

ESTONIA

1. Introduction


According to the World Bank, Estonia has a very business-friendly environment, supported by its leading e-government services. The country has the highest rate of early-stage entrepreneurial activity in the EU and an increasingly high uptake of digital technologies. However, Estonia does not have a specific policy on small and medium-sized enterprises (SMEs) and its R&D expenditure is significantly below the EU average. Additionally, support measures to mitigate the impact of the COVID-19 pandemic are failing to reach many SMEs.

SMEs in Estonia have been significantly impacted by the pandemic, the policy measures needed to combat it, and its overall impact on business. In 2020, SME value added dropped by 4.0%, while SME employment declined by 3.4%¹. The hardest hit sector was *accommodation and food services*, with SME value added and SME employment dropping by 37.7% and 17.7%, respectively. By contrast, the *professional, scientific and technical activities* sector generated 5.8% growth in SME value added and 4.1% growth in SME employment.

In 2021, SME value added is predicted to grow by 5.5%, while SME employment is predicted to increase slightly by 0.2%. Overall, SME value added in 2021 is predicted to be 1.3% higher than its 2019 level. SME employment, however, will remain 3.3% below its 2019 level.

SMEs dominate the Estonian business economy. In 2020, they generated a share of 78.3% of value added and 79.5% of employment. This was well above the respective EU averages of 53.0% and 65.2%. SMEs employed an average of 4.4 people in 2020, slightly above the EU average of 3.7 people. Average productivity, calculated as value added per person employed, was approximately EUR 32 200, almost one quarter below the EU average of EUR 40 000.

Figure 1: Number of enterprises, persons employed and value added in 2020



	Number of enterprises			Number of persons employed			Value added		
	Estonia		EU-27	Estonia		EU-27	Estonia		EU-27
	Number	Share	Share	Number	Share	Share	Billion €	Share	Share
Micro	70 373	91.5%	93.3%	139 160	32.9%	29.6%	4.0	28.8%	18.7%
Small	5 397	7.0%	5.7%	102 940	24.3%	19.7%	3.3	23.5%	17.0%
Medium-sized	998	1,3%	0.9%	94 708	22.4%	15.8%	3.6	25.9%	17.3%
SMEs	76 768	99.8%	99.8%	336 808	79.5%	65.2%	10.8	78.3%	53.0%
Large	158	0.2%	0.2%	86 631	20.5%	34.8%	3.0	21.7%	47.0%
Total	76 926	100.0%	100.0%	423 439	100.0%	100.0%	13.9	100.0%	100.0%

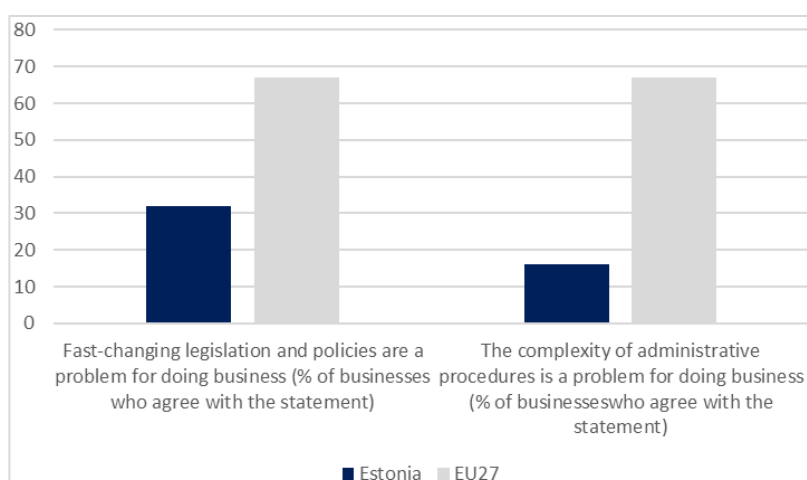
Source: These are estimates for 2020 produced by DIW Econ, based on 2008-2018 figures from the Structural Business Statistics Database as well as provisional data for 2019-2020 from the National Accounts Database and the Short-Term Business Statistics Database (Eurostat). The data cover the 'non-financial business economy', which includes industry, construction, trade, and services (NACE Rev. 2 sections B to J, L, M and N), but not enterprises in agriculture, forestry and fisheries and the largely non-market service sectors such as education and health. The following size-class definitions are applied: micro firms (0-9 persons employed), small firms (10-49 persons employed), medium-sized firms (50-249 persons employed), and large firms (250+ persons employed).

2. Key strengths

Estonia has an excellent business environment and is a leader in e-government services

Starting a business in Estonia takes only 3.5 days and requires very few procedures. Estonia is the EU country where businesses spend the least amount of time paying taxes – only 50 hours a year. Additionally, the cost of registering property is among the lowest in the EU². Estonian businesses are also the most satisfied in the EU when it comes to the administrative burden – only 16% consider it a problem³.

Figure 2: Fast changing legislation/the complexity of administrative procedures is a problem when doing business (% of businesses who agree with the statement)



Source: 'Flash Eurobarometer "Businesses" attitudes towards corruption in the EU', 2019⁴

Furthermore, the country leads on digital public services in the European Commission's Digital Economy and Society Index. This good performance is the result of having advanced digital public services for businesses and a transparent tax system⁵.

To achieve further progress, in 2019, the Ministry of Economic Affairs and Communications commissioned the development of a prototype of an IT-based application to measure administrative burden on businesses (*halduskoormus*). The prototype was launched in the spring of 2020 and will help implement the 'SME test'⁶, used to assess the impact of regulation on SMEs

Estonia has developed a highly dynamic ecosystem for start-ups, scale-ups and high-tech SMEs

In entrepreneurship, Estonia is among the best performing countries in the EU, with the highest rate of early-stage entrepreneurial activity⁷. Additionally, the positive perception of entrepreneurship education at university and vocational levels is among the highest in the EU⁸.

By end of 2020, Estonia registered 1 117 start-ups – a relatively high number for a population of 1.3 million. These start-ups are contributing significantly to the country's economy; they employ 6 072 people and, in 2020, paid EUR 97 million in employment taxes – an increase of 24% from EUR 78 million in 2019. The turnover of Estonian start-ups totalled EUR 782 million in the 2020, an increase of 43% from 2019. The number of start-ups that have been active for at least 5 years is 257 – accounting for 23% of the start-ups in the Estonian Startup Database⁹. According to State of European Tech¹⁰ 2020 report by Atomico, Estonia has 4.6 times as many start-ups per capita as the European average.

This favourable ecosystem has been supported by the dedicated public programme 'Startup Estonia' and several early-stage investment funds with public participation.

Substantial progress has been made in the uptake of digital technologies by SMEs

According to Statistics Estonia, in 2020, nearly 99% of all Estonian businesses had an internet connection and a website, 57% use paid cloud computing services, 16% use the internet of things and 9% analyse and work with big data. However, there are significant differences between SMEs and large businesses in the degree of uptake of digital technologies. In most indicators, medium-sized and especially large businesses outperform small businesses¹¹.

3. Key challenges

Estonia does not have a specific SME policy

Estonia typically adopts policies that are based on a 'one-size-fits-all' approach, with no exemptions or special treatment for small businesses.

Consequently, the 'Think Small First' principle is not systematically applied and the 'SME test' is not implemented, though a prototype was developed back in 2015. The contribution of self-employment is also underestimated at policy level¹².

Estonia's R&D expenditure is significantly below the EU average

Estonia is underperforming in R&D expenditure by the public and private sectors. According to the latest figures available, R&D investments represented just 1.61% of GDP in 2019, far behind the 2020 target of 3% set in the Enterprise Growth Strategy 2020. This is also substantially below the EU average of 2.2%¹³.

However, the state budget has set out an increase of the public R&D expenditure alone to 1% of GDP during 2021, which should push the total amount closer to 2%¹⁴.

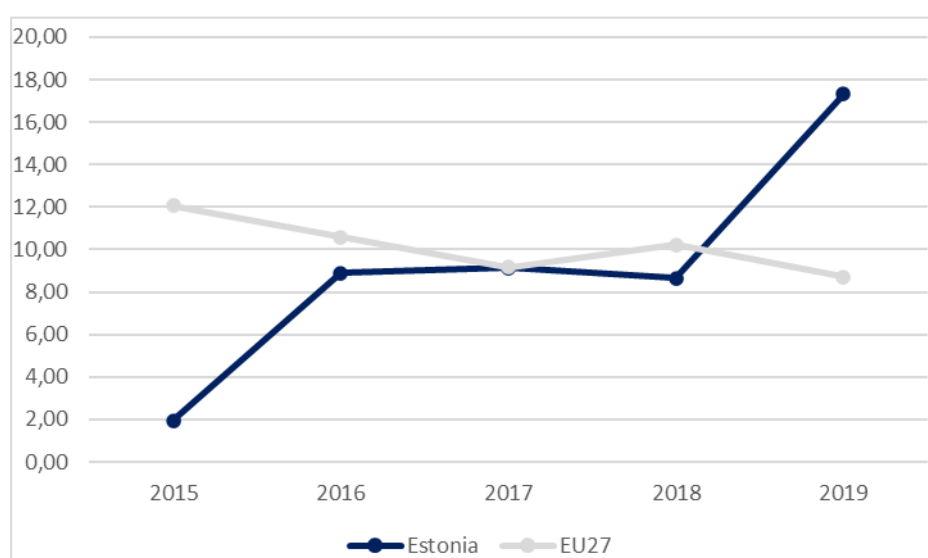
Support measures to mitigate the COVID-19 crisis were late and initially many SMEs could not access them

Through the public financial intermediaries KredEx and MES, different support measures were launched to help various sectors of the Estonian economy during 2020. A salary subsidy was offered, benefiting over 17 000 SMEs¹⁵.

While financial resources allocated to loans were very substantial, conditions were not favourable: the interest was high and many restrictions were applied that constrained the borrowing capacities of SMEs. Many micro and small businesses were excluded and most measures were not available to self-employed people and businesses without employees¹⁶. Due to these stringent conditions, as well as low demand, KredEx had only issued 122 direct loans¹⁷ and 156 guarantees¹⁸ by the end of October 2020. Additionally, the measures to support tourism and related sectors¹⁹ were considered substantially under-budgeted and were implemented late.

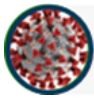
Furthermore, perceptions of the willingness of private banks to provide credit have been deteriorating, which puts additional pressure on SMEs' access to finance and makes Estonia one of the worst performing countries for this indicator²⁰.

Figure 3: Willingness of banks to provide a loan (% share of respondents who indicated a deterioration)



Source: Survey on the Access to Finance of Enterprises (SAFE), 2019²¹

4. Other key SME-related brief insights



IMPACT OF COVID-19 CRISIS ON SMES

The sectors hardest hit by the COVID-19 crisis were *accommodation and food services, tourism, foreign tourist-oriented hand-craft and souvenir shops*, as well as *entertainment*. The decrease in sales in these sectors since March 2020 has been between 60% and 95%²². Several subsidies, grants and loans were made available to support companies and SMEs. However, stakeholders have deemed these insufficient²³.



GREEN TRANSITION OF SMES

In the area of 'Environment', Estonia is one of the worst performing EU countries. Only 47% of Estonian SMEs have taken resource efficiency measures, the lowest share in the EU²⁴. Additionally, SME investment in clean equipment and technology is also among the lowest in the EU²⁵. Only a few measures to support the green transition of SMEs have been implemented so far, such as small grants for photo-voltage panels and a resource efficiency support scheme for industries. The Estonian government, however, is expected to provide more substantial resources to the green transition of businesses from 2021.



SOCIAL ASPECTS OF SUSTAINABILITY

As is the case for SMEs, a lack of specific attention towards the self-employed and businesses with no employees persists, as they lack access to social benefits and unemployment insurance. In terms of gender equality, Estonia has had mixed results²⁶. Despite it having a relatively high gender pay gap of 17%, Estonian women are faring relatively well in terms of entrepreneurship, as the country has the highest early-stage female entrepreneurial activity in the EU²⁷.



START-UP ENVIRONMENT

Estonia has one of the best start-up environments in the EU²⁸, and is implementing new measures to further improve it. Insolvency reform started in 2020, promising improvements in the area of 'second chance'. Similarly, amendments to the Bankruptcy Act will improve, simplify and speed up bankruptcy procedures²⁹.

