The World in COVID-19:
The Impact of the Pandemic on the Development of Countries and Regions

RANEPA
THE RUSSIAN PRESIDENTIAL ACADEMY OF NATIONAL ECONOMY AND PUBLIC ADMINISTRATION

Centre for Entrepreneurship Research

COVID-19, small business and government support in Russia

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Relevance and purpose of the study

Small and medium business (SME) is a significant sector of the Russian economy (≈43% of GDP of the business sector, 38% of employees), a potential source of employment, diversification and economic growth

- pandemic and economic crisis → risks of rising unemployment and informal employment
- increased risks of automation and digitalization → growth of the role of entrepreneurship as a creative process (*an entrepreneurs cannot be replaced by robots?)*
- falling prices for resources, increasing risks for commodity companies and the public sector in Russia → essential to form an entrepreneurial economy

The goal is to identify factors of SME development in the pre-crisis period to assess the adequacy of support measures during a pandemic

Hypothesis: based on forecasts of changes in the initial factors, it is possible to estimate the scale of the decline in the SME sector

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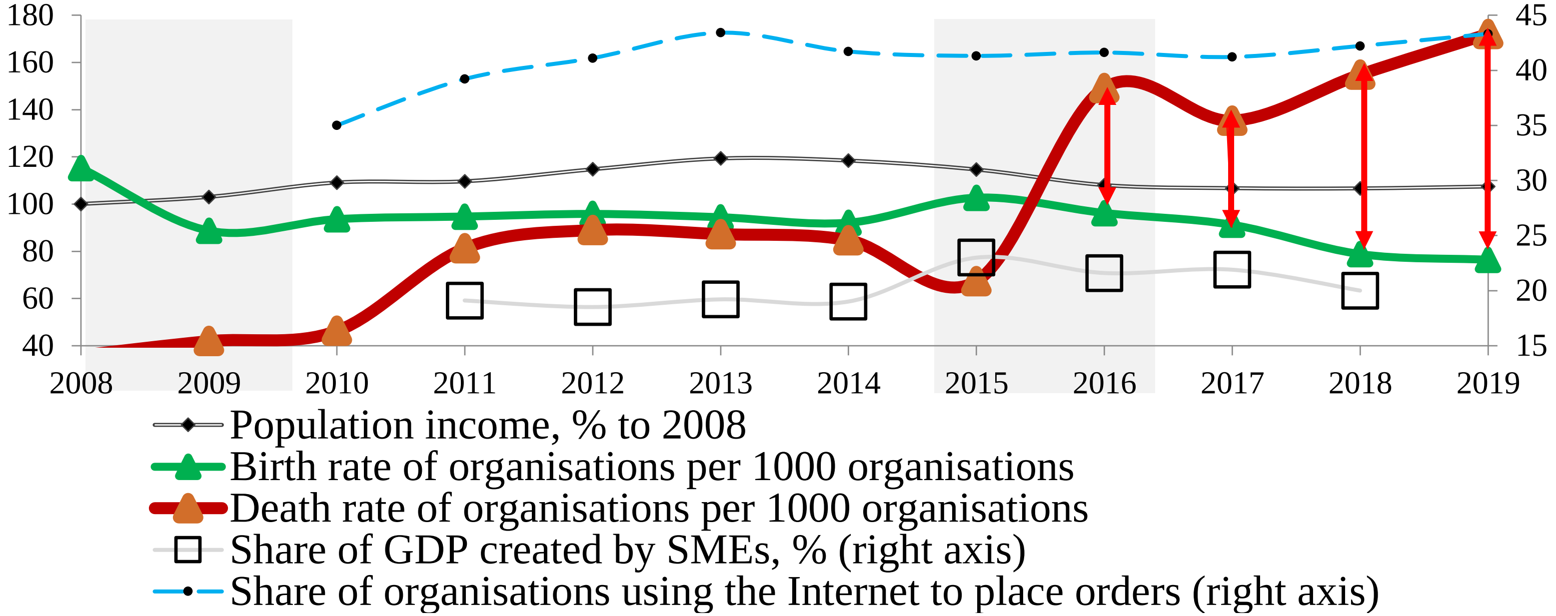
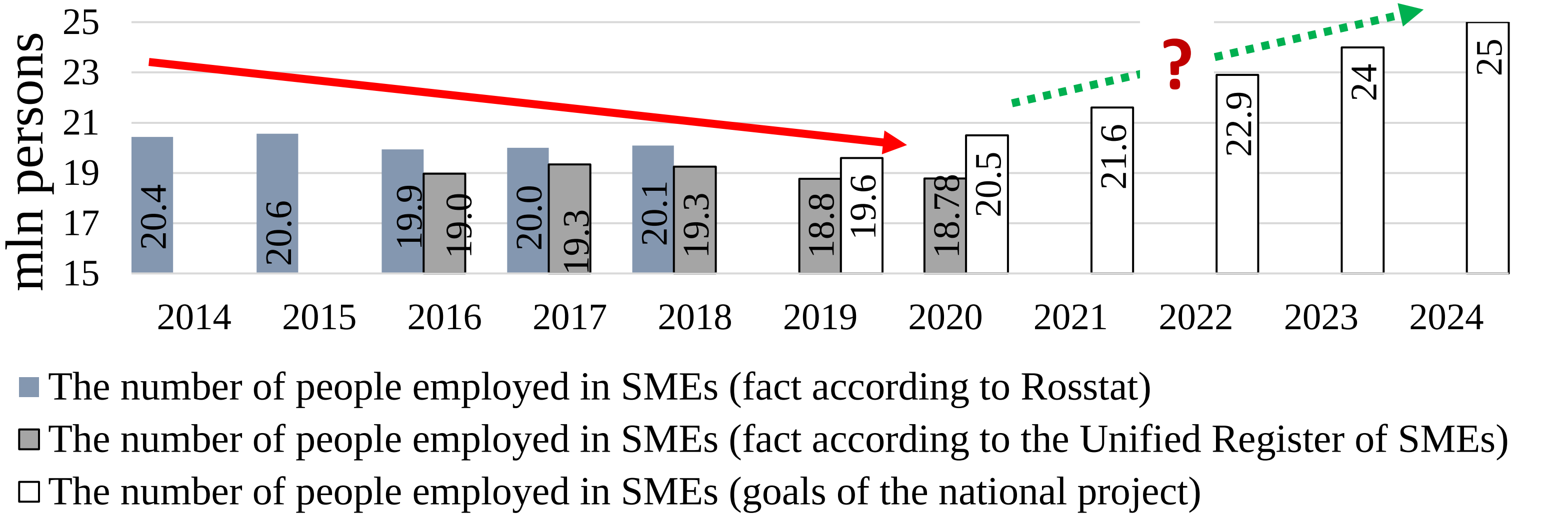
Contradictory dynamics of the SME sector until 2020

- SMEs declared as a federal priority: national project, SME strategy
- Decrease in the share of SMEs in Russian GDP in 2018 to 20.2% from 22%, increase of dearth rate of organizations after 2016 (figure ►)
- Reduction in 2019: -0.5 million SME employees (figure ►), - 100 thousand SMEs due to a drop in personal incomes, introduction of online cash registers and an increase in VAT
- In 2019, the share of those employed in the informal sector was 20.6% and was growing, although the self-employed were "whitewashed"

Does Russian state support work?





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Different business environment and vulnerability of SMEs

Types of regional entrepreneurial ecosystems in Russia

- 1 Entrepreneurial center
- 2 Developed diversified
- 3 Developed industrial
- 4 Southern diversified
- 5 Northern
- 6 Eastern
- 7 Southern underdeveloped

- High differences in geography and institutions
- **Best conditions:** largest metropolitan areas and coastal regions (market proximity)
- Weak ecosystems: the Arctic, the North Caucasus and the Far East: natural costs, remote markets, and poor institutions
- Weak ecosystems were more vulnerable during the previous crisis - the fall in 2015 was higher (!)

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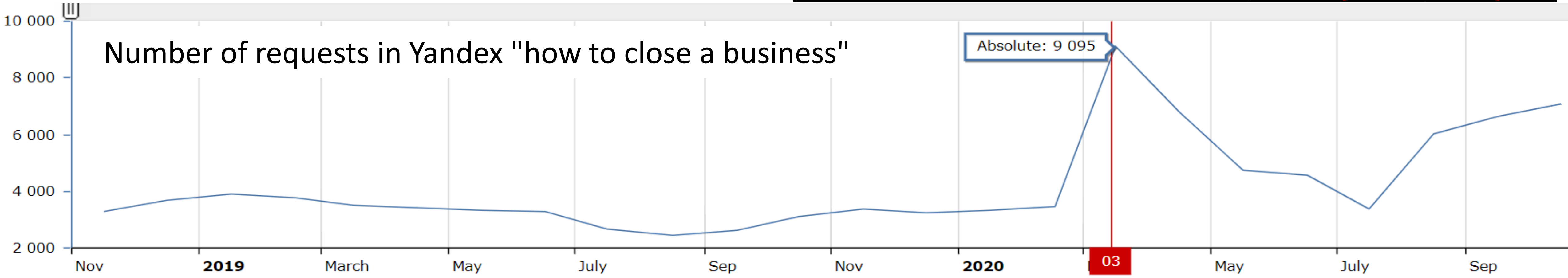
Downward trend of the SME sector in 2020

- COVID-19 affected about 75% (4 mln) of all SMEs and 63% of those employed in SMEs (12 mln persons) (figure ►)
- Number of web-requests "how to close a business" has doubled compared to last year (figure ▼)
- In the first half of 2020, the number of individual entrepreneurs ↓ by -18.2 thousand and firms ↓ by -107.8 thousand
- We will know the real scale of the fall only after 1-2 years (statistics)

Economic activity	SMEs employment, %	Number of SMEs, %
Total in the SME sector	100	100
Most affected by COVID-19 industries	5,5	11,2
hotels and restaurants	3,7	2,5
education	0,3	0,5
culture, sports, leisure and entertainment	0,6	3,9
provision of other types of services	0,8	4,2
Industries that may be affected by the multiplier effect	57,4	64,2
wholesale and retail trade; repairs	33,7	39,2
construction	9,5	8,7
real estate activities	6,5	6,7
transportation and storage	6,8	9,3
electrical energy, gas and steam	0,8	0,2
Total Affected	**62,9**	**75,4**



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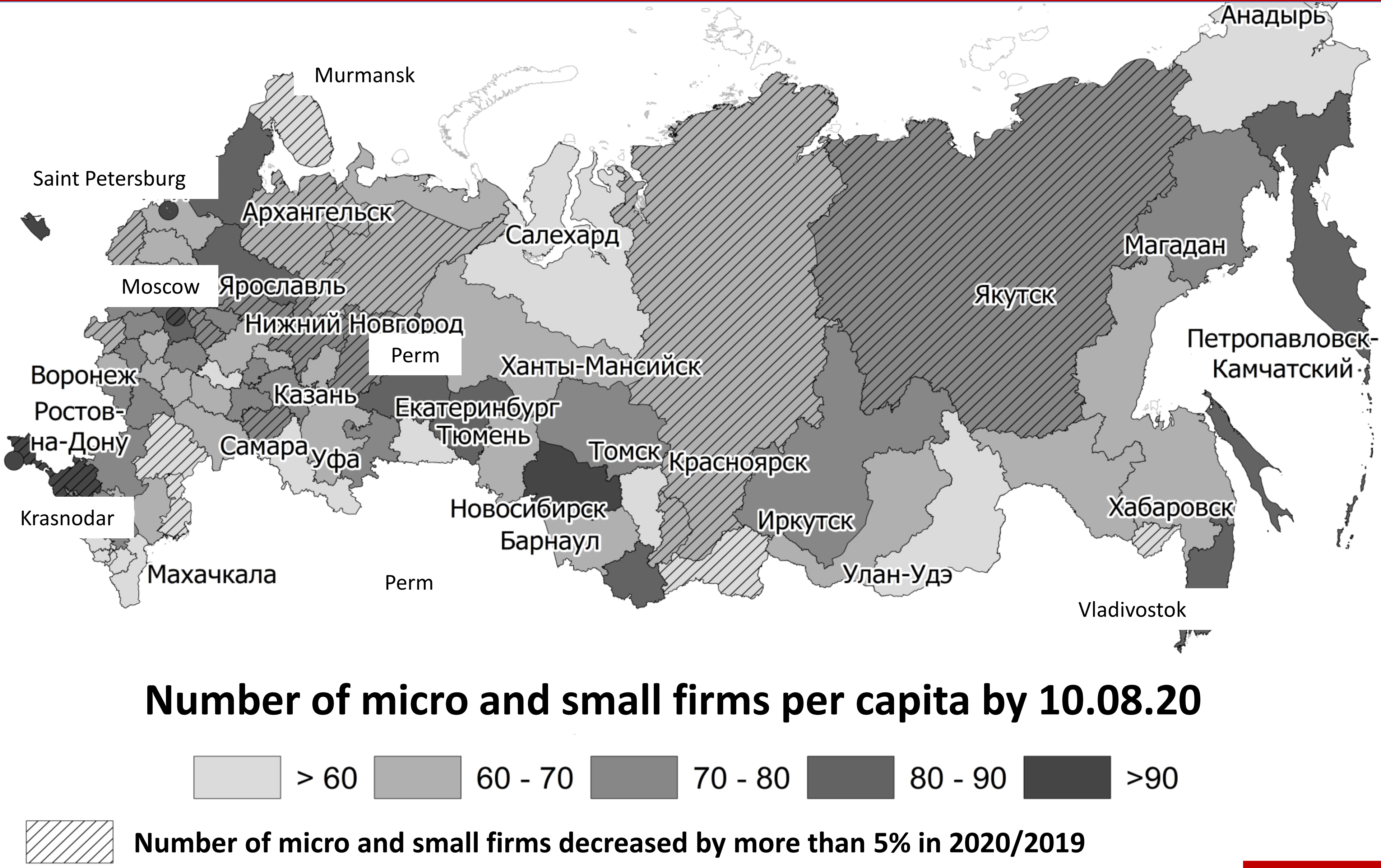
Geography and dynamics of the number of SMEs in 2020

- > 45% of SMEs - in 10 agglomerations
- The density of SMEs is higher, where there is demand (St. Petersburg, Moscow time, Novosibirsk), access to capital (+ Tatarstan, Tyumen) and market access (+ Kaliningrad, Primorsky, Krasnodar kr.)
- Sector ↓ after the pandemic in regions with vulnerable ecosystems (Ingushetia, Jewish region, Adygea, Komi, Tyva, Sakha, Crimea) but also in the largest agglomerations (Moscow, Perm, Samara Region) (!)



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Small business development factors in Russian regions

Dependent variable: **number of micro and small firms**. 83 regions. 5-10 years old. Fixed effects. Robust standard errors. All variables are logarithmic.

	Model number	(1)	(2)	(3)	(4)
Market	Population income (-PM), thousand RUB	0.40*** (0.068)	0.41*** (0.077)	0.46*** (0.090)	0.19 (0.15)
	Market potential, bln RUB	0.15*** (0.046)	0.12*** (0.040)	0.13* (0.070)	0.11** (0.043)
Human capital	Unemployment a year ago, %	0.14*** (0.047)	0.11*** (0.042)	0.14*** (0.044)	0.17 (0.12)
Capital access	Banking services availability index	**0.22** (0.10)**			
Digitalization	Share of persons with Internet access, %		**0.066* (0.036)**		
Public support	Tax incentives per organisation, thousand RUB			**0.032*** (0.0091)**	
	Subsidies for SME support a year ago, thousand RUB				**0.031** (0.014)**
	+control variables and constant				
	LSDV R^2	0.98	0.98	0.978	0.988
	Within R^2	0.54	0.544	0.47	0.12

Model introduction:
Barinova VA, Zemtsov SP, Tsareva YV. Entrepreneurship and institutions: Does the relationship exist at the regional level in Russia. Voprosy Ekonomiki. 2018; 6: 92-116

Do we need to save SMEs? The sector does not affect economy?

Entrepreneurial experience and skills (***Entrepreneurial capital***) is one of the factors of regional development through the implementation of new ideas and technologies and other mechanisms [Audretsch, Keilbach, 2004; Stephens, Partridge, 2011; Van Stel et al., 2005; 2008; Glaeser et al., 2014]

	Dependent variable: **gross regional product (per labor force)**. Fixed effect models. Period: 2004-2014. 79 regions. All variables are logarithmic	
	Constant	-8,863 *** (1,496)
Fixed capital	Share of investments in GRP, %	0,093 * (0,053)
Human capital	Average years of study	4,705 *** (0,629)
	Labour force growth rate + 5%	-0,100 ** (0,038)
Entrepreneurial capital	Micro and small firms per 1000 labour force (t-5)	**0,166 *** (0,050)**
	LSDV R^2	0,957
	Within R^2	0,715

- In regions, where the density of small business was **1% higher**, GRP was higher by **0.17%**
- Entrepreneurial experience and skills is a factor of long-term regional development in Russia
- Reduction in the number of entrepreneurs and undermining entrepreneurial intentions → long-term negative consequences for development

Zemtsov S, Smelov Y. Factors of Regional Development in Russia: Geography, Human Capital and Regional Policies. Journal of the New Economic Association. 2018;40(4):84-108.

WHAT IS HAPPENING?

- The SME sector ↓ and before the crisis due to a drop in income, the introduction of online cash registers and an increase in VAT; higher drop is expected in 2020 in most regions
- According to our model, with a reduction in world markets by **3%**, household income - by **5.5%**, the volume of banking services - by **5%**, it is possible the number of micro and small firms ↓ by **3.5-4%**, which is close to the data of the Federal Tax Service (about 4.3%)
- We can expect a drop in the Russian GRP in 2020 by **0.22-0.67%** (for different regions) only from a decrease in the activity of small businesses (!)
- Direct public support had little and lagged effect on SMEs development, covered a small number of SMEs before the crisis (**2-3%**)
- Potential SMEs development is related to digitalization and knowledge-intensive sectors: delivery, online services, Internet banking, etc.
- The most **serious social consequences** from the fall of SMEs can be expected in the North Caucasus and Crimea, where more than 50% of the employed are SME workers or self-employed, entrepreneurial ecosystems are underdeveloped and the level of digital inequality is high (in comparison with the largest agglomerations)

WHAT HAS BEEN DONE AND WHAT TO DO?

Short term (measures from regression factors):

- support for SME demand: subsidies for the poor, families with children, the unemployed, public procurement
- concessional loans to those affected but retained employment (≈4% of SMEs)
- tax breaks and deferrals for the most affected industries (but problems with OKVED!)
- wage subsidies are in demand (> 18% of SMEs every month), but not large - 26-30% of the average salary in Russia, in the OECD - 50-90%
- there has already been a moratorium on inspections; significant but not essential

Long term:

- digitalization of public services, transformation of the business climate, compensation for digitalization
- incorporating an ecosystem approach into policy
- retraining of the unemployed: digital technologies and entrepreneurship training, consulting
- reducing the digital divide: developing ICT infrastructure, educating the population and entrepreneurs

Thanks for your attention!

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- Zemtsov S., Barinova V., Semenova R. (2019) The Risks of Digitalization and the Adaptation of Regional Labor Markets in Russia. Foresight and STI Governance, 2(18), 84–96