left unattended by the private sector and industrial policies that were based on import substitution and infrastructural investments were given priority. As

of from 1960, the emphasis was placed on the preparation and implementation of development plans to accelerate economic, social and cultural development and to ensure rational public intervention in the economy. Towards this end, The State Planning Organization (SPO), attached to the Office of the Prime Minister, was established on September 30th, 1960. During the period between 1960-1980, an import substitution policy was followed to develop the private sector. After 1980, the process of liberalization and establishment of all the tools and institutions of a free market system were accelerated.

The first four plans which were prepared after 1960 cover the period between 1960-1984. We observed that the concept of small and medium sized enterprises (SMEs) and SME plans were brought up to the agenda with the Fourth and Fifth Five-year Development Plans.

The Fourth Five-year Plan displays an effort to make a definition of “small industry”, as shown by the following statement inserted in the plan (Section 6, page 279): “Studies for defining the basic properties of three sub-sections of small industry (small industry, artisans and craftsman/handicraft businesses) will be started in the first year of the Plan. Necessary legal arrangements will be completed so that the old (and still valid) definitions are replaced by a new ones” The fourth plan also states that the establishment process of small industrial zones will be accelerated and support will be provided in order to develop the technical and management capacity of small industry businesses. Moreover, it states that small industrial enterprises will be encouraged to organize within cooperatives or companies against the problem of remaining at the level of a single-person business. The Plan also indicates that public investments will be made to enable small businesses to attain economically viable scales.

An interesting point in the Fourth Plan is that it associates small enterprises only with the industrial sector. The plan also states that “scale related problems” can be solved by getting organized under the umbrella of cooperatives.

The Directorate General of Small Industry Development Organization (KÜSGET) was established in 1983 to reinforce the technology and management capacities of small enterprises. The efforts aimed at finding a common definition for small and medium sized enterprises had continued for a long time during which related institutions implemented their services according to their own definitions. This situation did not change after the Law numbered 3624 which established KOSGEB (Small and Medium Industry Development Organization), came into force. According to this law, enterprises operating in the manufacturing industry with a maximum of 150 employees are counted as small and medium sized businesses. The new SME criteria identified by the Council of Ministers Decree (dated November 18, 2005 and numbered 2005/9617), which aligned the definition of SMEs with that of the EU, were already presented in Chapter III.1 above.

In the Fifth Five-year Development Plan (1985-1989) small industrial enterprises are placed in the same category with artisans/ craftsmen, and it is indicated that state incentive policies will be implemented in such a way that small enterprises can be linked in a more effective way to medium and large enterprises as their subcontractors. In the Plan, the section related with the financing policies sets forth the objectives to increase credit facilities of Halkbank and to enable small industry businesses/artisans/craftsmen to get a greater benefit from these credits. Employment targets are also based on the development of small businesses which are considered to have a capacity to exploit local potentials to generate employment. The principles aimed at supporting the artisans/craftsmen and the small industries are stated in the Plan as follows:

- Encourage this sector to increase their productivity and develop their marketing skills in domestic and foreign markets.
- Develop a definition for artisans and craftsmen.
- Identify specific industry branches with priority for development.
- Develop incentive policies so that small enterprises can be linked, in a more effective way, to medium and large enterprises as their subcontractors.

- Increase the number of small industrial zones and establish a training system within these zones through which informal technical training and on-the-job training can be offered simultaneously.
- Help small enterprises to get organized under associations to be able to increase their production potentials.
- Ensure that necessary training arrangements are in place to meet the qualified manpower need of small enterprises.
- Carry on the studies which were initiated in order to obtain the statistics (necessary for preparing public policies for this sector) in a timely and healthy manner. Ensure that the State Statistics Institute collects business census information every year.
- Increase the opportunities to provide inexpensive-public funded investment and working capital loans for this sector.
- Encourage the establishment of small industrial estates in the areas where organized industrial zones exist.

As it is clear from the above statements, the Fifth Plan considers small industry businesses as the subcontractors of medium and large industries and looks at support mechanisms from this perspective. Identifying priority businesses (branches) appears to be an interesting approach and how this was reflected in the state incentives (or whether it was not reflected at all) will be discussed in the related section of this report (Investment Incentives). KÜSGET's activities were expanded and spread during the Fifth Plan period.

Chapter 14 of the Sixth Five-year Development Plan (1990-1994) which explains the principles and policies about artisans, craftsmen and small industry combines these three groups under the category of "small enterprises". The following goals are stipulated in the plan:

- Increase the technological level, productivity and competitive power of the small industry sector.
- Concentrate small industrial estates at locations where there is a potential for the development of small industries.
- Encourage integration of small industries with medium and large industries.
- Organize small enterprises under the roof of associations.
- Provide entrepreneurship training for small enterprises mainly in the subject of finance.
- Encourage technology-intensive small enterprises within the context of technoparks.
- Benefit from the employment generation potential of the small industry sector.
- Increase the volume of inexpensive loans available for small businesses, develop a system by which project-based loan applications are evaluated and accepted without requiring collateral.

It is seen that there is still an ambiguity related with the concept "small enterprise" in the Sixth Plan. Although the terms "small business" or "small enterprise" were occasionally used instead of "small industry", these terms in fact refer to "small industry". Service and trade businesses are not seen as a part of the small enterprise sector which needs to be supported. The plan also deals with the concepts "technology-intensive small enterprises" and "entrepreneurship training". But the association of entrepreneurship training with finance training shows that entrepreneurship training is not viewed in its contemporary sense but as traditional management training.

Within the Sixth Plan Period, the Small and Medium Industry Development Organization (KOSGEB) and the Credit Guarantee Fund Inc. (KGF) were established (1990 and 1991 respectively) and formerly established KÜSGET was incorporated into KOSGEB. KGF is currently being funded by KOSGEB, TOBB, TESK, HALKBANK, MEKSA and TOSYÖV. The establishment of these institutions is an important step towards achieving the goals listed in the Plan. The importance of KGF² for SMEs has been better appreciated after the latest global economic crisis. We can envisage that the number of credit guarantee institutions will increase in Turkey in the upcoming years and these institutions will be supported with greater resources.

The Seventh Five-Year Plan (1996-2000) emphasizes the employment creation capacity of SMEs and mentions the failure of SMEs to allocate sufficient funds for training. The Plan also puts forward the fact that there is a decrease in the level of employment created by large manufacturing industries whereas an increase is observed in the employment level of SMEs. It is also indicated that 230,000 additional jobs will be created upon the establishment of small industry estates proposed in the Investment Plan of 1995. The Seventh Plan covers the following findings and defines the following goals:

- With the development of high value added sectors based on advanced technology, the employment of a qualified workforce will grow. The employment potential of small and medium sized enterprises will be utilized at the maximum level.
- Entrepreneurship training programmes will be implemented and small and medium sized enterprises and entrepreneurs will be supported in the fields of project planning, finance, organization and technology. Enterprises with a potential to gain a competitive edge by utilizing local resources will be assisted with development.
- Viable projects in the production sector with employment creation capacity will be supported by a flexible and effective unit (government department) to facilitate their implementation. In this respect stock farming, carpet weaving, fisheries etc. Will be supported.
- Small and medium sized enterprises suffer from persistent problems in the fields of finance, research, product and quality improvement, marketing, technology and productivity. KOSGEB has not been able to attain the desired level of effectiveness in the delivery of its services which are delivered through its 38 local branches.
- 31.4% of the incentive certificates issued for completely new fixed investments between 1992-1994 was obtained by small and medium enterprises.
- Integration of small and large industries will be facilitated.
- Small and medium sized enterprises will be supported and developed by a special programme against the adjustment problems that could be encountered by them during the process of Customs Union. The Venture Capital System and Credit Guarantee Fund will be activated and Research and Development activities will be encouraged.
- Establishment of multi-partner export companies will be supported to enable small and medium sized enterprises to produce goods conforming to international quality standards.
- A programme will be prepared by KOSGEB to train new entrepreneurs in the fields of technology development and management techniques to provide consultancy for these entrepreneurs and to facilitate their access to finance.

² KGF which was established in 1990 and which is currently the single credit guarantee institution of Turkey has the following shareholder composition : TOBB (50.99%), KOSGEB (48.54%), TESK (0.43%), HALKBANK (%0.02%), TOSYÖV (0.01%), MEKSA (0.01%). Its registered capital is 79 million TL and its transaction volume is 300 million TL. KGF covers up to 80% of the guarantees required by the lending banks. The amount of guarantee for a single SME can not exceed 750,000 TL. After the global crisis, the importance of KGF for SMEs was further recognized, and this prompted actions towards restructuring the KGF. In its new structure, it is envisaged that the shares of TOBB, KOSGEB and TESK will be decreased and 20 banks operating in Turkey will gain a total share of 33.33%. Its capital will be increased to 240 million TL and the Treasury will pump 1 billion TL into the fund. With its new structure and funds, KGF will create a loan volume of 10 billion TL through which at least 20,000 SMEs will benefit from the system.

- Efforts will be utilized to ensure an extensive use of TS-ISO 9000 quality system documentation by small and medium sized enterprises.
- Small and medium enterprises will be informed about patents, licenses and utility models which are the tools which will become operational after the draft Patent Law is enacted.
- State Incentive System legislations will be collected under a single law which will be developed to minimize bureaucracy in compliance with the GATT and EU rules and to exercise a smaller number of instruments with greater efficiency. Incentive policies will be designed with due regard to the objectives of job creation, development of SMEs, environmental protection, development of priority regions, and the structural adjustment required by the Customs Union.

When we examine the Seventh Plan, we can see that the term “small enterprise” is replaced by “small and medium sized enterprises”. These enterprises have a more distinctive place in the objectives and policies and there are efforts to integrate them into the State Incentive System, but it is understood that, in fact, “manufacturing industry enterprises” are implied by the definitions “small enterprise” and “small and medium enterprise”. It is frequently emphasized in the Seventh Plan that small enterprises have a capacity to generate employment and they must be supported for this reason. However, their capacity to develop technology and innovations is overlooked although an objective is set forth to increase the awareness of SMEs about patents, licences and utility models. An interesting point in the Plan is the recognition of small agricultural and handicraft businesses as important sectors representing SMEs. This shows that setting the limits of SME definition and segmenting SMEs accordingly are not an issue of concern yet. However we need to examine the implementation side (incentive regulations etc.) to see whether there exists such an effort. For example, the stated need for developing venture capital companies can hardly be associated with the above mentioned micro and small business activities.

The Plan also indicates that KOSGEB has not been able to reach the desired level in the delivery of its services. It is necessary to examine the technical reports –which are assumed to exist- to understand what is meant by the “desired level” and which proxies were used to measure this level

“Entrepreneurship” and “new entrepreneur” seem to be the emerging concepts in the Seventh Plan. This is parallel to the awareness and policy approach which became evident at the international level, particularly in the EU during that period.

The Eighth Plan (2001-2005) points out that, as of 1999, SMEs account for 99% of the enterprises in the industrial sector and 55.9% of employment whereas they have a share of 24.2% in the value added and 5% in the bank credits. In the section entitled “State Aids for Investments”, it is indicated that the resources allocated for incentives (including those for SMEs) remained insufficient during the Seventh Plan period, the legislation changed too frequently, and there was excessive bureaucracy and a lack of coordination among the institutions which delivered state aids. In the section related with the priority regions, it is stated that enterprises holding an investment certificate are entitled to benefit from such investment tools as “exemption from customs duties and fund levies”, “exemption from VAT” and “investment allowance” in addition to investment and operating capital loans for SMEs. The Plan also states that the employment generation capacity of SMEs will be utilized at the maximum level, and the supports available for SMEs and individual entrepreneurs in the fields of training, project finance, organization, marketing and technology will be further expanded.

In the Eighth Plan, the following issues were raised in the chapter related with SMEs.

- The productivity of SMEs, their competitive power at the international level and their share in the added value and bank credits will be increased. Construction of small industrial estates will be completed on time and the establishment of sector based foreign trade companies in these estates will be promoted.
- SMEs will be supported by modern financial instruments and institutions in an environment which has regularly operating capital and financial markets. Such

mechanisms as the Credit Guarantee Fund, venture capital and equity participation programmes will be mobilized on a widespread basis. Necessary regulations will be arranged to ensure that SMEs can raise funds through the capital markets.

- SMEs will be supported in terms of increasing their technological level and product quality, facilitating their access to information, guidance and consultancy services, developing links between large (or main) contractors and subcontractors and diffusing electronic commerce among SMEs. SMEs will be assisted in adopting modern management systems and to assume a leadership role for the mobilization of local resources. SMEs will be kept informed of export issues, and the establishment of export-oriented organizations will be encouraged.
- SMEs will be directed towards Research and Development activities and their interaction with the universities in technoparks will be ensured.
- Necessary actions will be taken to improve the share of SMEs in public procurement
- SME legislation will be harmonized with that of the EU.

The Eighth Plan reiterates, similar to the Seventh Plan, the goals related to the improvement of SMEs (in the fields of productivity, technology, etc.). The Eighth Plan additionally emphasizes the issue of developing innovative financial instruments. An ongoing emphasis of the need for developing SMEs through all of the plans up to and including the Eighth Plan, gives the impression that hitherto applied models have remained insufficient. The Eighth Plan presented a complete package of goals covering most of the supports needed for the strengthening of SMEs. In this period (2005), the definition of SMEs was aligned with the EU definition.

Since the length of development plans was increased from 5 to 8 years in 2007, the Ninth Plan covers the period between 2007-2013. One of the sections under the axis of competitive power is devoted to the improvement of the investment environment in Turkey. In this section, the following statement is set forth: “access to loans will be facilitated (especially for SMEs) by the development of venture capital, start-up capital and credit guarantee systems”³. It is seen that two separate capital funds (venture capital and start-up capital) are used in the Ninth Plan in place of the general term “venture capital” of the Eighth Plan. Another objective stated in the Ninth Plan is to create a transparent and competitive environment through the administration of e-procurement tools to facilitate SMEs’ access to public procurement. The simplification of business and employment legislation is among the targets specified in the Ninth Plan. The Plan also shows that business start-up and business development training and consultancy services will be made available for SMEs and entrepreneurs in order to increase their competitive capacity and to facilitate their entry into new markets. In this respect, the plan indicates that business incubators (İŞGEM) and similar models will be put in wider use and necessary arrangements will be provided to ensure an effective operation of these models.

³ The first risk capital company of Turkey was set up in 1996 by Vakıfbank which is a state owned bank. The name of Vakıf Risk Co. (Vakıf Risk Sermayesi Yatırım Ortaklığı which had a capital of 11 billion TL) was changed to Vakıf Venture Capital Co. in 2004 (Vakıf Girişim Sermayesi Yatırım Ortaklığı A.Ş.) depending on the preferred terminology in the related legislation. The second risk capital company was established in 2000 with the following partnership composition: TOBB (%35,83), Halkbank (%31,47), KOSGEB (%9,44), Halk Leasing (%4,27), TESK (%0,31) and Industry and Trade Chambers (% 68,18) dir. (Although state owned, Vakıfbank has a corporate status in accordance with its Establishemnet Law whereas Halkbank and Ziraat Bank were established as state banks by their laws).

Although some initiatives including “TEYDEB” of TÜBİTAK (Technology and Innovation Support Programmes Directorate), “San-Tez” of the Ministry of Industry and Trade (the Industrial Thesis Project) and the “Teknogirişim (Technoventures)” Project were not established as risk capital companies, they can be counted among the state entrepreneurship support incentives since they aim to develop SMEs and candidate entrepreneurs by supporting R and D activities and by providing grants for technology based projects. To give an example, it has been envisaged by the Ministry of Industry and Trade to provide grants up to 100,000 TL for each of the 82 “Teknogirişim” projects in 2009. The number of projects to be supported in 2010 is 100. Related legislation (Law 5746) has been approved by the Parliament. The “San-Tez” Project aims to increase the innovation capacity of SMEs through a well established industry-university cooperation scheme.

TTGV (the Technology Development Foundation of Turkey) supports young entrepreneurs with its “Seed Capital” and “Start-up Capital” Programmes. TTGV is not a state agency, its activities are financed from a World Bank Fund. Endeavor is a civil organization which supports young entrepreneurs with its “Business Angels” Project.

It can be seen that in the Ninth Plan the objective of supporting SMEs is dealt with in a more holistic approach. In this sense, improving the investment environment is targeted as well as applying the support mechanisms. Additionally, the importance of business incubators (İŞGEM) is emphasized as a new support model. It is also observed that entrepreneurship is a more visible target in the Ninth Plan

Although it can be seen that SME support instruments have gained a more sophisticated characteristic with time, there's an increasing tendency towards using a more holistic approach consisting of not only individual supports but also the investment environment and the business and employment legislation. It is not known whether the implementation of these instruments have been successful. Chapter V touches upon the importance of evaluation and impact analysis to be performed both during and at the end of the planning periods.

SME Strategy and Action Plan (KSEP)-2004

The SME Strategy and Action Plan was prepared in 2004 and then it was revised to cover the period 2007-2009. After summarizing the contents of both versions, a comparative evaluation will be made below.

Ten strategy fields were identified in the SME Strategy and Action Plan-2004 for the development of SMEs. These areas and related objectives are summarized below:

- **Strategy field 1-** Education and Training for Entrepreneurship:

- 1.1 Support entrepreneurship training (Insert entrepreneurship education in formal education curricula; provide training and consultancy services for entrepreneurs)
- 1.2 Promote vocational education, training and consultancy services (provide training and consultancy services for SMEs, create a supply of qualified workers that can be employed by SMEs, establish necessary IT infrastructure for distance learning)

- **Strategy field 2-** Development of cheaper and faster processes for business start-ups:

- 2.1 Ensure that transactions between enterprises and public institutions and organizations are executed from a single centre (decrease the bureaucratic procedures faced by the enterprises during the start-up phase and when they move to another work place, establish one-stop shops as an information source for entrepreneurs)

- **Strategy field 3 –** Enactment of better laws and legislation:

- 3.1 Eliminate SME definitions which are incompatible with each other (prepare a definition which is in compliance with the EU definition)
- 3.2 Simplify SME legislation (set up one-stop shops, maintain the existence of YOİKK⁴ (the Investment Advisory Council of Turkey) workshops, and identify the legislations that need to be simplified, carry out necessary administrative arrangements at the level of institutions)

⁴ The "Coordination Council for the Improvement of Investment Environment in Turkey – YOİKK" which was established with the World Bank support in order to improve the investment environment has been carrying out its activities since the year 2001. The Council is comprised of technical commissions working on 12 separate areas (establishment of corporations, employment, sectoral licenses, investment location, tax and incentives, customs and foreign trade, intellectual and industrial property rights, investment promotion, foreign direct investment, SMEs, institutional management, Research and Development)

3.3 Develop a statistical database of SMEs to facilitate the decision-making processes (harmonizing SME statistics with the EU, preparing an SME inventory)

3.4 Improve the Bankruptcy Law

3.5. Develop actions to rescue businesses which are facing financial distress (offering support to that business which can recover after restructuring or rehabilitation, developing the “Anatolian Approach”)

3.6 Make improvements in the Turkish Commercial Code (facilitating the liquidation procedures, informing businesses of these developments)

3.7 Improve the legislation of state aid to SMEs, make its execution more effective (rearranging special tax supports and the cash support system taking regions scales and horizontal aids as the basis in line with the EU and other international agreements, classifying these regions according to NUTS).

- **Strategy field 4** – Training to provide qualified personnel:

4.1 Develop a pool of qualified human resources (Establish the National Institution for Occupational Standards, develop a system of occupational testing and certification, institutionalize the concept of lifelong education)

- **Strategy field 5** – Improving on-line access and transactions via the Internet:

5.1 Enhance communication between SMEs and public organizations by providing a greater number of SMEs with information about public services, diffusing internet utilisation among SMEs)

- **Strategy field 6** – Opening up to new markets:

6.1 Develop national policies to increase the competitive power of SMEs in international markets (developing policies at national and sector based levels, converting "Exports Strategy Plan" prepared by DTM into a binding national policy document)

6.2 Activate the sector-based Foreign Trade Companies (SDTŞ) System (examine the successful models, establish model SDTŞs in different sectors)

6.3 Increase the level of awareness among SMEs about international trade rules and quality standards of goods and services (inform SMEs about the availability of KOSGEB Common Facility Laboratories and other services, set up the Information Centres to be envisioned in the Export Strategy Plan)

6.4 Monitor/supervise the quality of services (support international quality certification and Research and Development activities within the framework of international commercial rules)

6.5 Support national and local brands (strengthening fashion-brand initiatives, assisting SMEs in a more effective way for investigating their markets)

- **Strategy Field 7** – Improvements in taxation and financial matters:

7.1 Increase the supportive role of taxation for SMEs particularly in the start-up and growth phases (Establishing a tax system which rewards success, encourages business start-ups and promotes growth and employment generation of SMEs)

7.2 Develop existing financial mechanisms and create new mechanisms (strengthen the Credit Guarantee Fund to distribute its activities more widely, expand the resources of the SME finance system, set up networks to connect entrepreneurs with investors, develop SME finance models convenient for Turkey, diversify state aids for SME investments)

7.3 Promote employment generation (encourage young and female entrepreneurs in their employment-generating activities, ensure maximum flexibility in working life, develop alternative work models and contract types, reduce the tax burden on employers, encourage wider application of KOSGEB employment support)

- **Strategy Field 8** – Development of technological and innovation capacity of SMEs:

8.1 Support technology transfer and dissemination (strengthen the know-how related services, develop technology transfer and consultancy capacity, ensure that engineering, consultancy, design and know-how transfer services to be purchased by SMEs are in compliance with market standards, develop a market for service providers, support the Research and Development activities (in-company or contracted-out) of SMEs.

8.2 Increase the knowledge level in SMEs about research, development and innovation

8.3 Create mechanisms which aim to follow and disseminate new technologies (create one-stop consultancy centres for technology and innovation, establish Innovation Relay Centres (IRC))

8.4 Strengthen cooperation between SMEs and large enterprises, universities, professional organizations and public institutions

8.5 Create local and regional clusters (create cooperation clusters in the organized industrial zones, small industrial estates and industrial zones, develop sector based and handicraft clusters)

- **Strategy field 9** – Informing SMEs on best practices via the internet and developing high level SME support schemes:

9.1 Assist SMEs to benefit from best practices (information services, opening KOSGEB information offices at chambers, starting SME observatory studies)

9.2 Facilitate access to information (inter-enterprise networks, spread the European Information Centres over the country)

9.3 Increase the quality and expand the scope of non-financial services

9.4 Increase the capacity of institutions/organizations representing SMEs to deliver services to SMEs

9.5 Support SMEs to comply with the environmental legislation (benefiting from the EU programs, developing an audit system to check compliance with the legislation, supporting the use of environment-friendly technologies)

- **Strategy field 10** – More effective representation of SMEs at national and international platforms

10.1 Ensure coordination among relevant ministries and institutions/organizations

10.2 Facilitate participation of professional organizations in the legislative process

10.3 Develop professional organizations and non-governmental organizations related to SMEs

It is observed that the SME Strategy and Action Plan (KSEP-2004) is generally in compliance with the objectives and goals which are covered by the Eighth and Ninth Development Plans. It is also seen that nearly all the subjects relevant for SMEs have been covered, and the general framework is in compliance with the Lisbon objectives as well. As the Plan consists of general expressions rather than numerical and measurable goals we think that confirming the realization of the objectives will be difficult. However, it can be inferred that tangible objectives are specified in the operation plans of relevant institutions as the Plan declares the names of the institutions and organizations responsible for the execution of the Plan. This is important in terms of achieving the identified objectives. But since there are several institutions in the Plan which are responsible for one objective, coordination and monitoring tasks become very important. The way these objectives are reflected in the State Incentive System will be discussed in the following chapter.

An interesting point in KSEP 2004 is the idea of supporting SMEs facing financial distress. At this point, “financial distress” appears to be an ambiguous concept since it is not clear whether it is envisaged to support SMEs through an evaluation and improvement plan and according to relevant scale or sector based criteria or through such mechanisms as interest subsidy, etc. without any discrimination between different categories of SMEs.

The issue of increasing SMEs’ access to public procurement which is placed in the Eighth and Ninth Development Plans is not dealt with in KSEP-2004. Furthermore, KSEP does not include any provisions concerning the transfer of businesses ownership which has an important place in the SME strategies of the EU member countries. Transferring a business, which would otherwise close, to a new owner is a way to protect employment in the business. It can also prevent negative effects that may be created on the production and sales volumes of other businesses having any kind of transactions with the closing business. Therefore it is vitally important to create awareness about the “transfer of business ownership” concept, establish databases, examine the related legal infrastructure and provide support both to the businesses that are being transferred and to the new owners takingover the business.

In KSEP 2004, “KOSGEB Employment Aid” is seen as an employment generating tool which needs to be made widely available for SMEs. It is understood from related KOSGEB documents that this support is in the form of grants or interest subsidies provided for SMEs in return for employing additional staff. However, when the EU practices are examined, it is seen that employment supports are in the form of general measures based on decreasing the tax burden on employers. We think that it would be more useful to adopt active labour policies in Turkey similar to those implemented by the EU such as encouraging the employment of disadvantaged groups, temporary job placement, creating apprenticeship positions in enterprises etc.

SME Strategy and Action Plan (KSEP)-2007-2009

Under the heading “Enterprise and Industrial Policies” of the 2006 Accession Partnership Document, it is emphasized that Turkey should continue its efforts for simplifying the business environment and aligning the SME definition with that of the EU.

As already indicated in the above sections, the SME definition was aligned with the EU definition and the Council of Ministers’ Decree dated 18 November 2005 (No. 2005/9617). Our opinions concerning this issue were already summarized in Chapter III.1.

The “Enterprise and Industrial Policies” section of the 2006 Progress Report sets forth the following arguments:

- A new definition for SMEs was made in compliance with the *acquis communautaire*⁵.
- Additional arrangements are needed in order to decrease unnecessary bureaucracy and improve the business environment
- Turkey has made good progress in the area of Enterprise and Industrial policy instruments and it has taken part in the “Multi Annual Program for SMEs” (MAP)
- No sector-specific strategies exist but some progress was made with respect to sector policies
- Turkey should improve its capacity to assess the impact of policy measures

In compliance with the Progress Report conclusions, the following objectives and strategy areas were identified in KSEP 2007-2009

Strategy field 1 – Development of entrepreneurship: improving the skills of candidate entrepreneurs, increasing the knowledge and skill levels in new businesses, ensuring widespread use of entrepreneurship support mechanisms, encouraging entrepreneurship among disadvantaged groups.

Strategy field 2 – Enterprise development: developing management functions and related skills in SMEs, establishing a qualified pool of human resources and improving employment opportunities, developing the production and quality processes of SMEs, spreading the use of information technologies, developing the consultancy mechanism and providing consultancy supports, enabling SMEs to comply with existing environmental and labour legislations.

Strategy field 3 - Integration of SMEs with international markets: increasing SMEs’ share in exports, promoting the branding efforts of SMEs

Strategy field 4 - Improving the business environment: Enhancing cluster development and revising related legislation, increasing the effectiveness of state aids establishing an effective, encouraging and supportive tax system developing regulations with a view to encourage employment, increasing the supply of finance for SMEs and assuring their effective use, establishing new financial mechanisms, facilitating cooperation and coordination among the institutions/organizations related with SMEs.

Strategy field 5 – Developing the technological and innovative capacity: directing SMEs towards technology, R&D and innovation, improving the mechanisms aimed at following, monitoring, relaying and disseminating new technologies, expanding supports available for technology, R&D and innovation, developing the media for technology implementation (Technoparks, TEKMERs, etc.) strengthening the technology based cooperation between SMEs, large enterprises and universities.

When KSEP 2007-2009 objectives are examined, it is seen that they are more or less similar to the objectives cited in KSEP 2004. But the objectives are shown using a different classification in each KSEP. Additionally, in the revised version (2007-2009), some of the objectives are defined in terms of numerical and measurable criteria. Since some objectives and actions are still explained in general terms, it is difficult to understand the underlying criteria. None of these plans show the sources of finance necessary for the realization of these actions nor do they show the indicators of success. But a model for monitoring the implementation of KSEP is put forward and establishment of an effective co-ordination system related with SME legislation and other relevant subjects is envisioned. The institutions responsible for the execution of the objectives are also shown in the Plan. The other specific topics mentioned in the 2007-09 Plan are as follows: Setting up an institutional structure to monitor and audit state aids, developing mechanisms for venture capital and seed capital (including investment partnerships), preparing SMEs for the BASEL II Process, improving the technology and innovation capacity of SMEs, betterment of the tax system and reducing the labour costs (taxes).

⁵ The body of Community legislation by which all EU Member States are bound. Countries joining the EU must have implemented the existing *acquis communautaire* by the time of accession.

Another point which deserves attention in the Plan is that the whole group of SMEs covered by the legal definition has been identified as the target group of all the objectives and action plans without discrimination. There is a lack of understanding towards segmenting SMEs with respect to scale, sectors, development level etc. and design of the objectives and actions accordingly. However, it is very well known that different segments of SMEs have different problems and different needs. To give an example, an SME operating in a high technology area has totally different support needs than a small maintenance-repair firm. Similarly, there is a big difference, in this respect, between an SME with 3 employees and another one with 200 employees. Many other areas (such as sectors) of differentiation can be specified in this regard. For this reason it is important to design and implement different support packages for different segments of SMEs.

The 2007 Progress Report (see TÜSİAD Comparative Table, 2007) indicates that the 2007-2009 KSEP Plan is compatible with the EU principles and the Lisbon Strategy to a great extent. The Report also presents the following findings: The Coordination Council for the Improvement of Investment Environment in Turkey (YOİKK) is preparing a new plan the infrastructure which is necessary for the supervision and monitoring of strategy and action plans is lacking, good progress has been achieved regarding the Research and Development Support Law, no progress was made to combat late payment in commercial transactions.

In the Bibliography Section (Section VI), we provide a list of national and international reports about SME policies in Turkey. When these reports are examined, it will be seen that almost all of them mention about the same problems and recommend similar actions to solve these problems. To give an example, in the OECD Report prepared in 2004 (OECD, Small and Medium Sized Enterprises in Turkey: Issues and Policies, 2004), the following recommendations are quoted:

- Improve general economic conditions
- Develop a better data collection system
- Strengthen the competition policy
- Improve the tax system
- Invest in the human resources
- Increase flexibility and productivity in the labour markets
- Increase the effectiveness of current support programs
- Increase the effectiveness of KOSGEB activities
- Establish an effective consultancy system
- Facilitate SMEs' access to finance
- Facilitate SMEs' access to export markets
- Monitor and evaluate implemented policies and supports
- Encourage SMEs to use information technologies

III.4 An overview of SME-oriented policies and plans within the framework of two selected areas of application (investment incentives and KOSGEB supports)

Investment incentives

In Turkey, SMEs were included in the State Aid Programme for the first time by the Government Decree 93/4000 "Principles for Directing and Promoting Investments, Foreign Currency Earning Services and Enterprises". This Decree rendered SMEs eligible for loans from the Investment Incentives Fund to purchase machinery-equipment with no need to obtain an incentive certificate. Furthermore, it enabled SMEs to benefit from other incentive options, provided that the minimum investment amount foreseen in the incentive certificate was attained. It is not difficult to understand that keeping the level of minimum investments (thresholds) the same for both large enterprises and SMEs would make it hard for the SMEs to benefit from these incentives. However, when similar

schemes in the EU member countries are examined, it is seen that the SME group is divided into subgroups and investment thresholds and other criteria are specified according to the characteristics of each group.

The Decree 1994/6411 placed SMEs under the category of “Investments which do not require a Certificate of Incentive”. Interest rates applicable to loans from the Investment Incentives Fund were not fixed according to the size of the enterprises but on the regional basis. This Decree reflects a transition from sector specific incentives to region-specific incentives.

It became possible to grant specific state aids for SMEs for the first time in Turkey by the Decree 96/8615. In the related directives SMEs were defined as the manufacturing enterprises employing maximum 150 persons and having less than 50 thousand TL as their registered book value of fixed assets (including machinery-equipment, plants, vehicles, fixtures and fittings, excluding land and buildings). Under these directives, SMEs were made eligible for “investment allowance, loans from the Investment Incentives Fund, VAT reduction, exemption from customs duties and fund levies, exemption from certain taxes, duties and fees”. In order to qualify for these incentives, it was necessary to obtain an incentive certificate. In the same year, an Income Tax directive was launched which eliminated the obligation to obtain an incentive certificate to be able to benefit from “Investment Allowance”. This enabled the SMEs which failed to meet minimum investment criterion to benefit from investment allowance. Thus the inconvenience caused by the previous Decree by setting forth a threshold for investment was eliminated.

After the Decree 98/10755 “Principles on State Aids for Investments and the Investment Encouragement Fund” came into effect, two other Decrees were issued: Decrees 98/10699 and 99/12474 “Principles on State Aids for the investments of Small and Medium Enterprises”. Although these Decrees contained similar provisions with the previous Decree (Decree 96/8615), it is observed that the amount of loans available from the Investment Incentives Fund was increased. Loan terms such as the upper limit and grace and maturity periods were determined on a regional basis. It was envisaged that minimum 20% of the loans should be utilized by the SMEs in the artisans and craftsmen category. Halkbank was designated as the institution where SMEs would submit their applications to obtain their incentive certificates. There was no marked difference regarding the incentive tools (investment allowance, VAT exemption, and exemption from certain taxes, duties and fees, energy support, land appropriation, Loans from the fund).

The Decree 98/10755 became invalid after the succeeding Decrees 2000/1821 and 2000/1822 (“Principles on State Aids for the Investments of Small and Medium Sized Enterprises”) were launched.

Whereas the Decree 96/8615 is distinctive for being the first SME specific decree, the Decree 2000/1822 is also important as it covers contemporary definitions and applications. SMEs were again included in the general incentive system by the Decree 2006/10921.

The following points are observed in the Decree 2000/1822:

- The definition of SMEs was changed. Whereas the enterprises with less than 150 employees were regarded as SMEs previously, in the new Directive SMEs were divided into three categories namely micro (1-9 employees), small sized (10-49 employees) and medium sized (50-250 employees) enterprises. Their registered book value of fixed assets (including machinery-equipment, plants, vehicles, fixtures and fittings, excluding land and buildings) can not exceed 400 thousand TL. Grouping SMEs in this way is seen to be very convenient in terms of designing and implementing different support tools for different categories. However, as shown below, this classification was not taken into account in the arrangement of the support elements except for the loans from the fund.
- An important change was made in the scope of SME investments. Whereas only the manufacturing sector investments were supported previously, the new Directive included the

agricultural industry, tourism, education, health, mining and software sectors into the scope of support. Thus an integrated approach covering a great many sectors is exhibited.

- The concept of “provinces which require emergency support” was abolished and the regions were divided into three categories (developed, normal and priority). This rendered it possible to arrange region-specific supports aimed at removing regional disparities. In line with this approach, different aid intensities were specified for some measures (for ex. Investment allowance) for different regions.
- While allowing SMEs to use investment and operating loans from the Investment Incentives Fund in proportion to the level of their investments, the limits of these loans were specified considering the regional and scale differences. Loan interests and the other measures were differentiated only on the regional basis.
- Türkiye Kalkınma Bankası (TKB), Türkiye Sınai Kalkınma Bankası (TSKB) and Türkiye Sınai Yatırım Bankası (TSYB) were included among the intermediary banks in addition to HALKBANK.
- “SME Investment Companies” were given the opportunity to use loans from the Incentives Fund (Fund for non-tax incentives). These companies were able to utilize Fund Credits (credit allocations from the Investment Incentives Fund) through specified intermediary banks in the amount corresponding to maximum 20% of the stakes acquired in SMEs in the previous year. This was an innovative approach towards SME financing. Supporting SMEs through a model similar to venture capital is particularly important for the technology firms. However, unless the performance displayed by these Investment Companies is examined, it is difficult to conclude whether this modern instrument has proven to be successful or not.
- It is possible for the credit guarantee institutions to obtain a maximum of 50% of the indemnities paid to the banks from the Incentives Fund. This amount can not exceed 10% of the guarantees issued by the institution in one calendar year.

We can see that support measures were changed with subsequent Decrees. For example these measures were limited to customs duty exemption, VAT exemption and interest subsidy in the Decree 2006/10921 which aimed to support SME investments and R&D and environmental investments. Investment allowance and other measures were not included into the incentives package (it is worthy noting that abolishing the application of investment allowance was a simultaneous action with reducing the income tax rates). With this Decree, SMEs were incorporated into the General System and they were allowed to apply directly to the Treasury. To be eligible for an incentive certificate, a minimum threshold of SME investments was specified as 200,000 TL and the upper limit was specified as 2 million TL. For the other investments, the minimum amount was defined to be 1 million TL. Although it seems that this decision was in favour of SMEs, it is clear that the minimum threshold is still too high for SMEs and only a small percentage of SMEs could meet this criterion. In order to make a comparison, it may be appropriate to look at the way SMEs less than 2 years old are granted state aids in a European country (e.g. Belgium). In this example, SMEs are divided into 12 sub-groups depending on the number of their employees. Different thresholds are specified for each of the sub-groups. Different amounts of supports are granted taking into account the size, location, subject of activity and employment generation capacity of these SMEs.

In Turkey, beside the tax legislation, there are two more legislations which arrange incentives. The first one is Law 5084 concerning the encouragement of investments and employment and the other one is Law 4691 concerning the development of technology zones.

Law 5084 does not provide any exceptions for income tax, corporate tax or VAT. The law aims at encouraging investments and employment generation in the provinces having a per capita income of less than 1500 USD (2001). The enterprises in these provinces can benefit from income tax and labour cost incentives, energy support and free land in return for employing additional workers. The law does not provide any discrimination for sectors or types of the investments (such as energy saving investments, security, R&D etc.). Being located in the specified province is a sufficient condition for eligibility. However these incentives are restricted to new companies employing at least

10 workers. Those enterprises employing less than 10 workers are eliminated from the system. Energy support expires as of 31 December 2008.

Law 4691 provides exemption from corporate income tax for 10 years for the companies involved in technology intensive activities in affiliation with universities or research institutions. Additionally, the employees of these companies are exempted from income tax for 10 years.

Under Law 5615, in effect from 2007, a minimum living allowance has been available as a tax credit against employment income (actual deduction taxation).

To sum up at this point, the following incentives are available for the SMEs in Turkey:

- Incentives under the Decree 2006/10921 and Laws 5084, 4691 and 5615
- Tax incentives (tax exemption, accelerated depreciation, declining balance depreciation, tax credits, and writing off such costs as Research and Development etc.)
- VAT incentives
- Customs duty incentives
- Loans and loan guarantees
- Other incentives (risk insurance, infrastructure, etc.)

Recent media news has revealed that the new incentive system to be in effect starting in 2009 will provide such measures as social security payment deduction, corporate tax deduction, compensation for employees' training costs, land allocation, interest refund, customs duty exemption and VAT exemption. It is also understood that enterprises which create additional employment will benefit from the incentives and all the provinces will be eligible for the incentives without discrimination.

All the explanations above show that the incentive system in general (particularly SME incentives) is being improved to be more sensitive to SME needs and more compatible with the EU applications. The system is also in harmony with the development plans and strategies. However, there is a need to collect data to be able to analyse whether these measures are being effectively used by SMEs, whether these incentives contribute to the development of SMEs and what type of barriers exist which deprive SMEs of these incentives.

The table below presents SME incentives data for the years 2003-2008 (see www.hazine.gov.tr) and fixed investment/employment rates calculated with these data.

Table 4. SME Incentives (2003-2008)

YEARS	Number of Incentive Certificates	Investment Loan (TL)	Working Capital Loan (TL)	Amount of Fixed Investment (TL)	Number of jobs created	Fixed Investment/job creation ratio
2003	455	34.637.329	10.720.788	105.508.776	2019	52.257
2004	436	52.499.523	10.815.093	112.613.418	3138	35.887
2005	218	33.171.301	4.444.930	67.019.307	2315	28.950

2006 January – November	136	24.691.915	1.488.510	49.699.667	1346	36.923
2006 - December (*)	9	7.990.225	-	7.990.225	140	57.073
2007	942	875.396.173	-	875.396.173	17.686	49.496
2008	1363			1.112.503.962	19.229	57.855

(*) The date in which SME incentives were included in the general system by the Decree 2006/10921

Although it is possible to derive some conclusions from this table, there are other factors (sectors, location etc) which need to be calculated for a healthy analysis. However, an analysis having such depth is beyond the limits of this study. Here, we wish to emphasize once more the necessity of conducting an in depth impact analysis.

One of the performance indicators for SMEs is their share in total credits. In Turkey, this share has increased from a level of 5% in the 1990s to 25-30% in the 2000s. The “SME Credits Monitoring Report⁶” prepared by the Under secretariat of Treasury in 2007 provides data concerning the 3 billion USD foreign credit programme out of which 19 projects were financed between 1999-2005. These credits were made available for SMEs through Halkbank, Vakıfbank, T.C. Ziraat Bankası, Türkiye Sınai ve Kalkınma Bankası (TSKB) and Türkiye Kalkınma Bankası (TKB) under the guarantee of Treasury. The credits were lent by the European Investment Bank (EIB), Council of Europe Development Bank (CEB), Japan Bank of International Cooperation (JBIC), World Bank (IBRD), German Development Bank (KfW) and the Spanish Government. The number of credits utilized by SMEs is 849. Distribution of the credits among regions is parallel to the share of these regions in the overall national income. The biggest share was obtained by the Marmara Region (56%) which was followed by the Aegean, Mediterranean, Middle Anatolia, South Eastern Anatolia, Black Sea and Eastern Anatolia regions. Regarding the sectors, the highest rate belonged to the industry sector (68.9%). It was followed by the services, energy and agricultural sectors. When the table below is examined, it will be seen that the major part of the loans were given to medium sized enterprises (43.5%) and this group was followed by the small sized and then large enterprises.

Table 5. Distribution of foreign credits by size (1999-2005)

Enterprise size	Number of loans	Share in total
Micro Enterprises (1-9 workers)	39	4,6
Small Enterprises (10-49 workers)	230	27,1
Medium Sized Enterprises (50-250 workers)	369	43,5
Large Enterprises (more than 250 workers)	211	24,9
TOTAL	849	100,0

In the 3 billion USD package of foreign credits, SMEs’ share was 1.8 billion (780 loans, 60%) in the period between 1999-2005. The average amount of credit per SME is 2.3 million USD. When a

⁶ Report dated 7 November 2007 prepared by the Foreign Economic Relations Department of the Undersecretariat of Treasury

region-wise examination is made, it is seen that the Middle Anatolia Region has the lowest “credit per SME” value (1.6 million USD) whereas the Mediterranean Region has the highest (4.3 million USD). The distribution is as follows when a classification is made according to size:

1-9 workers: 0.9 million USD

10-49 workers: 1.2 million USD

50-250 workers: 1.9 million USD

More than 250 workers: 4.5 million USD

As an impact of SME credits totalling 1.8 billion in the period between 1999-2005, the number of jobs increased from 152,178 (beginning of 1999) to 196,160 (end of 2005), an increase of 43,982 jobs. The average increase in jobs per SME was 56 which shows that the capacity growth created by credits resulted in employment generation.

KOSGEB Supports

In Turkey, activities related to supporting SMEs and entrepreneurship have accelerated since 1990. This is the year when KOSGEB was founded.

KOSGEB supports provided for SMEs are listed below. It should be remembered that KOSGEB supports only cover the enterprises operating in the manufacturing sector. KOSGEB supports are available in 8 groups.

1. *Consultancy and Training Supports*
 - a. SME Development Consultancy
 - b. SME Development Training
2. *Technology Development and Innovation Supports*
 - a. Technology Research and Development Support
 - b. Industrial Property Rights Grant
3. *ICT Supports*
 - a. Computer Software Support
 - b. E-Trade Support
4. *Quality Improvement Supports*
 - a. General Test-analysis and Calibration Support
 - b. Test-Analysis Support for CE Marking
 - c. System Certification Support
5. *Market Research and Export Promotion Supports*
 - a. Support for Participating in Domestic Industrial Fairs
 - b. Support for Participating in Domestic Fairs with International Features
 - c. Support for Participating in Foreign Fairs Within the National Level Organizations
 - d. Support for Participating in Foreign Fairs Out of National Level Organizations
 - e. Trademark Promotion Support
 - f. Brand Development Support
6. *Supports for the Development of International Cooperation*
 - a. Participation in Business Trips for Export Purposes
 - b. Twinning Support
7. *Regional Development Supports*
 - a. Local Economic Research Support
 - b. Support for the Purchase of Machinery-Equipment for Common Use
 - c. Infrastructure and Building Construction Project Preparation Support

- d. Support for the Recruitment of Qualified Personnel
- 8. *Entrepreneurship Development Supports*
 - a. Establishment of Business Incubators
 - b. Start-up capital

It has been seen that KOSGEB supports are also in compliance with the national development plans and SME Strategy and Action Plans. Besides the above mentioned supports of KOSGEB given in the form of repayable and non-repayable grants, KOSGEB also renders financial assistance to SMEs by subsidizing the interests of the loans provided by various public and private banks. Media news indicates that the share of interest support in the whole package of KOSGEB supports is increasing steadily. It is also understood that KOSGEB Law is in the process of being amended to cover the SMEs outside the manufacturing sector. The following table presents information about KOSGEB supports given in the period between 2003-2007 (Source: www.kosgeb.gov.tr)

Table 6: KOSGEB supports provided for SMEs between 2003-2007

Years	Number of Supports*	Total Amount
2003	14.710	25.345.485,30 TL
2004	21.488	103.523.390,65 TL
2005	4.811	43.118.420,00 TL
2006	2.405	13.542.546,80 TL
2007**	1.130	5.759.908,54 TL

* As the enterprises are able to get more than one support, this is the cumulative number

** January 1 – June 30, 2007

The figures given in Table 6 cover the KOSGEB supports which are listed in 8 groups above. It can be inferred from the examination of the table that the amount of supports increased sharply in the year 2004, but gradually declined thereafter. There is a need to carry out a detailed study on the reasons behind this decline⁷. It is also understood from the KOSGEB reports that the amount of supports given in the form of interest subsidy is increasing. In this context, 1 billion Dollars has been earmarked for the “Cansuyu Project” (Life line loan) which will be initiated early in 2009 for the SMEs in the export business. It is clear that the interest subsidy tool is being used to overcome the difficulties of SMEs to access finance, and this support is greatly welcomed by the SMEs. It is vital, however, to examine the possible effects of this mechanism on the establishment and development process of market structures which aim to provide debt and equity finance for SMEs (the SME Strategy and Action Plan targets the development of such structures). On the other hand there is a real danger that SMEs struggling with cash flow problems would remain blind to other supports which are indispensable for their development if they are too much attracted by the supports given in the form of interest subsidy by KOSGEB.

Export incentives

The Decree defining the “state aids for export” came into effect in 1995. Supports which were made available with this Decree for the *sector based foreign trade companies (SDTŞs) to be established by SMEs or a group of SMEs* are as follows:

- a. Support for environmental costs
- b. Support for market research
- c. Training aid
- d. Employment aid

⁷ One reason of this decline may be related with different visions of KOSGEB management regarding the content and methodology (being stricter in the later period) of SME supports.

Within the same aid scheme, the following supports are provided regardless of the firm size:

- a. Support for participation in international fairs
- b. Support for opening offices/stores abroad and support for Brand Promotion Activities
- c. Support for promoting and publicizing Turkish products abroad, establishing the Image of Turkish Goods

In Turkey, the share of SMEs in exports (10%) remains to be very low when their share in total number of enterprises and total production is considered. It is also low when compared to the export shares of SMEs in such countries as India (50%), Japan (38%) and Germany (31%). Therefore it is vitally important to increase the competitive power of SMEs by supporting their manufacturing and marketing activities. SME export aids are mainly implemented by the Undersecretariat of Foreign Trade (DTM) (the Export Development Centre – İGEME is entrusted for certain applications) and KOSGEB. It is easily seen that both institutions provide similar supports. Coordination between these institutions is very important in order to ensure an effective and productive use of state aids and prevent overlaps. It was reported by DTM that export aids which were given by DTM in 2007 amounted to 305 million US Dollars (Yeni Şafak, March 17, 2008).

Research and Development supports

TÜBİTAK, which is the leading institution implementing Research and Development supports, offers R&D supports for SMEs through its Directorate for Technology and Innovation Programs (TEYDEB). According to TÜBİTAK (The News Centre, 30 April 2007), in the period between 1995-2007, 2271 SMEs applied to TEYDEB for R&D support and at least one project from each of 1449 SMEs was granted support. TEYDEB started its “1507 –SME R&D Support Program” in 2007. Within the framework of this programme, SMEs can obtain 75% of their first two R&D project costs in the form of non-repayable grant. The upper limit for the project budgets is 400.000 TL. This rate compares well to the rates applied in similar programmes of other countries. The procedures of this program are more simplified than the procedures of other TÜBİTAK supports. SMEs have a share of 84% and 60% in the total number of enterprises supported within this scheme and the number of supported projects respectively.

The above paragraphs explain the services offered by certain institutions which provide state aids for the SMEs in Turkey. Their dedication to developing SMEs is clearly visible in their mission statements, policy documents and activities. When the implementation data is examined (types of supports to SMEs, the number of SMEs which benefit from these supports, the amount of supports etc.), some conclusions can be derived, however the absence of a comprehensive impact analysis study is still apparent. Such an analysis is vital for clarifying the roles and responsibilities of related institutions and preventing overlaps. Supports and aids can be developed and updated accordingly.

IV. AN EVALUATION BASED ON PERSONAL OBSERVATIONS OF THE SME SECTOR IN TURKEY

A very interesting evaluation about the SMEs in Turkey was made by Bülent Ecevit who was a guest speaker at a TOSYÖV meeting in February 1990. Ecevit said, “An American couple whom we have known for a long time visited us at our home in Ankara last month. While having tea together and chatting, I asked them how they liked Turkey. They said that they loved Turkey very much and they had even started to learn Turkish. When I asked them what they learned in Turkish, they gave a very interesting answer, saying, “First we came to Istanbul and stayed at the Grand Tarabya Hotel. Then we went to İzmir and stayed at the Grand Efes Hotel. Now we’re in Ankara and staying at the Grand Ankara Hotel. Here, we grasped the meaning of the words “grand” or “big” very well. We understood that Turks love these words so much.” After telling about this experience, Ecevit made the following comment: “It must be very hard to deal with the SMEs in a country where people love and adore the word “big” this much.”

Actually this characteristic of Turkish people should not be regarded as strange, because every society, every city, every enterprise and even every person in fact has similar characteristic. The slogan “small is beautiful” is very nice and attractive, but this slogan is nice only in the beginning. For any enterprise, “growth” should not be only a company goal but also a social responsibility. The most acceptable success criterion for an enterprise is “growth”, in other words, being in pursuit of growth during the life cycle of the enterprise. In this respect, the slogan “small is beautiful” should be changed as follows: “small is beautiful, but sustainable growth is desirable.” The goal of an enterprise (or its target) must be to follow a path of sustainable growth.

However this character (love of big things) has negatively affected the development of the SME concept in Turkey. As a matter of fact, the concept of small and medium sized enterprises had never been used in the development plans setting the economic targets from the beginning of the 1960s until the Fourth Plan that covers the period 1979-1983. Before then, all the supports were directed and focused towards large enterprises. The term “small industry” was first used in the Plans 1979-83 and 1990-94. It is only with the Seventh and Eighth Plans covering 1996-2000 and 2001-2005 respectively that the “SME” concept was handled in the correct way. The most important aspect of the Seventh Plan is the effort to ensure harmonization with the EU. Even in this Plan, it is observed that SMEs are seen as a source of employment rather than being an economic growth instrument.

The theme “entrepreneurship”, which should be the most important concept in approaching SMEs, had not become an issue of concern until the Eighth Plan covering 2001-2005. In the Ninth Plan (2007-2013) however, this subject was made the focal, dominant point of SME strategies. In these documents the importance of encouraging entrepreneurship and spreading the concept all over the country is emphasized and the objectives of increasing the added value and innovation and R&D capacity of SMEs are stressed. Whereas the appropriateness of the objectives set forth in these plans is out of question, whether these objectives have been successfully achieved in practice is doubtful. Some points to be criticized in these Plans are the lack of sufficient harmony between the objectives, identification of general objectives rather than measurable targets, abundance of responsible institutions and ambiguity in the responsibilities. However it is seen that these weaknesses have been recognised recently and a more positive approach to SME incentives has been adopted. We believe that the greatest weakness remaining is the failure to help potential entrepreneurs move into the economy and the inability to exploit Turkey’s young and dynamic population.

As it can be seen from the data presented elsewhere in this report, micro enterprises have a very important place in the SME picture of Turkey with a share of 90% in the total number of SMEs. The main point here is to enable micro enterprises to follow a path to attain small, medium, or even large sizes successfully. Unfortunately, other than a few examples, SMEs in Turkey have not demonstrated this growth process.

The existence of a healthy and sustainable SME sector in a country is very important. However, while this argument is relevant for the SMEs as a whole as an economic constituent of the economy, it is not relevant for individual SMEs. Individual SMEs, on the contrary, should be encouraged to grow regardless of the performance of others within the sector. In other words, state aids should be made available for those SMEs which have proven the ability to follow the growth path and be withheld from the ones which stay at the same level with no growth prospects. In this respect, the SME sector should be regarded as a selection corridor, since “sustainable growth” must be the most important company target. This is at the same time a social responsibility and a way to increase the welfare level of a country. On the other hand, for augmenting the SME sector on the whole, the establishment of small new enterprises should be encouraged and entry of young potential entrepreneurs into the market should be facilitated. In this respect, creating a conducive environment, delivering entrepreneurship training and spreading the concept of entrepreneurship should be an important economic objective. This is the sine qua non of a healthy and sustainable SME sector.

The number of enterprises that have successfully completed the process of moving from micro size to large size (passing through the small and medium stages) is very small in Turkey. Most of the

enterprises over one hundred years old today have not been able to grow to the large, even medium size bracket (e.g. Ali Muhittin Hacı Bekir (1777), İskender Kebapçısı (1871), Kurukahveci Mehmet Efendi (1871)). These enterprises have been able to maintain their existence for over 100 years almost by staying small and introverted. The lifetime of an appreciable number of them has been limited to the first generation (the founders) after which they have ceased to exist.

These characteristics of the SMEs in Turkey are well expressed in the following verses (anonymous, belonging to the Gaziantep Region)

“The poor are impoverished by empty stubbornness,
Civil servants by their pompous wives,
The rich by their spoiled children”

Here we can say that the poor symbolize micro enterprises. The idiom “empty stubbornness” emphasizes the inability of an enterprise to adapt itself to changing conditions. This is the most important reason for its failure. Flexibility and adaptation to change are important strengths of micro enterprises. Those who are able to exploit this strength in a wise manner can progress towards growth.

The “civil servant” symbolizes small enterprises. A small enterprise which gains a foothold in the market should further strengthen its position and increase its competitive edge, productivity and value. “Flashy” investments, wastefulness and extravagance may create fatal problems and the small enterprises that can protect themselves from these dangers can progress on their way to growth.

Finally, the “rich” refers to medium enterprises. In general at this stage, the founding entrepreneur reaches an old age and he needs his daughters or sons to embrace the business. Otherwise the end of the founder’s life will mean the end of the business. We can find many such examples in our country. In this context, family business management and institutionalization of these businesses are of utmost importance. This subject has gained wider recognition in Turkey in the last decade. This has become the most widely discussed theme during the SME meetings held in İstanbul and Anatolia.

Another important subject we wish to emphasize is the inability of many SMEs to establish successful relationships between their partners.

Unfortunately, there are very rare examples of smoothly running partnership relations among Turkish SMEs. This is especially important for the micro enterprise sector, which accounts for 90% of total enterprises, since it is almost impossible for these enterprises to compete in the global economy because of their small scales. Small enterprises which represent 8% of total enterprises are faced with the same situation. In short, an inevitable reality for micro and small enterprises which constitutes 98% of total enterprises in Turkey is the fact that, they should seek partnership alternatives not only in their vicinities but at the national or even global levels. This is crucial in order to survive and maintain healthy and sustainable growth. The recent economic environment offers many opportunities in this respect. Government institutions and NGOs should encourage inter-enterprise cooperation and provide suitable ground for successful collaboration among SMEs. There are examples of satisfactory attempts shown by SMEs themselves or related NGOs in the recent years.

Moreover, unsuccessful partnership examples in the SME and large enterprise sectors in our country require further attention. To be able to develop successful SMEs, the reasons behind this weakness should be investigated and necessary measures should be taken. Based on our personal observations about this issue, we can list the main points as follows:

- Partnerships are generally established among siblings, relatives, friends and fellow citizens. The opportunity of cooperation between SMEs which could create synergy for them is not utilized to the required extent and the partnership ceases after a short period. This is especially common among partnerships between siblings.

- Another interesting example in Turkey is the partnerships established between fellow citizens. Especially during the 1970s, Turkish expatriates established companies in their home towns which were called “workers’ companies”. Unfortunately these companies, which were supported by a state bank exclusively established for this purpose, could not remain successful. The main reasons behind this were the partners’ lack of knowledge about running a business, insistence to locate the business in their home towns and the failure to test the feasibility of the investments. There are many lessons that can be derived from this experience.
- Partnerships must be based on agreements which explain the rights and responsibilities of the partners in a clear and explicit way. In the beginning, the partnership has a sense of trust and excitement. As time passes, many problems appear which result from the uncertainties on many issues, and in the end the partnership is dissolved. In short, the partners start this journey with goodwill and dedication but end it in dispute. For these reasons partnerships must be bound with agreements which are prepared in compliance with legal procedures and which show mutual rights and responsibilities clearly.
- In a successful partnership or cooperation, it is very important to create synergy. In other words, partners should have different skills which complement each other in a positive way. (For example, one partner is experienced in production techniques, the second one in marketing and the third one in finance). Being good friends and sharing similar characteristics is a condition which lowers the chances of being good partners. The important thing is to be able to create positive synergies out of differing abilities. It should not be forgotten that such differences could turn into a negative synergy unless they are well harmonized. This is also a very important subject for Turkish SMEs in their search for cooperation. It is possible to increase the benefits of cooperation by gathering SMEs in events such as fairs and by informing and educating them about the merits of acting together.

Another point we wish to emphasize is related with the lack of ability in conducting feasibility studies and the insufficient quality of these studies which is especially a problem for the micro and small businesses. In Turkey, the typical investment scenario of small enterprises is generally as follows: A person who has money makes an attempt at establishing an enterprise and considers being an entrepreneur as easy. He just looks around and selects a business idea (a product) to invest in among those which seem to be most profitable or which seem to have the largest sale potential. This results in an increase in the supply of this product and a decrease in its price hurting his business as well as those of his competitors. In the end, most of these businesses begin to operate with idle capacity which increases their costs, and they become unable to compete in the market. In fact, most of the small enterprises in the manufacturing sector are scheduled to work one shift per day and their costly CNC (Computer numerical control) machines are only operated for 1-2 hours per day. Majority of these businesses have bought their own CNC machines because they just imitate their neighbours.

This scenario can be changed only by informing and educating these enterprises and conducting feasibility studies based on relevant and up-to-date information. Here we can say that, the main SME problems that require attention are related with marketing. These are; conducting market research, identifying the target group of customers and analyzing competition in a proper manner. This problem is also worsened as the size becomes smaller from medium to small and micro.

V. SME POLICY AND STRATEGY RECOMMENDATIONS TO ACHIEVE SUSTAINABLE AND SUCCESSFUL ECONOMIC GROWTH IN TURKEY

The State’s evaluation of SMEs and SMEs’ expectations from the State

The objectives set forth by the State to develop SMEs in Turkey and related expectations and evaluations have been analysed in the Third Chapter of our Report within the framework of the development plans and SME Strategy and Action Plans. As it can be seen from this analysis, SME

related issues were raised for the first time in the Fourth Five Year Plan (1973-1983) in which the concept “small industry” was introduced. In this period, the terms “small enterprise, small and medium enterprise (SME), enterprise and entrepreneur” were not in use. We can observe that “small industry” continues to be the preferred term in the Fifth Five-Year Plan. The only difference in the Fifth Plan is placing the small industry in the same category as the artisans-craftsmen (this is a result of the pressure exercised by TESK). In other words, there is no difference between the perspectives related with SMEs in the Fourth and Fifth Plans, both of which handled the issue from the point view of small industries. In the Sixth Plan (1990-1994), although the expression “small enterprise” was used, the objectives and incentives were targeted to the small industry sector. The services and trade sectors were not included in the incentive schemes.

The establishment of KOSGEB in 1990 is an important achievement. As indicated in its Establishment Law, KOSGEB is a State Agency exercising its activities only for the manufacturing sector. It is understood that the concept “small industry” representing the SME perspective of that period also prevailed in the Establishment Law of KOSGEB. Again in the same period, the establishment of TOSYÖV in 1990 and KGF in 1992 were signs of increased interest in SMEs. In fact, the Seventh Plan reflects the results of a change in the perception towards SMEs.

In the Seventh Plan (1996-2000), we can see that the SME concept became a more distinctive concept with efforts to align SME incentives with the EU practice. In this plan it is clearly visible that the term “small and medium enterprises” replaced the former expressions “small industry” and “small enterprise”. However, in this plan the manufacturing sector (industry) continues to be the targeted sector for the incentives. This is a natural consequence of the fact that KOSGEB Law only covered the manufacturing enterprises. It is envisaged that the new draft legislation of KOSGEB which is currently being debated in the Parliament will cover the services and trade sectors along with the manufacturing sector. The new law is expected to be enacted soon. An important change in the Seventh Plan is the introduction of the concepts “entrepreneurship” and “start-ups”. Moreover, the innovation and technology potential of SMEs is emphasized along with their employment generation ability and it is stressed that this potential must be effectively exploited.

In the Eighth Five-year (2001-2005) and Ninth Eight-year (2007-2013) Development Plans, the concepts such as entrepreneurship, innovation and value added etc. are dealt with in a more comprehensive manner in relation with SMEs. Objectives which include “increasing the competitive capacity of SMEs”, “increasing the value added created by SMEs” and “maintaining sustainable growth” are clearly stated in these plans. In the Ninth Plan, “entrepreneurship” has gained greater attention and was placed in the first place in the category of SME policies.

These developments are seen more clearly in the SME Strategy and Action Plans (KSEP 2004 and KSEP 2007-2009). As indicated in Chapter III.3 of our Report, ten strategy fields of KSEP 2004 and five strategy fields of KSEP 2007-2009 present the objectives which clearly reflect the above mentioned developments in SME policies. As also stated in this chapter, KSEP 2004 and KSEP 2007-2009 objectives are in compliance with the Eighth and Ninth Plans. A criticism here could be related to the formulation of general objectives rather than identifying numerical and measurable targets in KSEP 2004. This renders it difficult to monitor the level of their achievement. For this reason, monitoring and evaluation work has not been carried out although the institutions assigned to fulfil these objectives were identified in the Plan. Additionally, we need to admit here that monitoring and evaluation of this subject is not being taken seriously. Assigning more than one responsible institution for each target may have created further difficulties for monitoring.

Although the majority of objectives in KSEP 2007-2009 are again in the form of general expressions, in contrast to KSEP 2004, there exist some numerical and measurable targets also. However, it is not clear which criteria were adopted in identifying these numerical targets. Success indicators and possible sources of finance are not shown in these reports either.

We wish to reiterate here one criticism which we also placed in Section III.3 of our report concerning KSEP reports as it refers to an important weakness of State SME policies: The target group of all the objectives and action plans has been defined as SMEs in general. There is no attempt to separate SMEs under different categories with respect to size, sector, level of entrepreneurship etc. and identify the objectives and actions accordingly. However, it is a fact that different segments will have different needs and problems. For example, the needs of an SME operating in a high technology field are different from the needs of a small maintenance-repair firm. Similarly, an SME with 3 employees is different from another one with 200 employees. There are many other areas of differentiation including sector based differentiation. For this reason, it is necessary to develop and implement different support packages for SMEs which cover diversified elements for different segments.

However, there is a more clear-cut picture of the expectations of SMEs from the State. Whereas monitoring and evaluation work has not been carried out, as indicated previously, in relation to the development plans and KSEP on the side of the State, a number of sector based and regional associations, academics and NGOs conducted empirical studies. These studies have generally reached the same results regarding the expectations of SMEs from the State. In almost all of these empirical studies, “financial problems” of SMEs are placed as a priority in the list of the bottlenecks of SMEs. This is an expected result when we consider that the share of SMEs in bank credits remained at a level of 5% until 7-8 years ago. But now this share is estimated to grow to 20-25% after the banks in Turkey selected SMEs as an important market segment and they expanded their “SME Banking” activities.

On the other hand, SMEs do not put forward their financial problems in the form of “unmet credit demands”. They require subsidized loans with low, even, zero interest rates. In fact zero-interest loans (interest subsidy) have become a state support tool for SMEs in recent years. These are being implemented by KOSGEB whose responsibilities are defined as non-financial support to SMEs in its Establishment Law. KOSGEB interest subsidy support has become to be known as “KOSGEB Zero Interest Loan” among the SMEs. In short, SMEs perceive their finance problems as the need for heavily subsidized loans. Large enterprises are very skillfull in obtaining these subsidized loans. The fact that we live in a country where earning money through subsidies in place of competing under market conditions has become a habit and especially large enterprises are very skilful in this respect raises this question: “Do we need to reproach SMEs?” Our answer is “Yes!”. Because business ethics is an indispensable concept for SMEs which create a “nursery of entrepreneurship” in our societies.

However the financial problems of SMEs are generally the result of other problems rather than being a direct problem. Insufficient or incorrectly done feasibility tests, marketing and management mistakes and production system errors manifest themselves as financial problems. Financial problems can be likened to “raising body fever”. It is necessary to unveil the reasons behind the symptom instead of temporarily treating the fever with Aspirin. The underlying reasons must be researched in terms of the other management functions like marketing, procurement, production etc.

There are also, of course, real financing problems of SMEs. These mainly include difficulty in accessing loans (especially for micro and small SMEs), lack of widespread use of credit guarantee facilities and venture capital schemes, difficulty in accessing capital markets and the lack of availability of information and consultancy services.

“Lack of demand” is placed in the second row in the list of SME problems analysed by these empirical studies. This problem also has its roots in basic marketing problems such as incomplete feasibility studies and market and customer analysis. In other words, a lack of understanding of the importance of demand and competition analysis, and the importance of new products and supplies contribute to this problem. We wish to emphasize here once more that the answer of the question “what should the State do?” needs to be based on the following principle: “Inform SMEs, do not subsidize them”.

SME policy and strategy recommendations in this section of the report are based on the above mentioned evaluations. Since general SME and sustainable development policies and strategies for Turkey are available in a number of national and EU reports (the Lizbon targets)⁸, they will not be repeated here. More specific recommendations will be presented instead.

Institutions responsible for SME development should consider the following objectives to be included in their policies:

- The competitive power of SMEs should be increased at the global level
- The value added created by SMEs should also be increased
- The competitive power and added value of SMEs should be increased in a sustainable way.
- The establishment of new enterprises should be facilitated and encouraged. A favorable environment should be created so that people can set up their own businesses. This is particularly important for Turkey which has a young and healthy population. This potential can be utilized provided that the young populations are offered technical, occupational and entrepreneurship training at a satisfactory level.

What should the State do?

- The State should adopt an SME policy that assures the delivery of healthy, up-dated and correct information to SMEs. Subsidies must only be considered if necessary. Those SMEs that are able to use information in an effective way should be in a winning position, not those that manage to obtain subsidies. In reality a large portion of subsidies go into the hands of large enterprises. For this reason SMEs should not favour a policy towards subsidies.
- To earmark a share (quotas) for SMEs in public contracts will help them very much to increase their effectiveness. Depending on the subject matter of the contracts, allocations can be made solely for micro, small or medium enterprises.
- The prices of the goods and services provided by State Economic Enterprises (KİT), Municipal Economic Enterprises (BIT) and other public organizations should be stabilized. In this way the entrepreneurs can deal with uncertainties in the market. Thus, they will be encouraged to take risks and take seriously their obligation plan well before implementing any action.
- The State should invent mechanisms to provide security for the quality of goods and services produced by SMEs. This is important for small and particularly micro enterprises. Helping SMEs in this respect will increase their chances of entry into foreign markets. The “Turquality” Project is an important step in this regard. This project needs to be made more effective and widespread.
- In Turkey, Investment Incentives are generally provided for capital investments (investment allowance, accelerated depreciation etc.). Employment generating investments are almost punished through considerably high taxes. As a result of this, SMEs show a tendency towards unregistered employment. For this reason the level of informal employment is quite high in Turkey. This results in an illegal practice among enterprises on one hand and on the other, creates unfair competition, lowers the general performance of economy and destroys the order of competition. When we consider the fact that labour intensity increases as the size of the enterprises gets smaller, we can state that the existing tax policy in Turkey does not favour SMEs. This is particularly a problem for small and micro enterprises.
- The impact of regulations on SMEs should be assessed before they are put into effect (“Think Small First” Principle). As the enterprises get smaller in size, regulations have a more

⁸ SME Strategy and Action Plan for 2007-2009 and other strategy documents have been prepared in consideration with the Lizbon targets for SMEs (strengthening the spirit of innovation, achieving a conducive environment, facilitating access to research and technology, improving access to finance, promoting top-class business support for SMEs)

discouraging effect on them. Creating a conducive environment for entrepreneurship would bring a greater number of young people, who make up an important strength of our country, to the stage of entrepreneurship

- State aids (including tax incentives) and supports should be designed by taking into account technological changes, sustainable energy consumption and environmental issues in addition to economic development targets. They must be arranged in parallel to the diversified needs of different SME segments (number of employees, field of activity, employment generation potential, sector and location). It should be remembered that some sectors or businesses which are not popular today might gain enhanced economic value in the future.
- The burden created by tax, social security and other obligations on enterprises and the compliance costs (bureaucracy) should be reduced. The opportunity cost of bureaucracy is very important for SMEs, particularly the SMEs which have a smaller size.
- Measures to encourage SMEs to use their own funds (equity) for their investments need to be introduced. If the alternative cost of their own funds (opportunity cost) is considered to be an equivalent of the interest cost of borrowing, a reduction in income tax can be applied similar to some European countries (e.g. Belgium).
- Information and database services and tax concessions similar to the EU countries should be made available to ensure smooth implementation of the business transfer process. Encouraging and facilitating business transfers may help achieve an important step for the development and growth of small enterprises in our country where entrepreneurship is not recognized as a career requiring some skills. Instead, it is generally thought that ownership of money is a sufficient condition for setting up a business. Business transfer becomes a more important subject when we consider the facts that most of the businesses are faced with many problems after the take over of second or third generations, and enterprises over 100 years of age have not been able to grow at all.
- Supports in the form of grants should be provided to encourage the establishment of new enterprises. In this respect, training and consultancy networks should be set up and business incubators should be established.
- State aids should be given in a way to ensure the development of market instruments (such as private institutions, public-private partnerships, etc.) which can meet the debt and equity finance needs of SMEs. It should be remembered that supporting SMEs through interest subsidies might delay the development of these market instruments.
- For an effective and efficient use of the public resources, eligibility criteria (sustainability of the activities to be supported, unit cost, performance criteria etc.) for the public grants or supports should be well respected. Enterprises undergoing financial difficulty should be evaluated under a separate category. “Business transfer” should be distinguished from “business closure due to failures”. Supporting the SMEs in the latter case by extending their survival can not be a valid economic argument. This can only be accepted from a social perspective. The former case (the change of the owner of the enterprise), however, must be encouraged. Bureaucracy must be reduced and the business transfer process must be facilitated through tax concessions. If the ownership is transferred to more competent people the performance of both the enterprise in question and the whole economy will be enhanced. This is a very important issue for Turkey.
- Widespread use of a venture capital system which is adapted to the circumstances in Turkey must be ensured. This is crucially important in Turkey for putting the prospective young entrepreneurs on the stage.
- A legal infrastructure necessary for expanding the micro-finance mechanism should be established
- Innovative credit guarantee mechanisms (mutual guarantee, etc.) should be activated.
- Enterprises must be supported for generating additional jobs especially for disadvantaged groups
- An SME Observatory must be prepared periodically (for example once every two years). This practice has been adopted by the European countries and many other countries. Starting a similar practice in Turkey will have very positive effects on the performance of SMEs and all

of the other enterprises, since the experiences accumulated in the past are a valuable asset for the future.

- It is important to amend the KOSGEB law in a way to cover other sectors, particularly the services sector, along with the manufacturing sector. The importance of such a change will be understood better, if we consider the fact that economy of scale is effective predominantly in the manufacturing sector and much less effective in the services sector.
- The incentives covered by the current system are generally directed at established enterprises. Incentives for start-up businesses are rarely introduced and when they are they are usually in limited amounts. It is very important to encourage entrepreneurship and new businesses in all aspects in a country like Turkey which has a young, healthy and ambitious population. In this context, care must be taken about the following points which might otherwise turn into a discouraging factor for setting up new businesses:
 1. Cost of company registration (keeping the costs at a low level),
 2. Procedures for the establishment of companies (simplifying the cumbersome procedures, reducing bureaucracy, shortening the duration)

The experiences of the USA, Canada and Australia, which have gained real success in this respect, should be studied carefully to derive lessons for Turkey.

- The following are two essential conditions (sine qua non) of public SME policies:
 1. A clearly and narrowly defined SME policy (defining clear objectives in terms of scale, sector and regional dimensions). Country examples dividing SMEs into more than 10 segments can be considered in this respect.
 2. Policies in the fields of finance, cooperation, R&D, university-industry cooperation, technoparks etc which aim to support high growth and high value added SMEs at individual, sector based or regional levels

Ireland is among the country examples which can be studied in this regard.

- Specifying clear and narrow objectives will increase the efficiency of incentive policies by eliminating or minimizing any conflicts that might occur during the implementation of these policies. For example, trying to generate employment, create value added and increase the volume of exports with only one type of incentive are conflicting targets. Selecting only one target or at least giving priority to one of them is essential to have an effective incentive system.
- Although the policies are designed clearly and narrowly in the beginning, they are spoiled after the lobbying efforts of different sectors and/or regions and in line with divergent interests of different ministries. It should be remembered that the failure of the incentive system does not result from policy errors but from spoiling the system with the above-mentioned reasons or other reasons (for example, specifying exactly the same incentive standards for all of the 49 provinces has led to success in some provinces and limited success in others).
- Tax arrangements are an important field of SME policies. Tax policies need to be differentiated according to size, regions and sectors.
- We believe that the following points should be taken into consideration in the design of SME incentive policies aimed at eliminating regional disparities and developing the priority regions.
 1. Switch to a regional minimum wage system: This system is being implemented in many countries including the USA, Japan, Canada, Mexico, China and India. Initiating such a system in Turkey will create many economic and social benefits
 2. Labour taxes and insurances can be waived for a period long enough (10 years for example) to attract investments. This will be a solution for the unemployment problem deeply affecting these regions
 3. Removing energy taxes in these regions for a specified period (like 10 years) will create similar effects
- Turkey's exports to eastern and southern neighbours have increased in an appreciable amount in the recent years. Most of the frontier regions are the underdeveloped regions of Turkey. It could be an effective SME policy for these regions to support enterprises, which deal with

employment and export generating activities and which create value added by using domestic raw materials through EXIMBANK Export Credits.

What should the SMEs do?

SMEs should place their priority on getting organized. There are a lot of SME organizations in Turkey which compete with each other. They can increase their effectiveness by acting together. They can lobby for SMEs or provide direct support to them such as training, information, R&D, domestic and foreign market survey, matchmaking events for business cooperation etc. It can be possible to mobilize the potential of university-industry cooperation by means of these organizations.

SMEs should:

- get into the habit of identifying short, medium and long term strategies, revising these strategies as required and preparing written plans so as to achieve their technology and innovation targets towards increased productivity, new markets and new market opportunities, growth and increased competitiveness. They should understand the benefits of obtaining professional consultancy services look for existing resources in this regard and try to access these resources. Realistic strategies and plans are very important tools by which SMEs can promote themselves to their suppliers, new markets, customers and potential partners.
- try to find measures to reduce their costs, decrease energy consumption and environmental impacts by carefully examining their processes. The results of applications to reduce the use of energy and raw materials and to decrease the amount of wastes should be monitored.
- cooperate with other SMEs in the same sector for joint use of resources and collective purchase of goods and services and expand their networks in this regard. 96% of SMEs in Turkey are micro enterprises. The majority of them are in the bracket of 1-4 employees. When we consider that 3% of SMEs are small enterprises in Turkey, the importance of scale economies and creating a synergy among these enterprises becomes apparent. Thus, cooperation and merging among these enterprises will bring competitive advantages to them. Otherwise, it will be impossible for these enterprises to grow and even survive in the global competitive environment
- behave as responsible entrepreneurs
- provide healthy and safe business environments for their employees and help them to develop their careers.

What should the non-governmental organizations do?

The number and importance of non-governmental organizations (NGOs) in Turkey have gradually increased since the 1980's and continue to increase. There exist a large number of sector-based and regional NGOs especially in the SME sector (SİADs, GİADs, MUSİAD and others). In addition to this, nearly 300 industry/trade chambers have been organized under TOBB as semi-public institutions. Furthermore, there are the unions of artisans and craftsmen established in every province which operate under the umbrella of 12 federations. These federations are functioning under the direction of TESK which is the national organization. This means that NGOs have a power in the SME sector which must be utilized in an effective way.

Non-governmental organizations should:

- be able to acquire necessary knowledge about SME needs, problems and their solutions and make policy recommendations in this regard.
- display an innovative and entrepreneurial approach in conducting their activities. Behave as social entrepreneurs.
- implement projects and activities to satisfy the needs and problems of SMEs by utilizing national and international resources.

- establish networks and develop instruments to allow SMEs to access necessary training and consultancy services.

What should the large enterprises do?

Recently, outsourcing has become an important tool of large enterprises to increase their competitive advantage. This creates a big potential for SMEs to set up symbiotic relations with large enterprises. This potential must be effectively utilized by the SMEs in Turkey

Large enterprises should;

- publicise their procurement plans in the media accessible by SMEs.
- develop and implement instruments aimed at supporting SMEs in the fields of training technology, management and finance.
- establish and use necessary resources to be able to establish long-term strategic cooperation with SMEs (joint investments, joint Research and Development, technology transfer, etc.).
- remain loyal to Corporate Social Responsibility principles.
- be able to invent policies and solutions for the relevant sectors.

The above-mentioned recommendations listed for SMEs, non-governmental organizations and large enterprises also establish a framework for the support mechanisms which can be developed by the State.

As indicated in the beginning of our Report, the focus has been placed on the plans, strategies and investment incentives constituting only a part of State SME policies in Turkey. It would be useful to conduct similar studies in the fields of tax policy, technology, innovation, environment and energy. However, necessary arrangements must be immediately initiated for the preparation of a periodic SME Observatory which will thoroughly analyze SMEs in the context of all these issues.

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