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## **CURRENT DEVELOPMENT OF BUSINESS ENVIRONMENT IN SLOVAKIA AND CZECH REPUBLIC\***

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**Abstract.** At the time of globalisation business environment of a country is significantly affect success of domestic businesses, respectively their products, on foreign markets. Also, conditions for business of a state have an influence on its attractiveness for potential foreign investments. The paper provides results of the analysis and subsequent comparison of business environments of Slovakia and Czech Republic and other selected countries over 2014 - 2015 on the basis of data provided by organisations dealing with business environment surveys such as the World Bank, World Economic Forum and Heritage Foundation. Critical insights, which could be instrumental for economic policy implications are formulated.

**Keywords:** business environment, doing business, global competitiveness report, index of economic freedom, Slovakia and Czech Republic

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**JEL Classifications:** E22, F21, F43

### **1. Introduction**

Doing business also involves so called business risk, which can be characterised as likelihood of taking a negative direction from reaching identified goals. In their business activities, entrepreneurs are also exposed to influences preventing them from achieving anticipated success. A set of influences affecting the existence and development of all business activities is generally denoted as business environment. The results of business activities are considerably dependent on the business environment a company operates in. Conditions under which companies

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operate, or develop their activities, have a significant impact on their performance, competitiveness and growth potential, as well as they determine the attractiveness of a particular state for foreign investors.

Within interstate comparison, the term business environment can also be defined on the basis of definitions used by international organisations. English term business environment is used by e.g. UNCTAD and World Bank's Department for Small and Medium Enterprises, while the term business climate is used by e.g. Danish and Dutch governments. The term investment climate can be found in the documents of the World Bank and UNIDO, and the term enabling environment is used by the OECD.

Canadian International Development Agency characterises business environment as the existence of a competitive domestic market linked with the global economy, managed by a well-defined legal and regulatory environment and equipped with a strong and growing human capital base and sufficiently developed infrastructure. The issue of determinants of business environment is up-to-date and dealt with in a number of publications by both Slovak and foreign authors. The significance of factors affecting business environment is dealt with by e.g. T. Guay (2014), K. Hallberg (2006), L. Hamilton and P. Webster (2015), A. Harrison (2014) and P. Wetherly, and D. Otter (2014), S. M. Wagner (2016). Hallberg explains that business rules are laid down by governments through adopted decisions. Positive principles such as transparency, responsibility, encouragement of competition, enforceability of rights and safeguarding of assets should be applied upon the formation, respectively improvement of conditions for business. (Hallberg, 2006).

Wetherly opines that mutual interaction occurs between business entities and business environment. Businesses are influenced by the environment they operate in as well as they have an influence on their environment. It is in the interest of businesses to participate in the formation of business environment in order to enforce their own measures with resulting benefits for them. (Wetherly; Otter, 2014). According to Harrison, a particular business environment can be characterised on the basis of identifying and detailing its key factors and perspectives. In some cases, individual perspectives are denoted as environments themselves with regard to the fact that they frame business environment as a whole (Harrison, 2014).

Business, respectively business environment are also dealt with in domestic publications by authors such as K. Belanová (2014), J. Táncošová (2007, 2013, 2014) and Š. Majtán (2012), who develops knowledge on the personal qualities of an entrepreneur, which are based on their professional, practical as well as business experience (Majtán, 2012); D. Martinovičová (2014), who partially focuses on the issues of business risk (Martinovičová, 2014); or V. Juričková (2006), who characterises three levels of business environment and their analyses (Juričková, 2006). New trends in business and startup communities' among young people are focusing on creativity, new ideas and innovations (Hudáková; Papula, 2016). Numerous publications are devoted to elaboration of various business ecosystem facets (e.g. Tunčikienė, Drejeris, 2015; Štīlis et al., 2016; Laužikas et al., 2015; Apsītis et al., 2016; Petrenko et al., 2017).

## **2. Methodology**

The purpose of this paper is to analyse and subsequently compare the levels of business environment of Slovakia and Czech Republic based on evaluations of internationally respected organisations.

Analysis and comparison of business environments are applied in order to find out identical and differing qualities of the monitored entities, comparing data obtained by organisations specialising in business environment surveys. Data related to business environments obtained by internationally respected organisations specialising in the analysis of conditions for business in the majority of countries are compared. Such organisations most frequently

publish the results of their analyses as evaluations in the form of numerical indices, rankings and summary reports.

Every state has a business environment whose characteristics and quality are analysed in published international yearbooks, indices and rankings, which can be recognised in broader relations, since the published values include a lower or higher degree of subjectivity. The degree of objectivity is dependent on the ratio between statistical data and data obtained from questionnaires, the choice of analysed parameters as well as on the perspective of effects of the observed indicators on the quality of business environments. Due to this fact, the order of particular countries in individual rankings differs slightly. Hence, there is no universal approach to indicators and measures evaluating the quality of business environment.

Business environment in Slovakia and Czech Republic are compared on the basis of evaluations of the World Bank, World Economic Forum and Heritage Foundation, which are regularly provided in the following publications:

- Doing Business (The World Bank) – is focused on difficulties in business, it evaluates a group of particular processes taking place in business, and is especially grounded on case studies, i.e. actual situations;
- Global Competitiveness Report (The World Economic Forum) – evaluates so called pillars of competitiveness in a country, respectively specific areas affecting business activities and national economic growth;
- Index of Economic Freedom (The Heritage Foundation) – covers economic freedom in countries, defined as a degree of restricting the freedom of market on which both companies and individuals operate.

### 3. Results and Discussion

For Doing Business, results of the research of the quality of business environments are published as an index, final report and ranking in which states are ordered based on the favourableness of conditions for business, respectively difficulty in carrying out business activities. The highest positions in the Doing Business ranking of business environment were occupied by: Singapore, New Zealand and Denmark.

The Slovak Republic ranked 29th and no change of position was recorded compared to the preceding period. However, it achieved an increase of the evaluation index by 0.88 to 75.62. The Czech Republic similarly recorded an increase of the evaluation index compared to the preceding period by 0.09 to 73.95. However, the country has dropped by three positions in the ranking, currently occupying the 36th place.

According to the countries' rankings, doing business in the Slovak Republic is less difficult than in the Czech Republic. Based on Table 1, however, differences in the rankings and evaluation indices of both states are only insignificant.

**Table 1.** Positions and evaluation indices of selected countries in Doing Business Ranking

Country	Position in 2015	Index in 2015	Position in 2016	Index in 2016	Change of index
Singapore	1	87.34	1	87.34	-
New Zealand	2	86.75	2	86.79	+ 0.04
Denmark	3	84.26	3	84.40	+ 0.14
Slovak Republic	29	74.74	29	75.62	+ 0.88
Czech Republic	33	73.86	36	73.95	+ 0.09

*Source:* Own proceeding

The resulting position of the countries in the Doing Business ranking is based on evaluation of ten areas affecting business activities. The evaluations of individual areas of Slovakia and Czech Republic are provided in Table 2. In spite of the positive ranking of the Slovak Republic, the Czech Republic has achieved better evaluation in some areas of business environment. However, both countries are poorly evaluated in the areas of protecting minority investors and enforceability of contracts.

**Table 2.** Positions and evaluations of Slovakia and Czech Republic in the areas determining the final Doing Business Ranking of countries

Evaluated areas	Position of the Slovak Republic in 2016	Index of the Slovak Republic in 2016	Position of the Czech Republic in 2016	Index of the Czech Republic in 2016
Setting up a business	68	88.54	93	85.23
Obtaining building permits	84	69.48	127	62.73
Granting connection to electricity networks	48	80.30	42	81.58
Registering property	5	90.99	37	76.40
Obtaining financing	42	65.00	28	70.00
Protection of minority investors	88	53.33	57	58.33
Tax obligations	73	76.79	122	67.09
Cross-border trade	1	100.00	1	100.00
Enforceability of contracts	63	61.69	72	60.36
Solving insolvency	33	70.04	22	77.73

*Source:* Own proceeding

#### *Comparisons of individual business environment areas*

Based on Table 3, setting up a business entity with limited liability in the Czech Republic is demanding from the viewpoint of both finances and time and requires a higher number of procedures. Overall, Slovakia is higher rated also due to the fact that higher capital needs to be paid up upon setting up a company in Slovakia.

**Table 3.** Evaluation of indicators related to the area of setting up a business

Indicators	Slovak Republic	Czech Republic
Number of procedures	6	8
Number of days	11.5	15
Costs of setting up a business (% of AAIC <sup>†</sup> )	1.5	6.7
Minimum called-up capital (% of AAIC)	18.5	0

*Source:* Own proceeding

Based on Table 4, obtaining permits and documents related to building in the Czech Republic is more costly and requires a higher number of procedures. Slovakia is higher rated in this area also with regard to the fact that

<sup>†</sup> AAIC - average annual income per capita

obtaining permits and documents related to building lasts longer under Slovak conditions. The case study concerns construction of a warehouse in the value of fifty times the average annual income per capita.

**Table 4.** Evaluation of indicators related to the area of obtaining permits in building

Indicators	Slovak Republic	Czech Republic
Number of procedures	10	21
Number of days (necessary for building the property)	286	247
Costs of carrying out procedures (% of the overall value of the building)	0.1	0.3
Quality index of regulation and implementation in building	11	12

*Source:* Own proceeding

Based on Table 5, connection of a particular object to electricity network lasts slightly longer and is more costly in the Slovak Republic. The Czech Republic is higher rated in the given area.

**Table 5.** Evaluation of indicators related to the area of connection to electricity network

Indicators	Slovak Republic	Czech Republic
Number of procedures	5	5
Number of days	121	110
Costs of connection (% of AAIC)	54.8	27.6
Index of reliability of electricity supplies and affordability of its prices	8	8

*Source:* Own proceeding

Based on Table 6, registering immovable property in an event of ownership changes lasts longer and is more costly in the Czech Republic. Slovakia is higher rated in the given area even in spite of the lower quality of regional management. The case study concerns registration of plot and building in the value of fifty times the average annual income per capita.

**Table 6.** Evaluation of indicators related to the area of registering property

Indicators	Slovak Republic	Czech Republic
Number of procedures	3	4
Number of days	16.5	31
Costs of registration (% of the property value)	0	4
Quality index of regional management	26.5	21.5

*Source:* Own proceeding

Based on Table 7, the quality of protection of the rights of both debtors and creditors upon obtaining financial means is evaluated equally for both countries. Overall, the Czech Republic is higher rated in this area, as it has better coverage of credit registers. Through credit registers, future creditors are able to obtain data on the financial history of potential debtors, which can have a positive or negative impact on credit granting.

**Table 7.** Evaluation of indicators related to the area of obtaining financing

Indicators	Slovak Republic	Czech Republic
Quality index of security rights	7	7
Quality index of information on credits	6	7
Coverage of public credit registers (% of adult persons)	3.2	6.7
Coverage of private credit registers (% of adult persons)	67.3	78.7

*Source:* Own proceeding

Based on Table 8, the area of protecting rights of investors - minority shareholders is slightly higher rated in the Czech Republic. Unless potential minority investors are ensured sufficient rights, their decision regarding investment might be negatively affected.

**Table 8.** Evaluation of indicators related to the area of protecting minority investors

Indicator	Slovak Republic	Czech Republic
Quality index of protection of minority investors	5.3	5.8

*Source:* Own proceeding

The area of paying taxes is higher rated in Slovakia in spite of slightly higher tax and contribution burden and a higher number of executed payments. Based on Table 9, administrative burdens, related to the calculation, recording and payment of taxes are considerably higher in the Czech Republic. The case study concerns a company with 60 employees and annual turnover amounting to 1,050 times the average annual income per capita.

**Table 9.** Evaluation of indicators related to the area of tax obligations

Indicators	Slovak Republic	Czech Republic
Number of payments (yearly)	10	8
Time necessary for the calculation, recording and payment of taxes (hours/year)	188	405
Tax and contribution burden (% of profit)	51.2	50.4

*Source:* Own proceeding

Based on Table 10, enforcing performance of contractual terms and conditions at court requires higher costs in the Czech Republic. Slovakia is higher rated in the given area also with regard to a significantly longer time of enforcing performance of contract. The case study concerns the value of recovered amount representing two times the average annual income per capita.

**Table 10.** Evaluation of indicators related to the area of enforcement of performance of contracts

Indicators	Slovak Republic	Czech Republic
Number of days necessary for judicial enforcement of performance of contract	705	611
Costs related to trials (% of requested amount)	30	33
Quality index of trials	12	10.5

*Source:* Own proceeding

Based on Table 11, recovery of a debt from an insolvent company is better rated in the Czech Republic with regard to a higher level of satisfying creditors and considerably shorter time and lower costs related to the compensation procedure. The case study concerns the market value of insolvent company representing 100 times the average annual income per capita. In case of sale of property, the value of such company amounts to 70 % of its market value. The company bears a secured loan burden, has 201 employees and 50 suppliers representing creditors.

**Table 11.** Evaluation of indicators related to the area of insolvency solution

Indicators	Slovak Republic	Czech Republic
The number of years necessary for recovering a debt	4	2.1
Costs related to recovering a debt (% of debtor's estate)	18	17
Rate of compensation of creditors (cents/dollar)	54.7	66.0
Quality index of insolvency-related legislation	13	13.5

*Source:* Own proceeding

In its annual publication Global Competitiveness Report, The World Economic Forum ranks countries based on the Global Competitiveness Index - GCI. The GCI reflects competitiveness of states, i.e. their ability to ensure prosperity for their citizens on the grounds of sustainable economic growth, which is also affected by the quality of business environment. Out of 140 countries, the highest rated in 2015 were Switzerland, Singapore and the USA.

The Slovak Republic ranked 67th and a year-over-year improvement of its position by eight places was recorded. The Czech Republic ranked 31st and its position improved by six places compared to the preceding period. Based on the ranking, a higher level of competitiveness was recorded in the Czech Republic than in Slovakia. The GCI and ranking of selected states are provided in Table 12.

**Table 12.** Positions and Global Competitiveness Indices of selected countries in the ranking published in Global Competitiveness Report

Country	GCI in 2014	Position in 2014	GCI in 2015	Position in 2015	Change of GCI
Switzerland	5.70	1	5.76	1	+ 0.06
Singapore	5.65	2	5.68	2	+ 0.03
USA	5.54	3	5.61	3	+ 0.07
Czech Republic	4.53	37	4.69	31	+ 0.16
Slovak Republic	4.15	75	4.22	67	+ 0.07

*Source:* Own proceeding

The Global Competitiveness Index of a country is dependent on the evaluation of twelve areas, so called pillars of competitiveness. The highest score a state can obtain within individual pillars is seven points.

Based on the data provided in Table 13, the Czech Republic is higher rated than Slovakia in each pillar of competitiveness. The lowest rated area in both countries is the pillar of innovation, research and development. Based on the results of the survey of the World Economic Forum, the low ranking is mainly due to a low volume of private investments in research and development and a low level of cooperation of educational institutions with the private sector in research and development.

**Table 13.** Evaluation of the pillars of competitiveness based on which the resulting GCI for Slovakia and Czech Republic in 2015 is stipulated

Pillars of competitiveness	Evaluation in the Slovak Republic	Evaluation in the Czech Republic	Difference in evaluations
Efficiency of institutions	3.43	4.09	- 0.66
Quality of infrastructure	4.28	4.69	- 0.41
Development of macroeconomic indicators	5.21	5.97	- 0.76
Health and basic education of population	6.01	6.31	- 0.30
Accessibility and quality of higher education	4.62	5.10	- 0.48
Efficiency of market for goods	4.43	4.63	- 0.20
Efficiency of labour market	3.90	4.44	- 0.54
Maturity of financial market	4.41	4.62	- 0.21
Technology maturity	4.64	5.43	- 0.79
Size of domestic and foreign markets	4.03	4.47	- 0.44
Maturity of business processes	4.07	4.49	- 0.42
Innovation, research and development	3.29	3.79	- 0.50

Source: Own proceeding

The Heritage Foundation evaluates annually so called economic freedom of countries, defined as a degree of restricting the freedom of market, having an impact on the overall national prosperity. The evaluated areas also have an impact on carrying out business activities. Out of 178 countries, the highest rated in 2016 were Hong Kong, Singapore and New Zealand.

The Slovak Republic ranked 56th and a year-over-year deterioration of its position by six places was recorded. The position of the Czech Republic has improved by three positions, currently occupying the 21st place. Based on the evaluation and position of states in the given ranking, provided in Table 14, the freedom of market is less restricted in the Czech Republic than in Slovakia.

**Table 14.** Positions and evaluations of selected states in the Economic Freedom Ranking

Country	Score in 2015	Position in 2015	Score in 2016	Position in 2016	Change of score
Hong Kong	89.6	1	88.6	1	- 1.0
Singapore	89.4	2	87.8	2	- 1.6
New Zealand	82.1	3	81.6	3	- 0.5
Czech Republic	72.5	24	73.2	21	+ 0.7
Slovak Republic	67.2	50	66.6	56	- 0.6

Source: Own proceeding

The resulting score of economic freedom of a country is based on evaluation of ten items provided in Table 15. The best possible score achievable for a particular item is 100 points.

**Table 15.** Evaluations of areas constituting the resulting score of economic freedom in Slovakia and Czech Republic

Indicators	Evaluation in the Slovak Republic	Evaluation in the Czech Republic	Difference in evaluations
Property rights	50.0	75.0	- 25.0
Level of corruption	50.0	51.0	- 1.0
State expenditure	49.5	47.3	+ 2.2
Tax burden	80.1	82.5	- 2.4
Restrictions in business	68.4	66.6	+ 1.8
Labour market	55.0	77.7	- 22.7
Monetary stability	79.5	84.1	- 4.6
International trade	88.0	88.0	-
Conditions for investment	75.0	80.0	- 5.0
Financial sector	70.0	80.0	- 10.0

Source: Own proceeding

The Czech Republic received better evaluation in the majority of the given items.

Areas having received low evaluations in both states include corruption and state expenditure, which exceeds state revenues, resulting in budget deficit. Budget imbalances represent a precondition of increased indebtedness of a country, which, in a certain stage, leads to adopting consolidation measures.

## Conclusions

Using evaluations of the World Bank, World Economic Forum and Heritage Foundation, we compared two countries which used to create a common state. The following conclusion was adopted based on analysis and subsequent comparison.

Based on the analysed data, the components of business environment with low evaluations in both Slovakia and Czech Republic include enforcement of performance of contracts, protection of minority shareholders, research and development, innovation and level of corruption. Based on mutual comparison, the Czech Republic is higher rated especially in the area of recovery of debt from an insolvent company. Slovakia has achieved a significantly higher ranking in paying taxes, to which extensive administrative burden is connected in the Czech Republic.

In order to improve conditions for business activities, accelerating the processes of judicial enforcement of performance of contracts and compensation of the creditors of insolvent companies is also recommended. In Slovakia, low evaluations were granted to both given processes within individual components of business environment analysed in the Doing Business project. Judicial enforcement of performance of contracts or recovery of debts from insolvent companies lasts too long. Claimants thus receive respective performance after a long time, which can have a negative impact on their solvency. In addition, the value of a claim can be considerably decreased by a possible impact of inflation over the long time.

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