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# Factors for Increasing the Competitiveness of Small and Medium-Sized Enterprises (SMEs) In Bulgaria

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## Abstract

The competition is the trigger force of any market economies. Under modern contemporary conditions, competition is determinative for the business development, while competitiveness is the most important condition for overall business prosperity. The area of small and medium enterprises (SMEs), having extraordinary potential for flexible adaptation to the economic circumstances in the country and changing market conjuncture – is of major significance for the national economic development. The accession of Bulgaria to the EU provides great opportunities for SMEs support and development. On the basis of the above – mentioned, we can conclude that the purpose of this article is to define and analyze the key factors for enhancing SME competitiveness and to outline the direction of their sustainable development in the new economic reality.

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*Keywords:* competitiveness, small and medium enterprises, sustainable development

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## 1. Introduction

The rapid technological change and market globalization have a great impact on business competitive environment and create new possibilities for reinforcing the development of small and medium-sized enterprises (SMEs). Modern knowledge-based economy can be said to comprise a wide variety of financial and production methods, creativity and innovation, expertise and high efficiency of human resources. Non-compliance with the rules of competition is to be removed. Competition, therefore, is no longer viewed exclusively at national or international level, but, today is recognized as having a global dimension as well. Accordingly, the European Union policies aim to ensure not only a more favourable environment for SME start-ups but also further development of the existing small and medium-sized enterprises and achievement of competitive advantages of the European single market. Moreover, the strategies of the new 2014-2020 programming period tend to focus on the European market economy for the 21<sup>st</sup> century and identify the main priorities towards the achievement of smart, sustainable and inclusive growth. Accomplishing these priorities will be possible through the help of competitive small and medium-sized enterprises (SMEs), which account for the largest share among the enterprises constituting the national, regional and European economy. This results in enhancing the interest to examine and disclose different aspects and encourages the search for novel managerial approaches to boost SME competitiveness.

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## 2. Enterprise competitiveness and factors for its identification.

The theory of competitiveness has its origin in the 1980s and complements the ideas held by the founding fathers of the classical economics Adam Smith, David Ricardo, Weber, Schumpeter, Sloan, Peter Drucker, Solow and others. Based on the classical theory of economics, the concept of competitiveness reaches its full development in the 1990s following the publication of Michael Porter's works. In his book "The Competitive Advantage of Nations", Porter identifies the sources of sustainable prosperity in modern global economy.

In scientific publications related to the issue of enterprise competitiveness there are pronounced differences of opinion as to the nature of this concept and yet there is currently no commonly accepted definition of it. The result of this, therefore, is a great disparity of views as regards the factors, methods for its assessment and the strategies for its enhancement. Some authors reduce or limit enterprise competitiveness to its product competitiveness (Lifits, Danailov, Ribov, Chobanyaneva, Hardy, Garvin, Hayes, Schmener, Kumar and Motwani). According to them, if the products are preferred and purchased on a given market, then the enterprise that offers them shall be considered competitive. Yet there are others who believe that the indicators of the marketing level and enterprise management should be incorporated into products competitiveness (O'Farrell and Hitchins). Furthermore, factors determining the products competitiveness also appear to include production efficiency, marketing experience and lower administrative costs (Pratten). Additionally, these factors are more likely to be also complemented by return on assets (Hayes, Clark, Wheelwright and Skinner).

A number of authors claim that what determines the very nature of enterprise competitiveness is its efficiency and effectiveness. Thus, part of them include the level of a given performance indicator, not taking into account its complex character, restricting enterprise competitiveness to high return assets (Müller, Geroski, Jacobsen, Waring, Besanko, Goddard and Wilson). Return on assets, return on equity and the percentage change of market share also tend to be enlisted as important indicators of enterprise competitiveness (McNamee, Varadarjan and Pride). Alternatively, there is a group of authors who argue that enterprise competitiveness is determined by its high resource productivity (Alan, Porter, Brayan, Tatsiopolous and Kosmetatos, Markusen).

Enterprise competitiveness is said to refer also to product competitiveness, production efficiency, financial position and organization effectiveness in terms of restructuring and sales and demand stimulation (A. Sergeev). The major weakness of identifying enterprise competitiveness with the level of performance and effectiveness of their activities can be exemplified by the static and short-term character of such categories. Another group of researchers endeavor to define the static features of enterprise effectiveness by connecting it with the long-term performance of its activities. "Competitive advantages reflect in higher productivity, and then in profitability. A company that is able to develop and uphold such opportunities that provide higher performance and sustainable profitability is considered competitive. In other words, the level of success or achievement of a given industrial company is equivalent to its level of competitiveness". (Avila). A comprehensive review of the existing literature draws us to the following definition of the concept of competitiveness: "Enterprise competitiveness is its ability through continuous renewal and improvement to create and maintain sustainable competitive advantages, leading to higher economic performance over long periods" (Velev).

It is this definition that could help us analyse the driving factors for increasing enterprise competitiveness.

The level of enterprise competitiveness is the result of numerous factors that tend to be of a highly dynamic nature at times. They imply a complex of conditions both external and internal to the enterprise, affecting the nature of its performance and the level of its success as compared to that of its competitors. Diverse factors for enhancing competitiveness, within the operating activities of the enterprise call for diverse managerial impacts. A great number of scientific research focuses on the factors for enhancing enterprise competitiveness, and yet the definitions they provide vary in their nature a lot. These divergences of opinion stem mainly from different understanding of the nature of enterprise competitiveness. In order to meet the page limit requirements, the key factors for enhancing enterprise competitiveness are presented in the paper in a rather systematic way.

A particular mention is made in the annual report of Bulgarian Small and Medium Enterprise Promotion Agency of the fact that the favourable business environment is the main aspect that impacts upon the enterprise competitiveness. Such an environment involves the following key factors: state government, the quality of the institutions, the infrastructure, technological and innovation development, the quality of the human resources, liberalization of economy, financial system and business strategies. Another classification attempts to divide the factors for enterprise competitiveness into three separate groups:

1. Factors of the surrounding environment covering:
  - Macroeconomic conditions-economic growth, level of national income, concentration of wealth, inflation, interest rate, exchange rate;
  - Political conditions- economic freedom, bureaucratic procedures, the overall system of taxation, incentives and subsidisation, trade agreements with other countries, export and import quotas;
  - Infrastructure – telecommunications, electric power system, transportation, system for environmental protection.
2. Industry-level factors:
  - fluctuations- price elasticity of demand, income elasticity of demand, seasonal fluctuations;
  - competition-international level, coalitions between organizations, competition, strategic alliances;
  - suppliers- availability and quality of incoming resources, localization, concentration of supply;
  - Clients- localization, concentration of sales, financial health.
- 3 Enterprise(company)-level factors:
  - expenses or expenditure - raw material costs, labour costs, storage costs, cost of capital;
  - technologies- technological processes, products, investment in research and development, owned patents;
  - quality of processes- production processes, level of automation, level of incoming resource utilisation;
  - flexibility- a new product development and production-switching time, length of the production cycle;
  - product quality –product mix, price, design, consumer satisfaction;
  - distribution - new markets for the existing products, timeliness of supply;
  - innovation-successful introduction of new products to the market, time for the development of new products, company culture;
  - marketing-reputation, brands, stimulation of sales;
  - human resources-remuneration, training, career development;

The main factors, identified on the grounds of the above analysis, with a critical impact upon the enterprise competitiveness, can be summarized in the following areas:

- access to finance;
- innovation activities;
- intellectual property-related activities;
- internationalization;
- Implementation of best practices.

### 3. Methodology

The situation in the SME sector is reviewed mainly within 2012-2014 period. The standard statistical indicators for the sector, published by National Statistical Institute (NSI) are extended and improved by a nationally-

representative empirical study into SMEs, conducted in 2014. For the purposes of the present analysis, use is also made of research data from other studies as well as related statistics and reports referring to SMEs in the EU.

The main purpose of the analysis is not only to examine the current status or standing of the SME sector, the potential for the development of the overall activities of a given enterprises, but also to assess the effects of the factors for SME competitiveness impacting upon their business performance under conditions of economic recovery.

For the purposes of the study, enterprise competitiveness is viewed as a potential for achieving high productivity, grounded upon a creative approach towards human, capital and physical resources. The existing situation in the SME sector and its ability to overcome the difficulties caused by the global financial crisis are examined through the prism of five key factors for sustainable development and competitiveness— access to finance, innovation activities, intellectual property-related activities, internationalization and implementation of best practices.

### *3.1. Access to finance*

According to the most recent EC research study as to the access to EU's SME's access funding conducted in 2014, this access comes second in importance among the difficulties facing SMEs in the EU (following that of identifying consumers). The study conducted for the purposes of the present analysis shows that during the period under survey the most common funding sources for Bulgarian SMEs were the means of the owner (62% as compared to 42% in 2013), loans from family or friends (24% as compared to 17% in 2013) and bank loans (15% investment loans and 20% working capital (operating) loans, while for the previous year these shares were 14% each.

86% of SMEs do not have sufficient resources of finance necessary for every single investment activity. About 38% of SMEs made a purchase of machinery or equipment last year (90% of the medium and 30% of micro enterprises), and around 28% invested in the training of their human resources (80% of medium and 20% of both micro and small enterprises).

Financial instruments under European funds were implemented by 6% of SMEs, although 26% of them claim they are aware of the respective programs and funds set up to foster and assist entrepreneurship. Funding through government programs or other local and international programs encompass 3% of SME (which reveals a congruence of range with that of the last year— 4%). According to Bulgarian Industrial Association (BIA) research study, the main part of the business (about 80%) stipulates that burdensome procedures requiring undue documentation when applying for European projects and accounting for their usage are the most significant problem that hinders the use of their funds as effectively as possible. The results of the study suggest that some of the problems encountered in the process of absorption of EU funds are: delay payments on projects (around 70%) and the need for ensuring sufficient financial resources for the particular purposes of the project (about 30%).

### *3.2. Innovation activity*

It is generally recognised that in our modern knowledge-based economy characterized by accelerated pace of change, increasing complexity and insecurity, the capabilities of the companies to adapt to the external environment and to remain competitive is closely linked to their capacity for innovation. Not only the growth but also the survival of SME is largely dependent upon the ability of the companies for continuous innovation. Creating new knowledge or combining existing knowledge components in a new “entrepreneurial” way are thought to be the necessary prerequisites for every innovation. The share of innovative small enterprises has increased from 17% to 20.3%, of the medium - from 26.4% to 32% and that of the large ones- from 52.7% to 59.2%. Enterprises from the industry sector (sectors B, C, D and E) are more resourceful in their pursuit of innovative applications as compared to those of the service sector—23.8% and 14.5% in 2012 and 29.2% and 16.3% in 2014 respectively.

The study conducted among SMEs for the purposes of the present analysis indicates that during 2013 the most common type of innovation activity in Bulgarian SMEs had to do with the changes in business processes designed to bring about optimization and cost reduction. Two thirds of the medium and slightly more than one third of micro and small enterprises were reported to have undertaken such activities.

The least popular innovation activity was related to the promotion of joint initiatives in the sphere of education between a given enterprise and academic institutions— only about 9% of SMEs were actually involved in such an initiative last year. However, in this particular case, as in all other innovation-related activities, observed is a strong impact of the size (scale) of the enterprise. In medium-sized enterprises innovation-related activities are several times higher than those in micro and small-sized companies.

In 57% of SMEs there appeared to be low innovation activity, in 25% — slightly low, 10% — moderate, 6% — slightly high and only in the still small or rather negligible proportion that amounts to 2% of the enterprises — high innovation activity. In general, in 2014, detected is a tendency for increasing the level of the innovation activity as compared to that in 2013. Nevertheless, the level of the innovation-related activities undertaken by the Bulgarian enterprises is still very low.

### 3.3. Intellectual property

In a knowledge-based economy, increasing number of the sources of competitive advantages move progressively towards the assets of knowledge, which necessitates a change in business strategies. For M. Porter this is a movement from the effort to be “better than the rivals” towards the effort to “deliberately choose a different set of activities to deliver a unique mix of value”. To create such a value companies must possess unique abilities. This shifts the focus of the strategy from operational effectiveness to development and deployment of key or unique set of capabilities. These capabilities are based on the unique for the company technical knowledge and operational practices, processes and methods. That is how the changes in the new economy lead to an increase in the strategic role of the intellectual property (IP), which also applies to SMEs.

In 2013 10% of SMEs had registered brands in Bulgaria (their home country), with 6% -in a foreign country, in 2014 the proportion of those that had obtained brand registration (home and/or overseas) is 13%. With patents no change is noticed in these registrations, being at the time approximately at the same level as they were last year - 7%. Discerned is a much more pronounced polarisation as to the registered intellectual property dependent upon the size of the enterprise — 42% of the medium enterprises have registered brands as compared to 9% of micro companies. A similar tendency is also revealed in the case of the registered patents— 14% of medium as compared to 3% for the small-sized enterprises.

### 3.4. Internationalisation

The reasons for the globalization of the small business and those for the expansion of the large companies are almost the same. Initially the studies into the SME sector focused on barriers to their internationalisation. Only later studies revealed that due to the new technologies and the policy of deregulation, these barriers become less relevant. Consequently, research studies seem to be directed at identifying best ways and means to a successful internationalization of SMEs.

According to an EC study, a significant number of the European SMEs are engaged in international activities, but a small proportion of them are reported to have expanded their business outside the European single market. The two most common forms of internationalization are export and import: 25% of SMEs in the EU are export-oriented, of which about 50% also export outside the internal market (13%); 29% of SMEs are import-oriented, and again 50% import from the countries outside the internal market (14%). Additionally, 7% of the European SMEs have

entered into technological cooperation with foreign partner enterprises; 7% are subcontractors of foreign partner; 7% have foreign suppliers; and 2% participate actively in Foreign Direct Investment (FDI).

*The number of the export-oriented companies among Bulgarian SMEs is relatively small— 11%. The only indicator they are considered slightly above the average for the EU is the proportion of the export-oriented companies among the medium-sized enterprises (58%). The proportion of the export-oriented micro enterprises is 10%, whereas that of the small-sized - 15%.*

Import-oriented represent/form 19% of the SME sector. The proportion of the medium import-oriented enterprises is the same as that of those that are export-oriented (58%). As for the import, discerned is a much more pronounced presence of micro- and small enterprises – with the proportion being 17% and 22% respectively, as compared to those for the export. In 2013 there was a marked growth in the SME sector foreign trade on a year basis with the proportion of the enterprises achieving export sales, more than doubled from its 2012 levels, whereas the proportion of SMEs reporting import increased with 7%. The proportion of the SME that took part in trade exhibitions, expos or trade fairs remain relatively low (12%), which is a significant decrease as compared to that of the previous year (18%). Approximately one fourth of the entrepreneurs declare they have obtained information about international markets and contacts with potential partners. The participation of SMEs in cluster activities refers to a low proportion of the enterprises— 10.6%, despite the significant increase of the indicator as compared to its last year levels (4%). 10% of micro-, 15% of small and 19% of the medium enterprises take part in such activities.

### *3.5. Best practices: ICT, human capital and strategic management*

Schumpeter conceptualized the entrepreneur as a main agent of economic change, because, above all/primarily, they are innovators as regards the products, markets, raw materials, production methods and the organisation. Unlike this understanding, there are other economists who emphasize the entrepreneur's role and their importance for the acquisition and processing of information. They believe the entrepreneur is not necessarily the source of a change, but rather the one who is more adequately responding to the change. Such a perception of entrepreneurship seems to correspond better to the new global economy, in which changes stem primarily the external environment and in which the access to the necessary information (about products, markets, technologies, etc.) and the capacity for its processing are crucial factors for success. Global economy increasingly becoming an intricate complex of business networks, based on the new ICT. Companies, economic sectors and entire regions that fail to get involved with these networks are most likely to be subjected to hard survival and even threatened with extinction.

The literature says that the application of information systems (IS) is crucial for the economic growth in general and, in particular for the SME sector, because of the greater role SMEs play in most economies in the world. At the same time, SMEs differ substantially from the large companies and that has a great impact on their practices for the implementation of IS. These differences relate to the lack of (or less complex) management of information systems; frequent concentration of tasks on information gathering to be performed by one or two employees; less resources to search for information; quantity and quality of the information at their disposal/available from their surroundings.

One of the best ways to achieve sustainable competitive advantages is development of organizational learning and knowledge management in SMEs. Organizational learning can be defined as a process or a practice of creating, acquiring, retaining, sharing and applying knowledge, wherever it is, in order to achieve better performance.

Studies conducted among SMEs for the purposes of the present analysis indicate that the application of ICT comprises an ever increasing part of the Bulgarian SMEs: 45% of the enterprises have their web pages (as compared to 37% at the beginning of 2013), 61% make use of electronic signatures, online ordering facility— 32%. The proportion of SMEs, applying management information systems, is also on the increase— from 6% to 11-15% (depending upon the type of the information system). Nevertheless, the proportion of the turnover generated by online ordering still remains low— on average for the sector it amounts to approximately 2%.

Staff training as a practice has yet to become a common core activity in most SMEs, although being relatively widely applied. 36% of the enterprises organize internal trainings (almost the same proportion as that of the previous year), and 13% — external specialized training in the field of the enterprise business activity (as compared to 17% from that of last year). More than half of the enterprises have short-term business plans (55%), but slightly less than one fourth (23%) have mid-term ones. 30% of the companies in the SME sector have developed marketing strategies.

### 3.6. Economic policies for enhancing SME competitiveness

The present study reports/brings out the poor innovation activity, patent activity and internationalization as being major weaknesses of the Bulgarian SMEs. As key strengths of the the Bulgarian SMEs appear to be their flexibility, their contribution to the somewhat relative employment retention in the country, the increasing entrepreneurs' interest in human resource training, usage of ICT and implementation of best practices (planning, strategies, marketing). As in the beginning of economic reforms in a period of transition, as well as today, in order to reinforce SME sector development, it is necessary to improve the regulatory and institutional environment in two directions: strengthening institutions and corporate responsibility.

Strengthening institutions does not imply strengthening bureaucracy, but rather it stands for the establishment of a stable and predictable regulatory framework and a “high culture” of administrative services. The companies are required to display more accurate accountability and promote the de-shadowing of the country's economy. The development of SMEs towards the adoption of more modern organizational models and practices is a slow process that requires learning and overcoming traditional (inherited) stereotypes. These changes presuppose the presence of a new class of entrepreneurs with a different frame of mind and skills, making it possible for them to work not in isolation but in international business networks. A study into entrepreneur values in Bulgaria ascertain that entrepreneurial success is mostly achievable through the following factors *training, development, challenges, co-operation, physical conditions* and *social security*. Successful entrepreneurs demonstrate better preparedness for business, more emphatic manifestation of innovative behavior and greater willingness to take business risks. This brings us to the conclusion how important it is to enhance the quality of entrepreneurship training and formation of a new business culture not only in the private, but also in the public sector as well.

In order to address the low resistance of the SME sector as regards the inheritance of family business owners, the state has to organize information campaigns about the issue of inheritance and the opportunities to solve it. Since SME do not seem to have sufficient resources to provide qualitative training of their potential successors (heirs), the state, therefore, is expected to support the sustainable development of the family business through its own provision of training to the potential successors to small and medium-sized enterprises – language training, specialized training for the managerial personnel (executive trainings, MBA programs, etc.), marketing training and others.

Strengthening the state policy for providing alternative sources for SME funding is vital for the strengthening of the sector itself in the context of the ongoing financial crisis. To this effect, it is very encouraging that the EC is pursuing a strategy of improving SMEs' access to finance through increased financial support from the EC budget and that of EIB as well, and also by the proposed new capital raising regulations of the funds. Under “European Venture Capital Fund” (EVCF) logo these funds will be able to raise capital, without being forced to comply with the complex requirements of the various member-states. The new regulations are expected to alleviate capital raising namely the capital for start-up companies which find it most difficult to gain access to funds.

Financial instruments targeting to improve access to finance for Bulgarian SMEs, organized to date, are five funds: Emerging Business Fund, Venture Fund, Growth Fund, Mezzanine Fund and Guarantee Fund. Via these funds and through a combination of public support and private investments, the “Jeremy Bulgaria“ EAD will

contribute to the provision of finance for micro, small, medium and large enterprises totaled 562 million euro until 2015 and in a longer term.

Bulgarian SMEs will be capable of enhancing their competitiveness and become integrated into the European and the most developed global markets, if they succeed in redirecting their business activities from the widely spread low-value-added industries towards certain market segments (niches) determined on the basis of specific competitive advantages and innovative high value-added products. Increased international competition requires adjusting or redirecting to products and services, which cannot be produced at a lower cost by the newly industrialised countries with indisputable advantages in labour-intensive industries.

Investing heavily in Research and Development Activity (R&D) will bring about the much needed environment necessary for the acceleration of SME innovation capacity. A promising start for this is the draft of a new Law on Innovation and Institutionalization of Bulgarian Fund for Innovation. The fund is expected to ensure complementarity between all the funding sources for SME innovation activities. Since innovative activities are designed around the development of company's own new products, their encouragement should be based on patent protection activities— financial, expert, etc.

Technological modernization of SME sector requires appropriate organizational changes, which would lead to a much greater flexibility. Such a modernization will involve greater use of partial and hourly employment, which was regulated for the first time in our country only in 2011. The progressive and gradual opening of SMEs to new markets is a driving factor for their sustainable development. At the same time, however, only a small proportion of SMEs are assumed to be internationalized and have the necessary potential to be seen as such. The state, therefore, could encourage the process by providing financial, expert and other assistance in:

- Finding new markets;
- Developing marketing strategies in accessing new markets;
- Training entrepreneurs in negotiating, international trade, etc.;
- Participation in business delegations and organization of professional and trade forums, etc.

If some strengths of the Bulgarian SMEs are associated with greater attention to human resource training, more intensive deployment of ICT and e-business applications and implementation of best management practices on a wider scale, it is obvious, then, that these processes should also be promoted. This means significant relief for depreciation of new technologies; support for internal training programmes; provision of highly qualified courses in marketing and marketing strategies. To achieve higher quality, however, Bulgarian entrepreneurs need to develop new strategies. One such strategy would be, for example, the much greater involvement in the value chain of more advanced (European) companies which already have positions in the relevant well-developed markets. The minimum requirement for its implementation is achieving compliance to quality standards. The second strategy involves formation of strategic alliances (or clusters) with some of the above-mentioned companies in order to gain access to their technological advantages. This is the reason why supporting the process of implementation of quality standards and formation of clusters in the sector is the very basis for the development of these new strategies.

Furthermore, it is necessary to strengthen quality and the scope of the entrepreneurial skills in the sector. The state, therefore, could provide financial, expert and other assistance in offering specialized training for the managerial personnel in the sector (executive trainings).

More intensive deployment of ICT is needed not only for optimization of the company's internal processes, but also for the successful involvement in e-business. In social terms, this means substantial increase of computer literate population and greater expansion of access to the Internet. These are guidelines, which should become an integral part of the government policies to support SME development. Improving the information environment requires measures to improve information sharing between the companies and the state-run institutions as well as the non-governmental organisations (joint trade organizations (professional bodies, Bulgarian Industrial Association (BIA), Bulgarian Chamber of Commerce and Industry (BCCI), etc.); keeping dedicated web sites for the respective



joint trade organizations up-to-date with the latest information on various issues of the respective sector; establishing advisory and information services.

#### 4. Conclusion

The paper examines the existing situation in the SME sector and its sustainability through the prism of five crucial factors for sustainable development and competitiveness. The observed high degree of interconnectedness between all the factors of competitiveness emphasizes the importance of a more closely integrated system measures for enhancing enterprise competitiveness. The facilitated access to finance is to be combined with measures for best practice implementation, stimulation of innovation, registering of intellectual property and increasing the level of internationalization

This means that it might be more effective and efficient to stimulate a small proportion of enterprises (those that have demonstrated potential for development in terms of their human capital, intellectual property, innovativeness and/or internationalization), which is to be done in a systematic way so as to bring about synergy effects of the respective economic policies. In other words, what is needed is a more comprehensive support for a small proportion of enterprises with a competitive potential.

To achieve this objective, however, the state should apply a systematic and unified methodology to help identify those particular SMEs (through examinations, measurements and analyses, creation of their own databases, etc.) that demonstrate potential in terms of some or all crucial factors for development and competitiveness. It is only in this way that the state could be able to provide timely, adequate and objective support for precisely those SMEs in particular that are capable of bringing about sustainable growth in the sector.

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