Abstract. Small and medium-sized enterprises (SMEs) are the proof of human efforts in independent presentation of the leverage aimed to faster and more efficient economic development. Developed countries have accepted and implemented the concept of enterprises by creating positive business environment and a supportive financial structure.

The significance of SMEs in total economic development of Croatia became noticeable during last years. SMEs are increasingly represented by growing number of economic subjects, in financial results and in number of employees within the total economy. Certainly, the biggest problem to SMEs is funding, i.e. difficulty in approaching the capital essential for their establishing and development. In this area a very special role belongs to the state and regional units of self-government which should provide a stable and safe business environment in order to contribute to both, creation of new and development of the existing economic subjects.

By strengthening the competitiveness of the SMEs on the long-term basis there is tendency to create favourable conditions for the growth of investment and increasing the number of entities with new products resulting in higher added value. Namely, since the mid of the year 2013 all the participants have found themselves in a new situation, while SMEs are looking for a support and institutions which can provide it (Ministries, Environmental Protection and Energy Efficiency Fund, Croatian Bank for Reconstruction and Development, Croatian Agency for SMEs and Investments and the like). When Croatia became a member of EU, surveillance of the financial supports has been transferred to the rigorous „big boss“, European Commission. Looking forward to the future, the portion of EU funds of support should be growing, while national supports should lessen.

This work researches institutional and regulatory restrictions to development of the SMEs in Croatia. The research is specifically targeted to the problem of financing of SMEs in Croatia and it shows the complete system of financing of this part of the national economy. At the same time the purpose and goal of this work is to provide systematization, describe and explore relevant determinants of financial supports to SMEs in Croatia, as well as to propose improvements of the existing and implementing of possible new sources of financing, that would significantly expand possibilities of financing of these enterprises in terms of quality.

Key words: SMEs, financing, supports, restrictions, investments

1. Introduction

Enterprises today renew, transform and encourage the development of economies around the world - that generates the emergence of new business ventures, the opening of many new,
mostly small and medium-sized businesses, creating new jobs and restoring the national economy, providing them with vitality, innovative products and services. A special role in the development of small business belongs to the state and local units of government that coordinate stimulating measures which should ensure a stable and secure environment for the emergence of new and development of existing business entities.

At the same time, enterprises are faced with specific problems in businesses that they cannot solve independently. Therefore, the development of SMEs should be encouraged at the national level, and it is necessary to provide the legislative, institutional and financial support. Certainly, the role of SMEs in the overall economic development of the Croatian Republic in recent years is increasing evidently and significantly in the number of businesses, financial performance, but also by the proportion of employees in the overall economy.

The Republic of Croatia has accepted the concept of entrepreneurship in the last period and provides financial support through various financial institutions, and both - state and local government units. Considering this, the Republic of Croatia has created a system of financing small and medium-sized enterprises, which mainly relies on banks and public financial institutions. By joining the European Union of the Republic of Croatia, operators of SMEs have been given approach to additional financial resources of EU Structural Funds.

2. Brief literature overview of financing SMEs in Croatia

SMEs are a driving force of development of the economy and employment. This part of the economy has an outstanding role, economic characteristics, organization and institutional environment. Nevertheless, a small number of authors researched the financing of SMEs in Croatia. One of the authors who systematically studied problems of SMEs was Vidučić (2005). She found that financing is a major constraint for the establishment and growth of SMEs in Croatia and recommend measures to facilitate access to credit and the use of other sources of funding. She also argued that financing SMEs through factoring has strong growth. Ćorić and Piplica (2012) explained the basic similarities and differences of SME in Croatia under conditions of crisis and compare it with developed European economies. Rimac Smiljanić and Pepur (2012) analyzed the impact of global financial crisis on the financing and performance of SME in Croatia. They suggested that the availability of bank financing is worsened after the crisis and that the companies have turned to alternative sources of funding. On the other side, Kundid and Ercegovac (2011) found that SMEs continuously encounter higher borrowing costs and they suggest that government actions should stimulate more inclusive bank finance of creditworthy SMEs. Kraft (2002) showed that banks in transition countries face with many problems in financing SMEs like lack of historical data to base risk-assessment on; macroeconomic instability, weak legal frameworks, etc. Anic and Pauš (1998) identify major barriers to the development of SMEs as insufficient support by the Government, low access to loans, lack of information on new technological developments, and insufficient investment in education. Cziráky, Tišma and Pisarovič (2005), investigated SME loan requests in Croatia and didn’t find positive correlation between the bank's size and its loan-size preference. Gavran and Gregov (2005) have explored the possibility of establishing a network of business angels for SMEs in Croatia.

Conducted studies indicate that characteristics of SMEs are smaller size and production of fixed assets, small number of employees, larger share of knowledge and innovation and institutional autonomy, as such economic operators can simply and painlessly enter and exit the reproductive patterns. Particularly significant is the ownership structure that has caused a certain organizational structure of the company. Certainly, the fundamental problem of SMEs is insufficient and inadequate funding resources. In this view, the sources of financing can be equity or assets of investors and loan capital or loans. Policy of small businesses in the
Republic of Croatia has not changed much over the past ten years and not much thought has been given to the improvement of instruments on which this policy is based. However, the problem of financing SMEs is still insufficiently explored. Therefore, this work tries to help in shedding light the unused potentials of SMEs in Croatia.

3. Definition of SMEs in Republic of Croatia and the European Union

The criteria for the classification of subjects of SMEs in the Republic of Croatia are defined in the Accounting Act and the Act on Promotion of Small Business. Entrepreneurs or companies as per definitions of the Accounting Act are classified as small, medium and large, depending on the amount of total assets, the amount of income, and the average number of employees during the financial year.

a) Small businesses - not exceeding two of the following conditions:
   - total assets of 32.5 million HRK,
   - income of 65 million HRK,
   - average number of employees during the financial year up to 50

b) Medium-sized businesses - exceeding at least two of three conditions for small businesses, but not exceeding two of the following conditions:
   - total assets of 130 million HRK,
   - income of 260 million HRK,
   - average number of employees during the financial year up to 250

c) Large enterprises - exceeding two conditions of the definition of medium-sized enterprises.

By the Law on Promotion of Small Business Sector, SMEs consist of the natural and legal entities independently and continuously engaged in activities aimed to making profit or market income. Natural and legal entities that are a part of the sector of small and medium-sized enterprises must meet three of the following conditions:

- to have an average annual employment of less than 250 employees,
- to be independent in business, which means that other natural or legal entities, individually or collectively, do not own more than 25% of the property or the decision-making rights in the small business entity,
- to achieve a total annual income equivalent of EUR 50,000,000.00 or have an adequate active balance total being profit tax-payers, or have long-term assets if they are liable to income tax in an equivalent of EUR 43,000,000.00.

Given the size of the subject, the Law on the Promotion of Small Business Development distinctly micro, small and medium-sized entities:

a) Micro entities are natural and legal entities employing on average per year less than 10 employees, annual turnover equivalent to 2,000,000.00 EUR, ie, have a value of fixed assets equivalent to 2,000,000.00 EUR.

b) Small entities are natural and legal entities:
   - with an average annual employment fewer than 50 workers,
   - generating total annual income equivalent up to EUR 10,000,000.00, or having an adequate active balance total being profit tax-payers, or have long-term assets if they are liable to income tax in an equivalent of EUR 10,000,000.00.

c) Medium entities are natural and legal entities:
   - with an average annual employment of more than 50 and less than 250 employees,
– with overall annual income equivalent of EUR 10,000,000.00 to EUR 50,000,000.00, or an adequate active balance total being profit tax-payers, or have long-term assets if they are liable to income tax in an equivalent of EUR 10,000,000.00 to EUR 43,000,000.00.

Accounting Law and the Law on the Promotion of Small Business Development have agreed the limit on the number of employees to organize SMEs in the Republic of Croatia. The categorization size businesses in Amendments to the Law on the Promotion of Small Business in May 2012 is in line with the criteria adopted by the European Union\(^1\) enabling better analysis and comparison of SMEs in the Republic of Croatia and the EU, as well as better use of mechanisms designed to support SMEs through EU programs (table no. 1).

**Table no. 1:** Classification criteria of small business entities

<table>
<thead>
<tr>
<th>Type of business entity</th>
<th>Number of employees</th>
<th>Annual turnover in million EUR</th>
<th>Capital (assets / current assets) in million EUR</th>
</tr>
</thead>
<tbody>
<tr>
<td>EU/ Croatia Micro</td>
<td>0-9</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>EU/ Croatia Macro</td>
<td>10-49</td>
<td>10</td>
<td>10</td>
</tr>
<tr>
<td>EU/ Croatia Middle</td>
<td>50-249</td>
<td>50</td>
<td>43</td>
</tr>
</tbody>
</table>

Source: Law on the Promotion of Small Business Development (Official Gazette no. 29/02, 63/07, 53/12)

### 3.1 Importance of SMEs in Croatian economy

As a result of adverse conditions in the environment, and general economic downturns in the year 2011, there was a decline in the number of businesses, but the structure of the economy remains the same, due to the size of the company. The largest decline was recorded in the category of medium-sized enterprises (6.3%), followed by small businesses (5.7%), while in the category of large companies decreased by 4.3% (table no. 2).

**Table no. 2:** Distribution of firms by size of companies in years 2001, 2010 and 2011

<table>
<thead>
<tr>
<th>Enterprises</th>
<th>2001</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Number of subjects</td>
<td>%</td>
<td>Number of subjects</td>
</tr>
<tr>
<td>SMEs</td>
<td>56.416</td>
<td>99</td>
<td>96.383</td>
</tr>
<tr>
<td>Small businesses</td>
<td>54.213</td>
<td>-</td>
<td>95.004</td>
</tr>
<tr>
<td>Medium-sized enterprises</td>
<td>2.203</td>
<td>-</td>
<td>1.379</td>
</tr>
<tr>
<td>Large companies</td>
<td>571</td>
<td>1</td>
<td>375</td>
</tr>
<tr>
<td>Total</td>
<td>56.987</td>
<td>100</td>
<td>96.758</td>
</tr>
</tbody>
</table>


In addition to the number of businesses, SMEs have a significant share of GDP in Croatia (table no. 3). In 2011 the share of SMEs in total GDP was 50.2%, representing a decrease of 1.8% compared to the year 2010 (due to the decrease in GDP in small enterprises). In the year 2011 the total revenue generated by Croatian export companies increased, with the largest growth in small business (growth of 20.5 compared to the year 2010). Unlike medium-sized businesses in which employment is slowly growing and large businesses in which employment has stagnated, employment in small enterprises in the year 2011 fell by 6.9%.

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\(^1\) In accordance with the recommendation of the European Commission 2003/361/EC of May 2003.
Table no. 3: Size of Enterprises and GDP, Employment and Exports in the years 2010 and 2011

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP (million HRK)</td>
<td>Small</td>
<td>199.298</td>
<td>191.232</td>
<td>109.530</td>
<td>111.896</td>
<td>289.357</td>
<td>300.152</td>
</tr>
<tr>
<td>GDP (share)</td>
<td>Medium</td>
<td>33.3%</td>
<td>31.7%</td>
<td>18.3%</td>
<td>18.5%</td>
<td>48.4%</td>
<td>49.8%</td>
</tr>
<tr>
<td>GDP (share)</td>
<td>Large</td>
<td>415.320</td>
<td>386.692</td>
<td>157.147</td>
<td>159.616</td>
<td>287.341</td>
<td>287.035</td>
</tr>
<tr>
<td>Employment</td>
<td>Small</td>
<td>48.3%</td>
<td>46.4%</td>
<td>18.3%</td>
<td>19.2%</td>
<td>33.4%</td>
<td>33.4%</td>
</tr>
<tr>
<td>Employment</td>
<td>Medium</td>
<td>17.117</td>
<td>20.636</td>
<td>18.867</td>
<td>19.697</td>
<td>53.085</td>
<td>55.747</td>
</tr>
<tr>
<td>Export (million HRK)</td>
<td>Large</td>
<td>20.1%</td>
<td>21.5%</td>
<td>21.0%</td>
<td>20.5%</td>
<td>58.9%</td>
<td>58%</td>
</tr>
</tbody>
</table>

Source: Croatian Chamber of Commerce, Centre for Entrepreneurship, Innovation and Development, 2012; FINA

Asymmetrical changes in employment, depending on the size of the company, are visible in comparison to the year 2001 (although the year 2011 compared to the year 2010 showed some changes, global conclusion applies). Thus in 2011 employment in the category of small businesses significantly increased, in large enterprises we noticed a significant fall in employment, while the level of employment in medium-sized companies is the most stable (table no. 4).

Table no. 4: Structure of Employees with Regard to the Size of the Companies in the years 2001, 2010, and 2011

<table>
<thead>
<tr>
<th>Type of company</th>
<th>2001</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Number of employees</td>
<td>%</td>
<td>Number of employees</td>
</tr>
<tr>
<td>Small</td>
<td>247.340</td>
<td>34.0</td>
<td>415.320</td>
</tr>
<tr>
<td>Medium</td>
<td>161.426</td>
<td>22.2</td>
<td>157.147</td>
</tr>
<tr>
<td>Large</td>
<td>318.467</td>
<td>43.8</td>
<td>287.341</td>
</tr>
<tr>
<td>Total</td>
<td>727.233</td>
<td>100.00</td>
<td>859.808</td>
</tr>
</tbody>
</table>


Table no.5: Structure of Employees in Small Businesses 2008 to 2011

<table>
<thead>
<tr>
<th>Year</th>
<th>The number of small businesses</th>
<th>Number of employees in small businesses</th>
<th>Average - number of employees in small businesses</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008</td>
<td>87.807</td>
<td>448.803</td>
<td>5.1</td>
</tr>
<tr>
<td>2010</td>
<td>95.004</td>
<td>415.320</td>
<td>4.4</td>
</tr>
<tr>
<td>2011</td>
<td>89.539</td>
<td>386.692</td>
<td>4.3</td>
</tr>
</tbody>
</table>


Employment in the sector of SMEs can be analyzed by comparing the average number of employees in SMEs (table no. 5 and no. 6). The average number of employees in small firms
ranges between 4 and 5, while in the medium-sized enterprises it has increased by 8.3% (from an average of 114 employees in 2010 to an averaged 123.5 employed in the 2011).

**Table no. 6: Structure of Employees in Enterprises 2008 to 2011**

<table>
<thead>
<tr>
<th>Year</th>
<th>The number of medium-sized enterprises</th>
<th>Number of employees in medium-sized enterprises</th>
<th>Average - number of employees in medium-sized enterprises</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008.</td>
<td>1.396</td>
<td>170.038</td>
<td>121.8</td>
</tr>
<tr>
<td>2010.</td>
<td>1.379</td>
<td>157.147</td>
<td>114.0</td>
</tr>
<tr>
<td>2011.</td>
<td>1.292</td>
<td>159.616</td>
<td>123.5</td>
</tr>
</tbody>
</table>


### 4. Access to finance

Primary sources of financial support for the development of SMEs in Croatia are: banking, credit unions, venture capital funds, informal forms of financing (business angels) and government incentive programs and subsidized credit lines. In the GEM research of the 2002 to 2011, the point is that access to funding in every year meets more obstacles than the stimulus (because of the score and components of entrepreneurial environment are under 3). At the same time, SMEs are significantly focused on traditional sources of financing (bank loans). The weaker focus on non-traditional sources of financing (venture capital and business angels) is associated with limitations of such sources in the Croatian market.

The perception of the availability of non-traditional sources of financing in the year 2010 was above the average for the countries involved in the GEM study (2.42 compared to GEM countries average: 2.39), whereas in 2011 perception deteriorates and falls below the average of the GEM countries (2.26 in Croatia compared to 2.44 - averaging GEM countries, table 7). The highest grade of availability of non-traditional sources of financing in 2011 was in Switzerland: 3.50.

**Table 7: Perceptions of the availability of non-traditional sources of financing in the years 2010 and 2011**

<table>
<thead>
<tr>
<th>Financial support</th>
<th>Grade 5 shows:</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>There is sufficient equity funds, debt financing, government grants, private investors, venture capital funds, availability of an initial public offering (IPO)</td>
<td>Average</td>
<td>Croatia</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2.39</td>
<td>2.42</td>
</tr>
</tbody>
</table>

Source: GEM Croatia, CEPOR - Centre for Policy Development of SMEs and Entrepreneurship, 2011 (2012.)

In addition to information on access to funding provided by the GEM research, complementary information on the credit market, investor protection and registration of ownership are available in a study of World Bank's Doing Business (table 8).

Doing Business Loan Market research analyzes the following criteria: strength of legal rights index, depth of credit information index coverage and public registry. According to these criteria, the World Bank study of the 2012 positioned Croatia at 48th place out of 183 countries that participated in the survey. On a scale of 1-10, protection of the interests of creditors and debtors through the legislative obstructions or inlets in Croatia is rated 6 (which is lower than the average score of the EU countries 7, but it is more than 4 to assess how to
protect the interests of creditors and debtors in the legislative framework is valued in Slovenia). Depth of credit information is rated 5, on a scale of 0-6, which is more than 4 to assess how much is averaging EU countries and to judge the depth of credit information in Slovenia. In the UK, which is ranked with first place in Markets loan area, interests of creditors and debtors are fully protected with quality legislative framework (rated 10), and with high transparency of credit information (rated 6).

Table 8: Overview of indicators of the quality of the regulatory environment of the Doing Business, which refers to the loan market for 2012

<table>
<thead>
<tr>
<th>Regulatory region</th>
<th>Indicator</th>
<th>Croatia</th>
<th>The best indicator</th>
<th>EU (average)</th>
<th>Slovenia</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market loans</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Strength of legal rights index (0-10)</td>
<td>6</td>
<td>10</td>
<td>7</td>
<td>4</td>
</tr>
<tr>
<td></td>
<td>Depth of credit information index (0-6)</td>
<td>5</td>
<td>6</td>
<td>4</td>
<td>4</td>
</tr>
<tr>
<td></td>
<td>Public registry coverage (% of adults)</td>
<td>0</td>
<td>0</td>
<td>16,8</td>
<td>3,3</td>
</tr>
<tr>
<td></td>
<td>Coverage of the private registry (% of adults)</td>
<td></td>
<td></td>
<td>50</td>
<td>100,0</td>
</tr>
<tr>
<td>Registration of ownership</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Number of procedures</td>
<td>5</td>
<td>2</td>
<td>5</td>
<td>5</td>
</tr>
<tr>
<td></td>
<td>Time (days)</td>
<td>104</td>
<td>2</td>
<td>32</td>
<td>110</td>
</tr>
<tr>
<td></td>
<td>Cost (% of property value)</td>
<td>5.0</td>
<td>0.1</td>
<td>4.8</td>
<td>2.0</td>
</tr>
<tr>
<td>Protecting investors</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Disclosure index (0-10)</td>
<td>1</td>
<td>10</td>
<td>6</td>
<td>3</td>
</tr>
</tbody>
</table>

Source: Doing Business 2012, Croatia - Country Profile, International Bank for Reconstruction and Development / The World Bank (The index ranges from 0-10, where the highest value indicates a high level of transparency and corporate governance including five aspects of transparency in corporate governance).

The complexity of the registration of property valued by three criteria: the number of required procedures for registering property, time required and costs of registration, in percentage relative to the value of the property. Compared with the EU, Croatia has the same number of procedures (5) and the cost of registration, but the time required for the registration of ownership is significantly longer (104 days in Croatia, compared to 32 days, which is average in EU).

4.1 Banks

Market bank loans and services provided for small and medium-sized enterprises are very developed. Almost all banks offer loans to small and medium-sized businesses in a wide range of products and services: loans for tourism services, youth, women, new technologies, for veterans, for export, investment, working capital, for beginners, etc. When reviewing and analyzing financial products designed for small and medium-sized enterprises, the following conditions of financing can be seen:

a) Long-term loans
   - Amount: EUR 250,000 (depending on the creditworthiness of the application)
   - Duration: up to 25 years
- Grace period: up to 36 months
- Interest: contract, up 6%
- Insurance: 1:1 - 1:1.5, promissory notes, debentures, deposits

b) Short-term loans
- Amount: EUR 2,500, depending on the creditworthiness of the client
- Duration: 12 months
- Interest: consensual
- Insurance: deposit, pledge commissioning placements, pledge of securities, promissory notes, debentures.

Based on the annual report of Croatian National Bank in 2011, the banking sector is placed 291,724.5 million, of which the placement by the company amounted to 122,936.1 million or 42.1% of total loans unlike since 2010, when the total equity of the banking sector amounted to 274,954.2 million, while the placement by the company amounted to 109,234.6 million. In the year 2011 there was an increase in placements of the banking sector to corporate sector by 2.4%. The largest part of the total loans granted in the 2011 were directed towards the population (43.9%), while according to government units placed 10.8% of the total loan placements. As for the year 2010, the majority of corporate loans were used to finance working capital and maintaining liquidity, however the ordered data do not include display of corporate loans depending on the size of companies.

4.2 Microfinance and credit unions

Microfinance, as opposed to the standard models of financing includes loans and provision of basic financial services with very flexible terms and conditions that allow clients to overcome the shortcomings of traditional guarantees (such as real estate and guarantees), as well as training and mentoring. Holders of microcredit services in the Republic of Croatia are the credit unions, which by the Credit Unions Act, are a new organizational form that replaced the savings and credit cooperatives. A series of restrictions resulted in a severe reduction in the number of preformed savings and loan associations in the credit unions. Applying the limit of territorial principle, i.e. allowing membership in credit unions only to residents of the same local (regional) self-government, number of credit unions’ members was halved, as well as the depository and credit funds needed for operations. This also terminated the number of transactions, while lending was enabled only to individuals and small business owners.

According to the Annual Report of the Croatian National Bank, in the year 2011 only 22 credit unions operated, having assets of 569.17 million HRK (as opposed to earlier times when 124 savings and credit cooperatives existed). In liquidation proceedings in the 2011 year, there were 10 credit unions and more than one went into bankruptcy. Also according to the Croatian association of credit unions, members of the association in the year 2011 placement of loans was 4868, totalling 156,253,936 HRK, an increase in placements of 88% compared to the year 2010, when 4,065 loans were placed worth a total of 82,939,717 HRK.

During the year 2010 the credit union qualified for the smaller number of loans compared to the year 2009 by 6.5%. The average amount of allocated loans by credit unions in the Republic of Croatia in 2009 was 21,400 HRK million, in 2010 was 20,403 HRK, while in the 2011 amounted to 32,098 HRK, indicating the orientation of the credit unions and their significant role in financing the development of micro enterprises.

The comparison of models of microfinance in the Republic of Croatia based on the best international practices developed in the last three decades indicating the underdevelopment of microfinance in the Republic of Croatia in relation to the developed financial markets in which operates a wide range of institutions, while in Croatia only a limited number of
institutions is present, mainly banks and credit unions with a limited range of products for SMEs. The target markets for microfinance services are micro enterprises, self-employed and the unemployed, whose limited access to finance is a high barrier to the realization of entrepreneurial activity. Research on the state of microfinance in the Republic of Croatia to the year 2010 spent CEPOR highlighted the following issues:

- lack of guarantees for loans (60%),
- inadequate offer of banking products and services (53%),
- demanding credit documentation (46%),
- too high interest rate (34%) and
- lack of information among users of financial products (26%).

At the initiative of the Croatian association of credit unions to change the Credit Union Act, the focus is on the provisions of the Act relating to the founding principles of credit unions, types of activities / services (payment), membership, deposit insurance and deposits, as well as the financial resources and credit union deposits in credit institutions.

4.3 Venture capital fund

During 2011 started work with funds for economic cooperation - Croatian version of venture capital funds that represent public - private partnership between the Government of the Republic of Croatian and private sectors, comprising the large institutional investors such as pension funds, banks, insurance companies and large Croatian companies. The aim of the project is on one hand to encourage the development of venture capital funds in the Republic of Croatia and on other hand stimulation of the Croatian economy by providing access to additional sources of long-term capital. With the establishment of funds for economic cooperation, the plan to recapitalize the country's investment by private investors with amounts between 75 and 300 million HRK per fund. Thus, in 2011 the Ministry of Business and Trade in funds has paid 170 million HRK for economic cooperation. Through this project Croatian companies will have two billion HRK in the next five years through the following funds:

- Alternative Private Equity FGS (600 million HRK),
- Honestas FGS (155 million HRK),
- Nexus FGS (380 milijuna HRK),
- Quaestus Private Equity Kapital II (525 million HRK) i
- Prosperus FGS (340 million HRK)

Given that investing in venture capital funds involves entering into the ownership structure, procedures related to the analysis and approval of funding is very complex and time consuming in comparison to other forms of financing (on average six to nine months). For these reasons, the first investment fund for economic cooperation took place in late 2011 when the Nexus FGS invested 40 million HRK into the project of building a data center (IT sector). This type of financing is not aimed to small businesses for several reasons:

- The founders of the fund will finance projects under 100.000 EUR due to reduced viability;
- Analysis and due diligence of each company for at least 25.000 EUR, irrespective of size;
- Business management policy focuses on up to 10 projects.

Thus, during the year 2011, the Croatian Private Equity and Venture Capital Association (CVCA), which gathers Croatian venture capital funds continued to promote this type of
financing. The common organization of the Croatian Chamber of Economy (CCE) held a series of seminars for entrepreneurs throughout Croatia titled "How to finance a business venture capital funds?"

4.4 Business angels

CRANE (New Angel Network) - Croatian Association of Business Angels (www.crane.hr) is a non-profit association that since September 2008 connects entrepreneurs who need capital for their business ventures (usually beginners) and business angels - successful entrepreneurs and corporate leaders who want to fertilize earned money by investing in projects in their initial stages. Since 2008 by the 2011 the CRANE recorded a small number of projects, which shows the low levels of development of this form of financing business ventures in the Republic of Croatia. According to the Association of CRANE in 2010 the business angels in the Republic of Croatia invested 1,502,600 HRK, while in 2011 they invested 2,634,100 HRK in five projects, which represents an increase of total invested assets.

As a major obstacle in expanding the activities of business angels in the Republic of Croatia, the CRANE association points out underdeveloped market of capital funds to invest in projects in the process of exiting the successful start-up projects in foreign markets, lack of quality projects on the market, and low levels of education entrepreneurs.

5. Research results and suggestions for improving the investment support to SMEs in Croatia

Creating a quality system of investment support of SMEs is one of the most important prerequisites for the development of these businesses. Increasing awareness of their importance for economic development in the last few years in the Republic of Croatia has led to significant advances in the offer of the sources of investment financing support small businesses. Slowly reducing the share of aid from the holders of economic policy partly directed at those issues - those that have not resulted in positive economic effects, but even more to distort the principles of competition. Certainly we can look positively to the future; the aid should increase the share of European funds, while the national support should decrease. Furthermore, we will offer suggestions of measures to improve the system of investment support to SMEs in the Republic of Croatia:

   a) New sources of funding by the Croatian Bank for Reconstruction and Development, Croatian Agency for Small Business, Fund for Development and Employment, as well as programs and institutional support of local governments have made significant changes in the financing of entrepreneurship. Certainly that range of source of funding should extend to those institutions that contribute significantly to development of entrepreneurship in developed countries, while in the Republic of Croatia it is still not sufficiently developed. It is necessary to provide a stimulating legal framework for the development of venture capital funds, leasing companies and business angels. In particular, it is important to distinguish the investments of venture capital funds from other forms of investment and introduce tax breaks for investing in high-risk investments.

   b) Linking SMEs - active state measures to link SMEs with large systems, as well as small and medium-sized exporters to foreign markets. In this way, the SMEs would be strategically positioned as an integral part of export and economic success of the state. By connecting SMEs, to encourage the development of new products and reduce the import of certain components, which could produce small enterprises, as a result of increased production achieved to further employment. In this way, entrepreneurs secure market to sell their products and ensure the safety of the collection.
c) Favourable sources of capital - It is necessary to take advantage of favourable capital resources that are offered by the different programs of the European Bank for Reconstruction and Development, European Investment Bank and the International Finance Corporation. State institutions and local government units are vital to help SMEs in accessing EU assistance programs for the development of small businesses.

d) The use of foreign capital - One of the options is joint ventures with foreign partners. In this part, creating a favourable investment climate by providing specific legal requirements, especially stimulating tax legislation and reducing administrative barriers, are of the special importance.

e) The reorganization of the government financial institutions - Croatian Bank for Reconstruction and Development and the Croatian Agency for Small Enterprises should increase efficiency and boost their respective roles in granting loans and helping the Croatian exporters. The said institutions can consolidate due to the correlation of their activities and goals of action in the development bank as a single institution. Likewise, government financial institutions should turn more to equity companies, which grant loans and sell them later to an interested private investor or an existing owner.

f) New measures from Croatian ministries - assigning certain tasks to external collaborators and the like. "Outsourcing" in the civil service would lead to a reduction of costs in the ministries and unloading state budget whilst ensuring additional services to SMEs in the service sector. It is also necessary to consider the possibility of restructuring programs for financing SMEs through ministries so as to assist entrepreneurs in the development of feasibility studies and business plans, and with the reduction of spending on interest subsidy. It is necessary to improve the legal framework for the development of small businesses by, for example, tax relief for small businesses. Also, government support to entrepreneurs should enable and encourage access to public institutions of science and technology development, and research centres to solve the existing problems jointly.

g) Enable financing through pension funds - the change of the legal framework (the current Law on Compulsory and Voluntary Pension Funds) should remove restrictions on pension fund investments in securities that are not quoted on the stock exchange or other organized markets, but also simultaneously develop a good system of risk diversification.

h) The effect of the ESOP fund – Great potential and importance for the development of small and medium-sized enterprises have programs and employee stock ownership plans. The experience of developed countries shows that the ESOP model affects the rapid growth of the company; earn greater profits and easier access to organized capital market. Applying this model to small and medium-sized enterprises should enable faster growth and development and at the same time slower growth of unemployment in the Republic of Croatia.

i) Programs of local governments - Lower unit of government should be more active and more balanced to include fostering the development of technology parks and business zones which would enable more favourable conditions (lower cost of renting or buying properties, reducing costs through the use of common infrastructure). Likewise, local or county authority must determine the strategic directions of development with regard to regional and climatic advantage of their area (branch activities, types of production or services, etc.), and to that end to invite and attract large strategic partners.
j) The possibilities of financing from European funds are determined by the rule of the seven-year period, which is called "financial perspectives", giving potential users sufficient space for planning. The most important task is making timely implementation procedures and accreditation of the Paying Agency. The system of accreditation is something different and simpler than is the case with IPARD. The accreditation for the implementation of the EAFRD is done only at the national level, while for the implementation of IPARD accreditation ascribed by the European Commission. Since 2014, five funds will be available for the Republic of Croatia (European Regional Development Fund, Cohesion Fund, European Social Fund, the European Agricultural Fund for Rural Development and the European Fund for Maritime Affairs and Fisheries).

6. Conclusion

SMEs in the Republic of Croatia become increasingly important economic entities, both because of their role in the economy and the social significance. Because of their number (almost 92,831 subjects), small businesses have huge potential in hiring new labor. SMEs contribute to the development and improvement of the economic structure and harmonious functioning of the overall economy.

Small enterprises are faced with many problems that could not be solves independently, with particular highlights on the problem of access to the capital necessary for the establishment and development. With low self-financing of small and medium-sized enterprises, financial problems are the result of underdeveloped financial markets and non stimulating business environment in Croatia. By comparing the results of Croatian SMEs achieved compared to those of the developed countries, we can see that the possibilities of their development in the Republic of Croatia are very large. Access of SMEs to funding is limited, considering the amount of money required for the different stages of the development of entrepreneurial undertaking. On the financial market dominated by bank loans, while lacking the financial resources to finance risky stage of entrepreneurial ventures (such as the initial phase and the phase of rapid growth). Venture capital funds and business angels are not yet recognized in the Republic of Croatia as an important source of financing for SMEs.

With Croatia entering in EU monitoring of aid transferred into the hands of a strict "big boss" - the European Commission (EC). Therefore, the aid must be in function of economic growth and more rational use of budgetary funds should be secured. Certainly the aid will be based on rules and concepts by which the project proposals for EU sources work. The activities that we had in previous years should be changed by approaching the design methodology and evaluated projects of the EU. The structure and organization of the institutions that monitor small business in the Republic of Croatia is relatively large, but not efficient enough. By implementing a series of measures, better coordination among institutions as well as the establishment of new institutions of support and funding, and improving the legislative regulation would create a system that is cheaper, more effective and harmonized with the possibilities of the Croatian economy. Certainly those changes in the functioning of financial institutions and incentives for small and medium enterprises in the Republic of Croatia should lead to increased employment and overall economic progress.
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