

**University of Economics, Prague**

**International Business – Central European Business Realities**



# **Small business and international entrepreneurship**

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**Declaration:**

I hereby declare that I am the sole author of the thesis entitled “Small business and international entrepreneurship“. I duly marked out all quotations. The used literature and sources are stated in the attached list of references.

In Prague on .....

Signature

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## Content

<b>List of Attachments .....</b>	<b>6</b>
<b>List of Appendixes .....</b>	<b>7</b>
<b>List of Abbreviations.....</b>	<b>8</b>
<b>Introduction .....</b>	<b>10</b>
<b>Chapter 1. The theoretical aspect of the study. The role of small business in a market economy.....</b>	<b>12</b>
1.1 Types and functions of small business. ....	12
1.2 Role of small business in global competition .....	15
1.3 SMEs support and funding programs .....	17
1.3.1 Support of SMEs in EU. Help to access finances .....	17
1.3.2 Direct investors support for SMEs .....	22
1.3.3 Microfinancing .....	25
<b>Chapter 2. Problems and prospects of small business development .....</b>	<b>28</b>
2.1 Porter's Five Forces analysis of SMEs environment .....	28
2.2 Challenges on the way to growth for the start-ups and existing small business.....	30
2.1.1 Challenges for SMEs on the way to growth in the Czech Republic.....	33
2.1.2 Challenges for SMEs on the way to growth in Germany. ....	34
2.1.3 Challenges for SMEs on the way to growth in Italy. ....	35
2.3 Opportunities for start-ups and existing SMEs. Supportive programs.....	37
2.3.1 Opportunities for SMEs in the Czech Republic.....	38
2.3.2 Opportunities for SMEs in Germany .....	39
2.3.3 Opportunities for SMEs in Italy.....	39
2.4 Ways of overcoming barriers. Supporting programs for SMEs in EU countries.....	40
2.4.1 Support of SMEs in the Czech Republic.....	43
2.4.2 Support of SMEs in Germany .....	44
2.4.3 Support of SMEs in Italy.....	45
<b>Chapter 3. Business challenges in present environment.....</b>	<b>49</b>
3.1 How small business goes international .....	49
3.1.1 New way to enter foreign market for SMEs.....	54
3.2 How to contact customer.....	55
3.3 The analysis of marketing limitation.....	56
<b>Chapter 4. Analyzes and example of business plan for SME.....</b>	<b>58</b>
4.1 FeelTravel Hotel – is an example of small hotel business in Prague. ....	58
4.2 Uniqueness and positioning .....	59
4.3 Customer analyses .....	60

4.4 Industry analysis .....	61
4.5 Competitive analysis .....	62
4.5.1 SWOT .....	62
4.5.2 Porter 5 Forces analysis .....	63
4.5.3 Rivalry in the Industry .....	64
4.6 Marketing plan .....	67
4.6.1 Marketing communication .....	68
4.7 Distribution channels.....	69
4.8 Revenue management .....	70
4.9 Operations plan and management team .....	70
4.10 Financial plan.....	71
4.10.1 Calculation of expenses .....	72
4.10.2 Profitability calculation.....	76
4.10.3 Break-even analyses and effectiveness calculation .....	78
4.11 Summary of business plan .....	80
<b>Conclusion.....</b>	<b>82</b>
<b>Bibliography .....</b>	<b>84</b>
<b>Appendixes .....</b>	<b>91</b>

## List of Attachments

Figure 1. Objectives and actions of the COSME Program.....	21
Figure 2. Comparison of interest rates for SMEs and large enterprises of one-year loans, 2015.....	23
Figure 3. SME investment types in Europe.....	24
Table 1. Programs for eliminating financing barriers.....	43
Table 2. Rating of the three-star hotels in Prague 31.03.2017.....	65
Table 3. Calculation of the main expenditures for the business establishment.....	72
Table 4. Assumption of the operating and non-operating expenses.....	74
Table 5. Summary of the operating expenses.....	76
Table 6. Monthly revenue per room.....	77
Table 7. Sales, depending on the season.....	77
Table 8. Break-even analyses of FeelTravel Hotel.....	78

## List of Appendixes

Appendix 1. Graph One, three and five-year survival rates of enterprises, business economy, 2014 (%).....	91
Appendix 2. Labor costs per hour in euro, whole economy (excluding agriculture and public administration).....	92
Appendix 3. Evaluation of investment grade of individual countries.....	93
Appendix 4. Drawing of the ground floor of FeelTravel Hotel.....	94
Appendix 5. Drawing of the first floor of FeelTravel Hotel.....	94
Appendix 6. Drawing of the second floor of FeelTravel Hotel.....	95
Appendix 7: Most non-residents arriving to the Czech Republic and staying overnight.....	95
Appendix 8: Hotels and similar accommodation establishments by size class, 2015 (%).....	96
Appendix 9: Net occupancy rates of bed places and bedrooms in hotels and similar accommodation establishments by size class, 2015.....	97
Appendix 10. Cost of the building Ke Koulce Prague 5 – Smichov (03.03.2017).....	98

## **List of Abbreviations**

ADR - average daily rate

ANAC - The Italian National Anti-Corruption Authority

CEE - Central and Eastern Europe,

CIP - Comprehensive Instructional Program

COSME - the Competitiveness of Enterprises and Small and Medium-sized Enterprises

DMI - Deutsches Mikrofinanz Institute

EaSI - The Employment and Social Innovation

EEN - Enterprise Europe Network

EMN - The European Microfinance Network

ERDF - European regional development fund

ESF - European social fund

EU - European Union

FDI - Foreign Direct Investment

GDP - Gross domestic product

GRW – Gemeinschaftsaufgabe the Joint Task Program for the Promotion of Industry and Trade

IP - Intellectual Property

IT – Information Technology

KMU - Kleine und Mittlere Unternehmen

MFIs - Private Microfinance Institutions

MIGA - Multilateral Investment Guarantee Agency

NGOs - Non-governmental Organization

NOI - Net operating income

NOPAT - Net operating profit after taxes



OECD - Organization for Economic Co-operation and Development

OTAs – Online Travel Agencies

RITMO - Italian own microfinance network

ROIC - Return on invested capital

SBA - The Small Business Act

SMEs - Small and medium-sized enterprises

ZIM - ZIM (Zentrales Innovationsprogramm Mittelstand) is a funding programme for SMEs

## **Introduction**

Nowadays due to globalization and liberalization of trade international entrepreneurship plays a crucial role in business environment.

Small business stimulates economic growth, improves economic development, contributes launching new products, creates jobs, and pushes for innovations. Due to these reasons, it is vital for the countries' governments' budgets. Along with that fact, there still exist barriers for SMEs on the way to success. Such challenges arise because of the legal requirements, industry saturation and competitiveness, unstable economic and political situation and cultural differences.

For large enterprises, it is quite easy to cross borders and do business internationally since they have more financial opportunities, brand awareness among customers and experience. Indeed foreign companies are more interested in cooperation. Entering new market will allow businesses to expand production, gain on economies of scale, create more stable and well-known brand etc. As a result, companies are using equity and non-equity modes of entering the market.

However, for small businesses and start-ups internationalization is a more complicated process hence most entrepreneurs lack the experience and financial resources. According to the latest data from Eurostat (a five-year period from 2009), an impressive number of new businesses are not able to overcome the challenges on their way – 56%. For that reason, many small businesses are going internationally after having stabilized on their local market. Thus there are also small companies that are operating globally, being on the early development stage.

Small and medium-sized enterprises (SMEs) are economically and socially important for both developed and developing countries. In conformity with World Bank researchers, SMEs are representing two-thirds of all employment and provide more than 50% of value added and total turnover in the European Union (EU). Additionally, SMEs and their cooperation have a great power and influence on the international trade and competitiveness of the particular country. Identically trade leads to the creation of new job opportunities which takes place due to the creation of new businesses.

This study explores the main barriers and opportunities for existing small business and start-ups; factors of their sustainable growth, reasons and possibilities to overcome difficulties that

arise due to internationalization as well as the supporting programs that currently exist for SMEs and play an important role in the countries' economies.

Since analyzing small business on the global level would be too extensive, let's focus on three countries (Italy, Germany and the Czech Republic) that were taken into a deeper consideration for business operation analysis. Moreover, the benefits of going international as well as the obstacles on that way and supportive programs for each country are highlighted. For better understanding, an example of business plan and analysis are provided. Based on the comparable analysis of business and economic environment in all three countries that are being explored, a final decision has been made to pick the Czech Republic.

The thesis consists of four main parts: starting with the theoretical background and SME's role definition in the market economy, followed by the description of potential threats, ways of overcoming barriers and opportunities. The third part is about the current international business trends followed by the business plan analysis of micro business.

The objective of the thesis is to provide guidelines for starting a business in global environment. The study combines quantitative and qualitative approaches to examine the factors of small business functioning in three chosen countries.

The thesis is useful for potential entrepreneurs, who are willing to start their own business in one of the EU countries, are eager to know more about the business support programs, advantages, and drawbacks that can be faced on their way.

## **Chapter 1. The theoretical aspect of the study. The role of small business in a market economy.**

### **1.1 Types and functions of small business.**

According to the European Commission SMEs are companies that have less than 250 employees and 50 million EUR of annual turnover<sup>1</sup>. (However, Organization for Economic Co-operation and Development (OECD) provides a different number of employees in definition of SMEs, which amounts up to 500 workers in the USA for instance<sup>2</sup>). Besides, around 99% of all enterprises in the EU countries are mostly SMEs, employing 60% of the workforce. And what is more, the vast majority of them are micro companies.<sup>3</sup>

The SMEs can be structured according to the number of employees:

- large business - more than 250 people (in some countries like Germany more than 500 employees),
- medium – sized - employs up to 250 workers,
- small enterprises is the business with 50 people employed,
- micro business has less than 10 employees,
- companies with one-person operations.

Small business has a tremendous influence on the local economy. This type of business is more flexible to the environmental changes, consequently, it can easily adjust accordingly. It does not require so many bureaucracy and department reorganization as the large corporations. Mostly, small business is customer oriented, meeting the demand of local needs. An extremely valuable factor in SMEs functioning is consumer's loyalty, due to which business can survive during the recession. In addition, small business is more likely to enter niche areas on the market, satisfying the needs or adapting innovations for the specific segments of the target group.

Obviously, SMEs are earning much lower revenues, although they have respectfully less to lose during the crises. Afterward, a business that survived crisis period, can grow into a big

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<sup>1</sup> Ec.europa.eu. (Commission Recommendation of 6 May 2003). Entrepreneurship indicators - Eurostat. [online] Available at: <http://ec.europa.eu/eurostat/web/structural-business-statistics/entrepreneurship/indicators>

<sup>2</sup> Directorate, O. (2017). OECD Glossary of Statistical Terms - Small and medium-sized enterprises (SMEs) Definition. [online] Stats.oecd.org. Available at: <https://stats.oecd.org/glossary/detail.asp?ID=3123>

<sup>3</sup> OECD Country and partner economy profiles of SME and entrepreneurship financing 2007-14.

corporation and become a powerful player on the market. In a worst case scenario, small business can go bankrupt and disappear from the market.

The most common types of small business are the following:

- Sole trader - is a business with one owner, who is responsible for the whole firm and decision-making process as well as being solely liable for any debts and responsible for selling personal assets in case of need. It is a time-consuming work as everything is on the owners' shoulders including production, financing and marketing aspects. Therefore, it is relatively cheap and in case of success, an owner retains all profit.
- The cooperation on the agreed basis - is a partnership of up to twenty people, who are running the business together. In this type of small business, everyone can have different rights and shares of business. In fact, silent partners can be present, they have limited rights and usually do not participate in decision-making process. Availability of agreement is crucial to designate the obligations and rights of each member. Here the diversification of roles takes place, as more people are responsible for decisions-making process. Such structure helps to avoid conflicts concerning the decisions of running a business.
- Company – is more complex and expensive type of small business. It is created due to the compound of capitals of some organizations. Owners are the shareholders, who have limited liability. Public companies have up to fifty shareholders whereas private ones should have minimum five shareholders. This type is considered to be more expensive than the previous one due to the government regulations. Sometimes the decisions can be made and the whole operation process can function without the owner. Moreover, company should be registered and must meet numerous legal requirements.
- Manufacturing business usually requires quite large investments in the initial stage as well as deep and broad technical knowledge. Consequently, a thought-out strategic plan and financial strategy should be in place. Therefore, this type of small business creates a lot of jobs.
- Small business is saturated with the retailers that are the fifth identified type. Retailers are also focused a lot on the consumers and are paying a great attention to the holiday

season. During that important period, the easiest way to influence purchases is pushing customers to do unplanned shopping.<sup>4</sup>

Mainly, each business acts in a way so that it performs the basic functions. Operational function aims to meet the customers demand with products or services supply. The function performs via sales organization and control, marketing campaigns and logistics. Besides, the cooperation of all of the departments is crucial to reach the target; otherwise, operational function cannot be realized.<sup>5</sup>

The following function is finance. This function concerns the allocation of the financial resources for the departments of the organization, according to their needs and depending on their importance. Such function lies on the managers' shoulders and depends a lot on their decisions, leading the company to the profitable or bankrupt result. It is highly important to recognize, which department inquiries financial resources most of all and which one acquits the investment.<sup>6</sup>

The third function is the marketing that is becoming more and more important over the last years due to the increasing competition on the market and availability of similar products and services. Promotion is mandatory for start-ups and small business as the emerging and already existing products even with the high quality are usually eclipsed by the well-known brands. For this reason, companies should deliver their message to the potential consumer in a clear way, show benefits from the consumption of the product, present the difference from the competitors. On each stage of the lifecycle, the marketing campaign is different.<sup>7</sup>

All business functions can be divided into the internal and external functions. Internal functions concerns producing, selling and supporting departments; they are based on the entrepreneurial orientation. On the contrary, external functions are dealing with the same departments but are mostly focused on the explorations out of the company such as management consultants, market

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<sup>4</sup> National Retail Federation. (2014, October 29). Small Business. Retrieved from <https://nrf.com/who-we-are/retail-communities/small-business>

<sup>5</sup> Hezam,A. (2015, April 1).What are the Three Basic Functions that run the business. Retrieved from <https://www.linkedin.com/pulse/what-three-basic-functions-run-business-abdul-hezam>

<sup>6</sup> Heizer, J & Render, B. (2011). *Operations Management. 10th Edition. Global Edition for Laureate Education*. Pearson Learning Solutions. VitalBook file

<sup>7</sup> Youngfinanceguy [6 February 2015].. The 3 Basic Business Functions [Online] Available from: <http://youngfinanceguy-benweb.blogspot.com/2010/11/business-basics-3-fundamental-functions.html>.

researchers, and analyses of customers' feedbacks. External function shows the level of dependency of the small business from the changes in the environment.

In the small business itself, one of the most important functions is creating employment and stimulating economic growth. Especially in the United States, this function is clearly seen, as small business has generated and created employment of more than half of the workforce, mostly by the private sector.<sup>8</sup> In EU, the situation is similar as SMEs are creating the majority of jobs as well.<sup>9</sup>

To be more precise, these are not the small companies that create employment but rather the young ones. However, it should also be mentioned that many of such companies are out of the market because of business failure that leads to the sharp decrease of all the jobs that have been created. Subsequently, the quality level of such jobs is unstable and unpredictable. On the contrary, start-ups - survivals are the powerful job providers.

## **1.2 Role of small business in global competition**

In current economic environment, SMEs bear a certain economic and social responsibility with significant innovative, productive and export potential.

Such businesses are vital to provide:

- The economic growth, sustainability and industry development.
- Generate new jobs due to the establishment of new companies. The cost of employment creation is lower than for big companies. The quality and efficiency of such positions are discussed below.
- Export contribution, which is possible due to new businesses creation. The more people are employed - the more goods are produced and exported.
- Saturation of the market with products and services that complement the system of public consumption. A variety of products and services created by SMEs meet needs of local citizens.

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<sup>8</sup> The United States (Jan. 2011) Small Business Administration. "Frequently Asked Questions." Frequently Asked Question about Small Business. SBA Office of Advocacy.

<sup>9</sup> Airaksinen A., Luomaranta H., Alajääskö P., Roodhuijzen A. (2015, September) Statistics on small and medium-sized enterprises . Eurostat [http://ec.europa.eu/eurostat/statistics-explained/index.php/Statistics\\_on\\_small\\_and\\_medium-sized\\_enterprises](http://ec.europa.eu/eurostat/statistics-explained/index.php/Statistics_on_small_and_medium-sized_enterprises)

- Innovations, which raise competitiveness of the country and industry. Innovations do not always require new ideas. Likewise, already existing ideas can be upgraded with a modern approach or unique service.

Small business is attractive to many young entrepreneurs and start-uppers. First of all, it is a low-cost investment. It is possible due to the ability to make profit from the lower number of sales comparing to the large companies. From 2000, it started to be popular doing business via the Internet and today there are still many niches to start-ups.

The most attractive and profitable industries to create a start-up are the ones described below. The first and the most popular is IT sector: virtual reality, games, software development and social networks are all on trend and on the top of people's mind. Next is a biometric scanning that becomes increasingly popular. While recognition systems are coming into use, the need for special security programs arises. Consulting business in financial sector for individuals and legal entities is an additional opportunity for start-uppers. Moreover, due to the latest tendency to live a healthy life, the corporate wellness is highly attractive and popular industry for start and develop the business.<sup>10</sup>

On the EU scope the most popular SMEs sectors are wholesale and retail, business services, food and accommodation, manufacturing services and construction. However, the most famous do not mean the most effective ones. In a profitability ranking mining industry is in the first place; followed by business services, information, and communication; after which comes transportation and all the popular sectors named before. Such inconsistency arises because of the level of difficulty to create and do business in certain industry. Hence the most profitable industries are complicated and require more enclosed efforts.

For the local economy, small business is crucial. Due to the high level of diversification, a community with many small businesses is less sensitive to the stresses and crises at a whole. Moreover, SMEs prevent economies from the monopoly creation.

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<sup>10</sup> The Best Industries for Starting a Business in 2016. [online] Available at: <https://www.inc.com/graham-winfrey/best-industries-2016-the-best-industries-for-starting-a-business.html>



### **1.3 SMEs support and funding programs**

Most of the small businesses and especially start-ups need financial resources. The first need of capital arises during the business establishment. Due to the technological development company should have an ability to renew the equipment and expand the production lines. Also, bringing additional workforce requires training which, in its turn, requires additional financial resources. After successful functioning and growth, business enters new markets. Consequently, the need of financial resources for foreign environment research and marketing communication arises. All the mentioned processes need the capital inflow.

Finances were mentioned in barriers for SMEs, not in vain. Notwithstanding the fact that funding provides business opportunities, some types of financing can slow down businesses growth. Such problem appears because of the high cost of the loan in a bank, guarantees or high investors' requirements.

Small business founders usually experience the lack of financial resources. Some of the loan applications from small businesses can be rejected. Due to the increased value of SMEs in present economic environment, there exist financial support programs from both governments and private investors (lenders).

#### **1.3.1 Support of SMEs in EU. Help to access finances**

In case of EU, the main support is provided by the European Commission.

The European Commission establishes projects that help entrepreneurs to merge into the business environment and to find answers to multiple questions arose. One of such campaigns is the European SME Week, which aims to inspire people to participate in business and to show the available support services for promotion provided by the EU.

In addition to that, Your Europe Business Portal aims to increase international cooperation in a single market scope. There is a possibility to get information about the business outside the EU, using database and support services from the SME Internationalization Portal. Also, Intellectual property rights helpdesks offer free advice concerning the IP and also training sessions. All the

helpful information about access to finances and markets can be found on the European Small Business Portal.<sup>11</sup>

Indeed, to provide support for entrepreneurs and SMEs in various areas needed, different networks were created. For instance, The Enterprise Europe Network (EEN) helps to manage problems with the legal issues and distinguishes the potential business partners and encourage innovations. It includes support in the internationalization process, strengthens competitive features, provides consultations, and encourages participation in Horizon 2020.

Moreover, there are some special programs invented for SMEs support. One of them is the European Enterprise Promotion Awards. The Program motivates potential business people to participate in the competition. There exist six award categories and the winners are rewarded each year at a special ceremony. To take part in such competition, companies should be original, prove their influence on the local economy and ease to transfer the project to other European regions.<sup>12</sup> The main objectives are internationalization, elimination of regulations, encouraging of entrepreneurship and access to finance, which is not provided as a direct funding but as an aid through the financial instruments. However, if the project complies with the specific EU program or policy it can be fully financed.<sup>13</sup>

In line with the described help, the Europe 2020 strategy introduces the program that is targeted on the economic growth, the increase of employment and poverty elimination. Together with the European Commission, as the main supporting force of small businesses, the following funds were created under the Europe 2020 strategy: Social Fund (ESF), the Regional Development Fund (ERDF) and Cohesion Fund.

ESF – a 60-year fund, which is focused on the employment growth, poverty prevention and education opportunities enhancement. Basically, these are investments in the human workforce in order to fight unemployment. ESF includes requalification programs and assists in job seeking via support of local projects that are related to the employment. The fund works in a partnership between the national authorities and European Commission to gain the more

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<sup>11</sup> Growth. (2017). Support to SMEs and entrepreneurs - Growth - European Commission. [online] Available at: [https://ec.europa.eu/growth/smes/support/networks\\_en](https://ec.europa.eu/growth/smes/support/networks_en)

<sup>12</sup> Growth. (2017). European Enterprise Promotion Awards - Growth - European Commission. [online] Available at: [https://ec.europa.eu/growth/smes/support/enterprise-promotion-awards\\_en](https://ec.europa.eu/growth/smes/support/enterprise-promotion-awards_en)

<sup>13</sup> Growth. (2017). Access to finance for SMEs - Growth - European Commission. [online] Available at: [https://ec.europa.eu/growth/access-to-finance\\_en](https://ec.europa.eu/growth/access-to-finance_en)

efficient result. The aim is to create a better environment in the employment sector among the whole EU. Funds are allocated according to the level of regional GDP per head.

ERDF pay particular attention to such areas as innovation and research, low-carbon economy and namely support for SMEs. Resources are allocated depending on the development of the regions as well as specific territorial characteristics<sup>14</sup>.

According to the European Commission, Cohesion Fund is focused on EU countries, which have the "... level of Gross National income per inhabitant less than 90% of the EU average."

<sup>15</sup> The Fund allocates money according to the priority of the projects, which reflect the European Union interests. Moreover, it supports environmental protection projects. The Czech Republic is one of the 15 priority countries for the fund.

The following program names Employment and Social Innovation, which was created to support social innovations, providing annual financial support. The total budget of 920 million EUR aims to support:

- Learning, training and practice exchanges for employees ( more than 60% of budget spending);
- Consultations concerning the working environment in various EU countries (18% of the total budget spending);
- Microfinancing, in order to ease access to loans for social enterprises (more than 20% of budget expenditures spending)<sup>16</sup>

Starting 2007, the Competitiveness and Innovation framework program (CIP) has been running for six consecutive years. The aim was to help the expansion and development of around 350 000 SMEs start-up. A number of financial resources that were directed to loans and capital investments were more than 1.1 billion EUR.<sup>17</sup> Moreover, 2 billion EUR were targeted to help

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<sup>14</sup> Ec.europa.eu. (2017). European Regional Development Fund. [online] Available at: [http://ec.europa.eu/regional\\_policy/en/funding/erdf/](http://ec.europa.eu/regional_policy/en/funding/erdf/)

<sup>15</sup> Ec.europa.eu. (2017). Cohesion Fund. [online] Available at: [http://ec.europa.eu/regional\\_policy/en/funding/cohesion-fund/](http://ec.europa.eu/regional_policy/en/funding/cohesion-fund/)

<sup>16</sup> European-microfinance.org. (2017). EMN. [online] Available at: <http://www.european-microfinance.org/index.php?rub=microfinance-in-europe&pg=microfinance-and-eu>

<sup>17</sup> Welcomeurope.com. (2017). List of EU funding and European Funds and Grants for Small and Medium-sized Enterprises (SMEs). [online] Available at: <http://www.welcomeurope.com/european-subsidies-beneficiary-SMEs.html#afficheTexte>.

SMEs to bring innovative ideas together with the environmental safety. From 2014 CIP was transferred to Horizon and COSME.

Horizon 2020 is representing the large-scale program, that offers 80 billion EUR worth grants, 2,8 billion EUR of which are only dedicated to SMEs. It is targeted at SMEs focused on innovations and researchers, aiming to increase EU competitiveness, create more jobs and promote economic prosperity. Basically, the main idea is to eliminate borders and help to bring innovative ideas into reality.

In line with Horizon, COSME program (Competitiveness of Enterprises and Small and Medium-Sized Enterprises) is created to support SMEs and facilitate the process of getting loans and other financial support.<sup>18</sup>

It is important to note that enterprises cannot get the direct loans and grants from the European Commission. The organization helps businesses to find the locally available intermediaries that can manage the loan. The European authorities provide the financial support of small business, which is carried out with the help of public and social programs implemented under the auspices of the EU. Financing can be in form of trade credit, leasing, bank loan or credit line (the most popular type).

COSME program issues guarantees for such intermediaries to increase the number of loans, issued for SMEs. On the scale of the EU, 250 000 of SMEs more will be able to get financial support due to this program. Also, the program supports SMEs on their growth stage, provides equity financing. Moreover, COSME provides support for market access: informs businesses about the opportunities of entering the third countries' markets as well as EU single market; supports Internet provision of information for businesses.

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<sup>18</sup> Growth. (2017). Access to finance for SMEs - Growth - European Commission. [online] Available at: [https://ec.europa.eu/growth/access-to-finance\\_en](https://ec.europa.eu/growth/access-to-finance_en)

Figure 1. Objectives and actions of the COSME Program<sup>19</sup>

Objectives	Actions	Total budget 2014-2020
<b>Improving framework conditions for the competitiveness and sustainability of EU enterprises</b>	Activities to improve European competitiveness: <i>Studies, impact assessments, evaluations, conferences</i>	<b>EUR 101.7 million</b>
	Activities to develop SME policy and promote SMEs competitiveness: <i>Meetings, reports, databases</i>	<b>EUR 64.5 million</b>
	Tourism: <i>Projects, prizes, surveys, events</i>	<b>EUR 131.4 million</b>
	New business concepts for consumer goods: <i>Market replication-type projects</i>	<b>EUR 86.8 million</b>
<b>Promoting entrepreneurship</b>	Activities promoting entrepreneurship: <i>Erasmus for Entrepreneurs</i>	<b>EUR 86.8 million</b>
<b>Improving access to finance</b>	Financial instruments	<b>EUR 1.4 billion</b>
<b>Improving access to markets</b>	Enterprise Europe Network (EEN): <i>Support services, partnership proposals<sup>9</sup></i>	<b>EUR 424 million</b>
	Support to SMEs abroad: <i>Studies, helpdesks, platforms, events, promotion activities</i>	<b>EUR 99.2 million</b>
	Support to international industrial cooperation: <i>workshops, meetings</i>	<b>EUR 12.4 million</b>
<b>Total</b>		<b>EUR 2.4 billion</b>

Source: Annex 3 of COSME proposal COM (2011) 834 final on the "Estimated financial impact of the proposal/initiative"

Late Payment Directives is the other type of support that exist in order to organize invoice payments in time. They had to be implemented in each country's law by 2013. Such measure aims to decrease bankruptcy of small businesses because of the financial difficulties. For this reason, deadlines for invoice payments were created: for instance, 30 days - for public authorities and 60 days - for enterprises. Indeed there are some envisaged exemptions for special cases. In addition to that, the penalty for late payment in a form of a fee amounts for minimum 40 EUR.<sup>20</sup>

The great assistance while starting business and keep it functioning on the respectable level is provided by the Small Business Act for Europe (SBA, which should not be confused with the

<sup>19</sup> Differences and similarities between CIP and COSME (April 2012) Briefing note [online] Available at: <http://www.europarl.europa.eu/document/activities/cont/201204/20120426ATT44002/20120426ATT44002EN.pdf>

<sup>20</sup> Growth. (2017). Late Payment Directive - Growth - European Commission. [online] Available at: [https://ec.europa.eu/growth/smes/support/late-payment\\_en](https://ec.europa.eu/growth/smes/support/late-payment_en)

similar organization in the USA - Small Business Administration). Before entering business surrounding, the potential entrepreneur should clearly understand his objectives; targets to achieve; market to enter; distinctive features of the product; advantages among competitors, their strengths, and weaknesses; an approximate sum of needed financial resources; strategy; legal structure and specifics of the industry. SBA can navigate business beginners and give advices in order to take right decisions and make more concrete targets. In addition to that, SBA aims to decrease barriers in the way of creation and development of SMEs, including regulatory policies. All the facts mentioned ensure the SMEs-friendly legislation. The "Think Small First" principle considers the interests of SMEs and eases the environment of the businesses functioning for the enterprises.

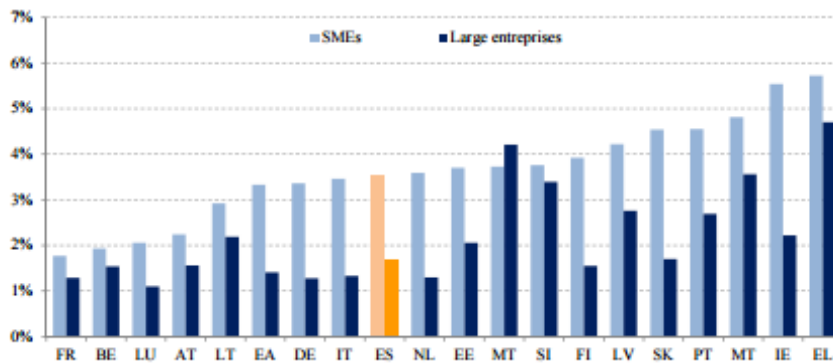
SBA promotes entrepreneurship for economic prosperity. Such support starts from the education background, including some exchange programs, following by ease of administrative procedures and financing issues. These actions motivate more individuals to start their own business when they feel favorable environmental conditions.

### **1.3.2 Direct investors support for SMEs**

The financial support can be provided in a form of loan, guarantee or equity investment from banks, leasing organizations, business angels, venture capital or crowdfunding.

Bank loans are the most famous source of finance for SMEs. The two crucial barriers for small business lenders are the high-interest rate and refusal of the loan. As it is shown in the figure below, the interest rates for SMEs are more than twice higher than for large businesses in some of the EU countries (in particular Germany and Italy). Therefore, during the last years due to the support programs the sums of loans for SMEs increased.

Figure 2. Comparison of interest rates for SMEs and large enterprises of one-year loans, 2015<sup>21</sup>



Source: European Central Bank and European Commission

According to the data from ECB and EC, more than half of the Czech applications for a loan were rejected, while in Italy and Germany this index is a bit lower. Also, some of the applications were refused due to the high cost of the loan.

Leasing is one of the crucial tools in financial support of SMEs. For some companies, it is even more valuable than the loan from the bank. Leasing organizations support start-ups and SMEs with high potential. It provides mandatory assets for businesses like land, equipment, technologies, machinery and others. Such type of financing is beneficial for companies as it does not require any guarantee. Moreover, lessors can replace the provided asset with the better one in the end of the contract.<sup>22</sup>

<sup>21</sup> Small and medium-sized enterprises' access to finance (2015). European Commission.[online].Available at: [http://ec.europa.eu/europe2020/pdf/themes/2015/small\\_medium\\_enterprises\\_access\\_to\\_finance\\_20151126.pdf](http://ec.europa.eu/europe2020/pdf/themes/2015/small_medium_enterprises_access_to_finance_20151126.pdf)

<sup>22</sup> Leaseurope.org. (2017). Leaseurope - SME Leasing. [online] Available at: <http://www.leaseurope.org/index.php?page=smeleasing>.

Figure 3. SME investment types in Europe <sup>23</sup>



Source: "The use of leasing amongst European SMEs", 2015

The network of the angel investors exists to help businesses to find a Business Angel for them. "It is a smart and patient capital" - due to their knowledge and financial opportunities. Business angels are very experienced, mostly act individually and have a good eye on start-ups with a great potential. They provide private assets in a form of capital and also share management skills and even some valuable contacts. In the EU business angels investments are appreciated, especially the cross-border cooperation of new companies with the investors. There were around 200000 Business Angels in total in EU according to the final report of Evaluation of EU Member State Business Angel Markets in 2012. It should be mentioned that not all of the registered members are active players. The average sum of contribution varies depending on the project from 20000 to 150000 EUR<sup>24</sup>.

The opportunity of venture capital is for those SMEs that have troubles with getting loans. Most often this instrument is used to support the business that has a good potential to grow with innovative products or services. Although there are also some situations when it can be used for usual business. Still, investors are more careful dealing with start-ups because of the big risk. For this instrument, such initiatives as Regulation on European Venture Capital Funds as well as Competitiveness and Innovation Framework Program (functioning till 2013) were created to set common rules for venture funding.

Venture funds help small businesses to grow due to the involvement of experienced managers. Data from the European Commission shows that in 2015, venture capital funds of EU had at its

<sup>23</sup> The use of Leasing amongst European SMEs (2015) [online]. Available at: <http://www.leaseurope.org/uploads/documents/SMEs/Leaseurope%20SME%20Report%202015%20Key%20Findings.pdf>

<sup>24</sup> European Commission (2017) Internal Market , Industry, Entrepreneurship and SMES. Business Angels [online]. Available at: [https://ec.europa.eu/growth/access-to-finance/funding-policies/business-angels\\_en](https://ec.europa.eu/growth/access-to-finance/funding-policies/business-angels_en)



disposal about 5 billion EUR. In addition, the European funds were quite small to help start-ups to gain a position on the world market.

To improve this situation The European Commission and the European Investment Bank created the program Venture Capital Fund-of-Funds. Behind this name hides a huge financial machine, which aims to raise a number of private investments in order to increase the potential of growth of new companies. Inflows into European businesses amount up to 400 million EUR. Funds received from private sources, which allow young EU companies to get at least EUR 1.6 billion investment.<sup>25</sup>

Crowdfunding, as one of the latest tendencies, gained a great attention in funding area. Such financial support more often is realized via the Internet with such instruments as contributions, investments or donations. It can be beneficial for any type of the business or industry.

There also exists a guide for SMEs on crowdfunding and all mentioned before policy areas on the web page of the European Commission to help entrepreneurs to use this form of finance in a right and favorable for them the way.<sup>26</sup>

### **1.3.3 Microfinancing**

The great majority of created businesses have a life duration about five years and the most often problem is the lack of finances. For this purpose during the last years, microfinancing became a solution, which implies issuing of microloans for companies that are close to poverty. Microloan, in accordance with its title, is short-term loan (up to one year) with maximum sum available up to 25000 EUR<sup>27</sup>. Due to such loans, entrepreneurs are able to prolong their activity without crisis experience<sup>28</sup>.

Microloans are helpful for the businesses that have enough own resources and need only recurrent financing (typical in Germany). On average, the most frequent sum of loan is between 1000 – 10000 EUR. “The Facility aims to help those with limited access to the conventional credit market: female entrepreneurs, young entrepreneurs, entrepreneurs that belong to a

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<sup>25</sup> Euforyou.biz. (2016, Dec 1). Стартапы в Польше и Евросоюзе в 2017 году будут развиваться активнее. [online] Available at: <https://euforyou.biz/posts/2235832>.

<sup>26</sup> Growth. (2017). Crowdfunding - Growth - European Commission. [online] Available at: [https://ec.europa.eu/growth/access-to-finance/funding-policies/crowdfunding\\_en](https://ec.europa.eu/growth/access-to-finance/funding-policies/crowdfunding_en).

<sup>27</sup> Regulation (EU) No 1296/2013

<sup>28</sup> Luckett, K. and more, R. (2014, Aug 5). 3 Startups Offer New 'Microloan' Options for Entrepreneurs With Big Ambitions. [online] Entrepreneur. Available at: <https://www.entrepreneur.com/article/235947>.

minority group, those with a disability, sole traders, etc.”, - according to the EU Small Business Portal.<sup>29</sup>

The receivers are most often self-employed individuals or micro businesses. Intermediaries are important participants of microfinancing as the financial support is not awarded directly by the EU. Such agents offer cash loans or equity finance.

The reasons for applying for the microfinancing are the following ones: Assistance in the Framework Program; the entrance of the individuals of the business world after being fired or just loss of the job – European Progress Microfinance Facility; Funding for the already existing small business – the Joint European Resources to Micro and SMEs network. The micro business occupies an influential place in the European economy and it is vital to enable the businesses development.

The European Microfinance Network (EMN) deals not only with the microfinance but also provides training and business development consultancies. According to the data available on the EMN web page, almost 80% of microloans are issued for the business reason. In 2013 around 390000 microloans were issued amounting 1,5 billion EUR in total. Such credits supported more than 120500 micro businesses and start-ups.

German Raiffeisen Bank and Italian cooperative model of loan “Casse rural” were the founders of the microfinancing idea.<sup>30</sup>

For the Czech Republic, the information about microfinancing is absent on the EMN web-page.

In Germany, microfinancing is gaining momentum. Deutsches Mikrofinanz Institute (DMI) is a special institution that settles and monitors the standards. Such support can be implemented by the private microfinance institutions (MFIs), regional banks (public, private and cooperative ones) and by governmental bodies that are focused on unemployed or immigrants.

Microfinancing in Italy develops due to the unreasonably high-interest rates from various types of lenders. Italy has own microfinance network – RITMO, that aims to share gained experience in order to ease the microloans development. The examples of no- bank institutions, which

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<sup>29</sup>European-microfinance.org. (2011, July). EMN. [online] Available at: <http://www.european-microfinance.org/index.php?rub=microfinance-in-europe&pg=introduction>.

<sup>30</sup> Growth. (2017). Loans and guarantees - Growth - European Commission. [online] Available at: [https://ec.europa.eu/growth/access-to-finance/funding-policies/loans-guarantees\\_en](https://ec.europa.eu/growth/access-to-finance/funding-policies/loans-guarantees_en).

provide micro credits are the following: cooperatives, providing loans mostly for the household need; lenders within the determined limits; microfinance institutions or NGOs.<sup>31</sup>

To sum up the role of SMEs is determined by its contribution to the economy. SME is one of the development and prosperity forces in the country. Due to the positive impact on the economy, governments are supporting SMEs via various programs that motivate more entrepreneurs to start their business activities.

Generally, the first step for many entrepreneurs is to ask for a loan in a bank. However, sometimes it is very difficult to get as SMEs are not considered to be stable and banks are afraid to give them loans due to the risk of non-return. For that reason, European Commission introduced SME support programs, which can issue guarantees and provide financial support, assistance and consultations in various aspects. Due to such instrument around 340000 SMEs got financial support in the EU.<sup>32</sup>

The funding from European Commission is available for companies any size or sector, and the decision about financing is made by the local financial institution. Priorities, which are highlighted are the promotion of entrepreneurship and skills, improvement of the market access, decreasing the level of bureaucracy, SMEs' growth, strengthen the communication of shareholders with SME.

Unfortunately venture capital and private equity are not very popular types of financing among the EU SMEs. Notwithstanding that fact these types of support are important for innovative and sometimes risky SMEs, which could not get the financing from the bank.

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<sup>31</sup> European Commission - European Commission. (2017). Funding, Tenders. [online] Available at: [http://ec.europa.eu/contracts\\_grants/microfinance\\_en.htm](http://ec.europa.eu/contracts_grants/microfinance_en.htm).

<sup>32</sup> European Commission (2017) Internal Market, Industry, Entrepreneurship and SMES. Loans and guarantees [online]. Available at [https://ec.europa.eu/growth/access-to-finance/funding-policies/loans-guarantees\\_en](https://ec.europa.eu/growth/access-to-finance/funding-policies/loans-guarantees_en)

## **Chapter 2. Problems and prospects of small business development**

### **2.1 Porter's Five Forces analysis of SMEs environment**

The evaluation of the environment in which certain business operates is conducted using Porter's Five Forces. This analysis helps to determine the barriers and opportunities of small businesses and start-ups, find the potential for development and the key competitive features in order to reach the success and constant growth of the company. Usually, this analysis is done on the very initial stage. In line with this idea, the analysis is also beneficial for existing companies to highlight the most important factors that are affecting businesses success. Afterward, it can advance the strategic planning.

According to Porter's Five Forces, the following tools are distinguished:

1. Buyer power - value of each individual buyer for the business. Concerns the information of the number of customers that really need the offer, the easiness to switch from our products and services to another. Start-ups usually invent some rare products that customers will not be able to get from somewhere else, which means that buyers have less bargaining power. Therefore, commodities can be available and easily got from many suppliers, this is why it is important to provide additional services and satisfy the client to make him loyal.
2. Supplier power can influence the entrepreneurs' margins. It is vital to understand the easiness for suppliers to drive up prices, a uniqueness of their product or service, the cost of switching from one supplier to another. Suppliers of rare inputs have an extremely high power, especially in small business. Large enterprises usually have the ability to choose among the variety of suppliers, from whom they can order the materials. For this reason, supplier power in big business can be limited.

Usually, when starting the business each entrepreneur is dependent on the supplier and can spend much time to find the most appropriate offer, taking into account price, quality, distribution services, etc. Moreover, suppliers are less interested in SMEs as they need big sales. But situation can be different, depending on the industry.

To sum up, not only customer should be motivated to buy the product or service but also supplier should be interested to cooperate with the entrepreneur. The vendor should be interested in cooperation with SME, having benefited from a partnership, the opportunity for cooperation with other SMEs from the same industry and being motivated by company's potential to grow and expand.

3. The threat of substitute products – type of indirect competition that can affect sales. Often it can happen when the brand new innovative product appears. Moreover, customers can find an alternative products or services, which suits them more, meeting the demand in a better way. Nowadays environment is extremely progressive and miss of some innovations can effect on loss of customers, as they can switch to a modern innovative solution. That is the reason for day-to-day investigations of new trends to be demanded by customers. Start-ups are usually based on innovation, but the rate with which they appear does not allow already created the business to function with a stable pace. Constant updates are crucial on the way to success.
4. A threat of new entry means that more competitors can occur in future in a certain sector. For the industries with a high entry cost, such threat is lower. However, a threat of new entry is quite dangerous for the sectors with the low entry cost as a market can be flooded with many new opponents. Moreover, in a tough competition companies can decrease the product prices to attract more clients. And if the target group is price sensitive, the company can become bankrupt. That is the weak side of the SMEs.  
  
Such businesses do not require huge capital in the beginning, plus there exist a lot of supportive programs, subsequently, new entries are predictable. The only border can occur for SMEs is the idea uniqueness or secret of production. The new company should not be always recently established, sometimes experienced player can come from the different sector with a good background. As a result, entry of competitors in the industry is one of the reasons of SME's failure.
5. Competition in the industry. The force is about the number of existing competitors that provide the similar or the same service as the company does. That is a consequence of the previous force. New entries obviously create competition in the industry. The market analysis and evaluation help to understand the prices that can be offered from the both sides. However, more important is to define the feature, which makes the company different from the others in quality and service parameters. Such differentiation can increase market share and business profits in future. Small businesses that have similar products can differentiate with the help of additional services provided, technical support, friendly staff and creative marketing communication.

For the company, the following questions can help to find the most effective and efficient forces.

- Can the supplier be easily changed to another one? How much could it cost?

- What is the proportion of buyers and sellers of the product? What is the extent to which customers are buying? How valuable is the service or product for the client?
- What are the number and the size of competitors? How different are the products among competitors? How much can it cost for buyers to switch from one seller to another?
- How different is the price and quality of substitutes? To what extent substitutes could replace the original offer.
- How fast the industry grow? What are the barriers to entry; are they small or big? How much capital is necessary to invest? What are the expected revenues? Which limitations exist from the government's side?<sup>33</sup>

## **2.2 Challenges on the way to growth for the start-ups and existing small business.**

Starting a new business is a responsible step, which requires accuracy, attention to details and motivation. Some potential businesses cannot overcome faced difficulties and leave their ideas halfway to complete. Not to be among failed businesses, entrepreneurs should be aware of the common barriers and challenges; try to make their own research to get primary data concerning the industry and target group.

The biggest problem for start-ups is the ability to stay on the market. They are very sensitive to crisis periods. There is an extremely low number of new businesses that are able to survive more than 5 years. (See Appendix 1)<sup>34</sup>

In accordance with the European Parliament briefing, there are the following obstacles that slow the SMEs functioning and create barriers on the way to growth.

Internal obstacles are connected with the information problems, price setting limitations, employee's professionalism.

The cost of market research is also the expensive process and entrepreneurs are using secondary data. However, such information can be inappropriate for the company's idea and unreliable.

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<sup>33</sup> Cate Costa (2015, Sept 22) Porter's 5 Forces Analysis for Your Startup or Small Business [online]. Available at: <https://www.linkedin.com/pulse/porters-5-forces-analysis-your-startup-small-business-cate-costa>

<sup>34</sup> Euforyou.biz. (2016, Dec 1). Стартапы в Польше и Евросоюзе в 2017 году будут развиваться активнее. [online] Available at: <https://euforyou.biz/posts/2235832>.

Focus on the domestic market can be a beneficial option when a product is not standardized and should be adapted to the every foreign market. However, from the other point of view, such option limits the scope of consumer audience and the possibility of global expansion. Afterward, all these factors depend on the founder's strategy, targets and expectations.

The challenge of a creation of exclusive product or service exists in almost every small business. Nowadays it is difficult to invent an absolutely new product, therefore already existing products on the market can have high standards. Moreover, price settlement opportunities by the competitors' prices on the market.

Usually qualified workers are costly and for SMEs it is difficult to find affordable and appropriate workforce. Moreover, for large companies, it is easier to enter the new market due to the better resources availability. Furthermore, such organization is able to employ more costly working force even from abroad that is qualified and experienced. On the contrary, SMEs are looking for the cheap labor. Likewise, big companies have opportunities to provide training and workshops for the employees to increase professionalism level, however, small firms usually cannot afford it.

Administrative barriers are dealing with the legal issues. The regulations require a lot of red tape work. For the majority of SMEs' taxes are a great obstacle faced during small business functioning. The taxes are much more costly for small companies than for large ones. Moreover, the corporate tax rates are different among the EU countries

Financial burdens are about the ability of the company to cover the expenses. This is the most common obstacle faced. The rules of access to finance differ among EU countries.<sup>35</sup>

SMEs usually lack the finances, have difficulties in borrowing money from the bank and spending much time to look for the investor. In addition to that even with the ability to get loan companies sometimes cannot afford it because of the requested guarantees and high-interest rate.

Moreover, in small business CEO makes decisions by himself and does not get a lot of suggestions. Going international is more often fully CEO's responsibility. The manager should gain a certain level of experience, explore new markets and look for the most beneficial and convenient approaches to make the correct decisions, although that is again a time-consuming process. Moreover, such market analysis requires a lot of time to be spent abroad, being without

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<sup>35</sup> European Parliament (2016, May). Briefing. Barriers to SME growth in Europe

family. If CEO's presence is needed at home it would be difficult to find a person, who can substitute him for a certain period. Consequently, people refuse to sacrifice family for business.

Usually, in big corporations, there are special responsible departments with the divided commitments among them. Therefore, due to the lower number of employees in a small business, there are many obligations on the shoulders of CEOs and managers. Indeed the target can be achieved in a longer period as it can be difficult to manage a lot of tasks simultaneously. The lack of managerial time can lead to the business stagnation.

Unfortunately, for small and medium-sized businesses there is no chance to find a possibility to benefit from the economy of scale. Additionally, small businesses do not get a high discount as they are buying the comparatively small amount of raw materials. Moreover, they have fewer opportunities to introduce innovations, use forces of marketing or management specialists to increase sales. Such decisions are too costly for SMEs, and even if start-up was already with the innovative idea it should be updated according to the new tendencies. Also, promotion is a vital part that requires finances for research and analysis of the target group.

One of the common problems of failing is that SMEs are neglecting the strategy formulation. A good company's performance is directly related to a strategy prepared and settlement of a clear goals definition<sup>36</sup>. Such actions allow to have a clear plan of the steps that should be followed.

There is no specific template for SMEs barriers as every company depends on many factors: the location, industry, strategic planning, and business structure. However, there are also psychological factors, which are sometimes even tougher to overcome.

Fear is one of them. Statistics shows that many businesses fail to exist more than a five-year period that leads to the death of some good business ideas without a chance for existence. There are other fears of changes, of being worth than competitor etc., although encouragement is the thing that can paralyze all the fears on the way to success.<sup>37</sup>

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<sup>36</sup> Miller C. & Cardinal L., 1994; Bracker & Pearson, 1986; Sanford, 1982; Fletcher & Harris, 2002

<sup>37</sup> Williams. The three biggest barriers to small business success, and what you can do to break through.. [online] Evancarmichael.com. Available at: <http://www.evancarmichael.com/library/donna-williams/The-three-biggest-barriers-to-small-business-success--and-what-you-can-do-to-break-through.html>.



Fear is a negative managerial attitude, which may be the result of the scarcity of international experience in turn. Such attitude also pushes entrepreneurs to cooperate with the close nations as usually, they have a similar history, tastes, mentality, and values.

To be more precise as it was mentioned three European countries will be analyzed for both barriers and opportunities. Afterward, we will make a conclusion, highlighting the most favorable environment for doing small business and the ways of overcoming the problems on the way to success.

### **2.1.1 Challenges for SMEs on the way to growth in the Czech Republic.**

The Czech Republic, according to the World Bank Group, is ranked in 27<sup>th</sup> position for the ease of doing business and 81<sup>st</sup> place for the starting a business on a country level comparison.<sup>38</sup>

One of the most visible problems lays in the bureaucratic system, which is the first challenge on the way to start a new business. The following problem is the public transparency. It goes without saying that financial report is a great help and crucial information for a potential investor to make the right decision. In order to get the investor, some Czech companies hide the real situation. Such actions increase the risk for investment in all the SMEs of the country. Investor protection is not on the high level. However, Czech Republic is a member of the Multilateral Investment Guarantee Agency (MIGA) that is the part of World Bank-IMF group.

Investors are crucial for Czech SMEs as it is difficult to get equity financing or take the loan in a bank. There are either small sums offered or huge interest rate.

For operating internationally Czech Republic businesses need to process export goods around 16 days and import goods nearly 17 days, having prepared at the same time up to seven documents, that will let the goods move across the borders, which is not the worst scenario but could be better.

The period of time, consumed by mandatory processes is also a border for SMEs development. For instance, construction permits take approximately four months to get and 33 procedures to accomplish. Also, electricity connection, confirmation of the connection plus the contract itself takes half a year to complete. Despite the fact that there are not so many corporate tax payments (only eight) much time should be spent to process them. The judicial process is quite long

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<sup>38</sup> Doingbusiness.org. (2017). Ranking of economies - Doing Business - World Bank Group. [online] Available at: <http://www.doingbusiness.org/rankings>.

because it is very slow. In addition to the mentioned factors, enforce the contract takes more than one year and a half and again up to 27 procedures.<sup>39</sup>

One of the most differential aspects is culture, which makes each country individual in a way of life, thinking as well as the way of doing business. Czechs businessmen and businesswomen are unequal in treatment and accession. They can sometimes evade a direct answer that is a similar characteristic of Japanese business people. Hurrying is not a typical characteristic of business should constantly grow and develop.<sup>40</sup>

### **2.1.2 Challenges for SMEs on the way to growth in Germany.**

In accordance with the World Bank Group data, Germany is holding the 17<sup>th</sup> in the world for ease of doing business and 114<sup>th</sup> for starting the business out of 190 countries analyzed.<sup>41</sup>

Germany is a leading country in Europe that has stable economy. The country became so influential and strong due to the factors which now can be seen as drawbacks when it comes to business. For example, the legal and tax structure are tough and difficult to navigate, especially for those who are not familiar with it. There are nearly 14 various taxes for business, paid annually. Environment standards and safety are complicated and protective.

Bureaucracy is unavoidable, but still, it brings inconvenience in bigger scope for those, who are doing business internationally. For instance, registration of property can take around 40 days, however, a lot of red tape with the documents accompanies.

Comparing with the other European countries labor costs are high as well as social ones. In Germany, it exceeds EU average level by one-third. In 2015 hourly labor cost was 32.2 EUR on average, while in the Czech Republic it is around 10,2 EUR and 27,8 EUR in Italy.<sup>42</sup> (See Appendix 2)

Cultural factor is important in German business and it can be risky to deal with Germans without cross-cultural awareness. A highly important place is allocated for hierarchy, which can slow a

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<sup>39</sup> Association for foreign investment. [Online]. Available at: <http://www.afi.cz>

<sup>40</sup> Tmf-group.com. (2017). Top 10 challenges of doing business in Czech Republic. [online] Available at: <http://www.tmf-group.com/en/media-centre/resources/top-challenges/emea/czech-republic>.

<sup>41</sup> Doingbusiness.org. (2016). Ranking of economies - Doing Business - World Bank Group. [online] Available at: <http://www.doingbusiness.org/rankings>.

<sup>42</sup> Ec.europa.eu. (2004-2015). File:Labour costs per hour in EUR, 2004-2015 whole economy excluding agriculture and public administration.png - Statistics Explained. [online] Available at: [http://ec.europa.eu/eurostat/statistics-explained/index.php/File:Labour\\_costs\\_per\\_hour\\_in\\_EUR,\\_2004-2015\\_whole\\_economy\\_excluding\\_agriculture\\_and\\_public\\_administration.png](http://ec.europa.eu/eurostat/statistics-explained/index.php/File:Labour_costs_per_hour_in_EUR,_2004-2015_whole_economy_excluding_agriculture_and_public_administration.png).

process of business negotiations. The highest position is to hold by the person, who deserves it due to the skills, abilities, and experience, consequently, the status is always merited.

There can also exist a competition between workers of different departments of a company in order to achieve more. This feature, on the one hand, helps the company to reach the target with the high-quality work done. On the other hand, that is a great disadvantage for teamwork, as competitive environment creates rivalry among employees.

German business people are very precise for the details and usually spend much time for the contract examination. In addition to that, they are direct, expressing opinion in a straightforward manner, expecting the same attitude from their counterparties. Criticism at work concerns only the working process without any transition to individuals. Praise is not common for doing a good job as it is considered to be obvious - to do job in the best way. Jokes and humor can be misunderstood and inappropriate.

### **2.1.3 Challenges for SMEs on the way to growth in Italy.**

Italy is in the 50<sup>th</sup> and 63<sup>rd</sup> places, concerning ease of doing business and starting a new business in turn.<sup>43</sup>

Having a large percentage of SMEs and startups there is still a number of problems while doing business in Italy. One of the widespread and unavoidable challenges is the bureaucracy. Unlike the previously mentioned countries, here corruption appears and consequently unfair competition. Along with that, high levels of taxation with 15 payments annually are required. Italian business environment suffers from the political interference and ineffective judicial system.

Even though Italian industry is considered to be the second manufacturing sector in Europe, it was losing competitiveness on the market last years. As a consequence, Italian government has opened door for FDIs even in strategic areas like transportation and energy.<sup>44</sup> According to the data from 2016, Italian industry is growing again.<sup>45</sup>

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<sup>43</sup> Doingbusiness.org. (2016). Ranking of economies - Doing Business - World Bank Group. [online] Available at: <http://www.doingbusiness.org/rankings>.

<sup>44</sup> Esteri.it. (2017). The Italian Economy. [online] Available at: [http://www.esteri.it/mae/en/ministero/servizi/benvenuti\\_in\\_italia/conoscere\\_italia/economia.html](http://www.esteri.it/mae/en/ministero/servizi/benvenuti_in_italia/conoscere_italia/economia.html).

<sup>45</sup> Italianinsider.it. (2017). Italian industry returns to growth. [online] Available at: <http://www.italianinsider.it/?q=node/3991>.

Time-consuming processes problem is also present in Italy. Although getting the construction permits does not apply more than the average number of procedures of the OECD, it is still a long process, as just to receive a building permit takes around five months. Another time-consuming task is getting electricity, together with trading across borders with 19 days necessary for export and 18 for import in turn.

The painstakingly complex is the process of enforcing the contracts, which needs 1210 days to complete and 41 procedures to perform, compared to the OECD it is 2,5 times more than average norm.

Getting credits is not an easy tool due to the financial crisis problems. The investor protection in Italy ranks 46th in the world and is lower than in Germany.

Resolution of insolvency takes 1,8 years, as there are many procedures to be done.<sup>46</sup> Unfortunately, insolvency resolution issues, which increase due to the financial problems, encumber courts.

Enterprises should appreciate both the business landscape and the culture to overcome international obstacles and interact more effectively and successfully. In Italy, traditions play a crucial role in the society as well as in a business environment. Emotions can also influence the decision-making process, which is why there exist some difficulties with communication. Along with the emotions, the close personal contact and hand gestures are present. However, together with those facts, being informal means impolite attitude.

A typical but a bit unpleasant feature is that people can ignore those, who holds the lower position within the organization.

Italy is a very hierarchical country, which can be a reason of the long decision-making process. To become successful, business people should spend a lot of strengths and energy to build good relationships with their potential counterparties. As it was mentioned already, families are the basis of the culture and there is a strong family presence with a hierarchical managerial style in a business environment.

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<sup>46</sup> Tradeconomics.com. (2017). Time to resolve insolvency (years) in Italy. [online] Available at: <http://www.tradeconomics.com/italy/time-to-resolve-insolvency-years-wb-data.html>.

Decisions are usually made by the key person in a company or by the owner of a business. Surprisingly, Italians do not make detailed business plans and even can avoid marketing plan, relying on improvisation during the tough times.

Italians appreciate traditions and family a lot. Due to such reason there are many family businesses and mostly micro businesses. As a result some people are not keen on migration and are not very mobile as they are responsible for the family business. The young generation is not so concentrated on the family business and does not afraid to try their forces abroad. But it takes time for the country's mentality to change the attitude.

### **2.3 Opportunities for start-ups and existing SMEs. Supportive programs**

The European Union realizes the importance of SMEs and creates supportive programs in order to ease the way of doing business for entrepreneurs. These programs aim the promotion of self-employment among the population; elimination of administrative barriers; strengthen the single internal market of the EU; improvement of laws for the normal existence of the business.

According to European Commission estimations, in the next 20 years in EU, an additional million of jobs can be created because of the growing number of young businesses.

For the potential entrepreneur, the great advantage is the low capital requirements on the entrance level. Despite the fact that legal requirements are the unavoidable obstacles, there is still less bureaucratic work than for of large enterprise.

Also, every large business begins its way from the small company. The opportunities for growth are more real after the break-even point achievement. The company can expand its business, enter new markets and create global product. Starting from the small business, entrepreneur has more chances to get experience, analyze industry and customer segment.

The most attractive opportunity for start-ups is the possibility to get support from the government. Moreover, there are many individual investors in a business environment, who would like to invest their capital in a perspective projection. Basically, innovative and creative ideas can turn into a real business without the necessity of large capital inflows from the owner's side, due to the help of funding programs.

One more advantage of small business is freedom, which allows to make decisions without any dependence from headquarters. Moreover, there is an ability to take risks getting the outcome

of the entrepreneurs' own achievements. Conversely, some large companies can be dependent from SMEs as a result of outsourcing.<sup>47</sup>

To compare and to understand the opportunities of doing business in the three analyzing countries their advantages and positive aspects will be highlighted.

### **2.3.1 Opportunities for SMEs in the Czech Republic**

The strategic location of Czech Republic in the Central Europe, EU membership, competitive infrastructure and educated workforce are the benefits of this country, which lead to the attraction of many foreign direct investments (FDIs) into various sectors.

Obviously, most investments are coming to sectors with a great potential for development like automotive, manufacturing, aerospace, nanotechnology, energy and business support services. Moreover, due to the absence of restrictions on the investments or ownership makes Czech Republic one of the most successful CEE countries in terms of FDIs attraction<sup>48</sup>.

Furthermore, Czech Republic is one of the EU countries with inexpensive and skilled labor. While in some other countries registration of property is quite a time-consuming process, in the Czech Republic is one of the fastest, which takes around 25 days to complete.

For starters, a new business getting a credit is one of the important issues and the Czech Republic is a favorable country for this purpose. Not the last factor is the own currency, which is more stable and does not depend on the economic situation of other countries as euro currency.

The Czech Republic has numerous bilateral agreements signed with other countries, concerning investment protection. (See Appendix 3)

Due to the strict legal rules, modern financial sector is stable and functions without problems. Infrastructure is developed and very sophisticated, being highly productive the last years. In addition to that, there is a large consumer market that motivates investors to invest their capital in Czech business.

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<sup>47</sup> Longenecker, Justin G.; Carlos W. Moore; J. William Petty; Leslie E. Palich (2008). Small business management: launching and growing entrepreneurial ventures. (14th ed.). Cengage Learning. p. 768.

<sup>48</sup> Startupoverseas.com. (2017). Starting a Business in Czech Republic: Startup Overseas. [online] Available at: <http://www.startupoverseas.com/starting-a-business-in-czech-republic#sthash.BtR9oeIW.dpuf>.

### **2.3.2 Opportunities for SMEs in Germany**

Geographically Germany is situated in a pleasant location, having access to eastern and western European markets and consumers. Similarly, Germany is the basis of the European Union standards. The strict rules covering intellectual property rights (IPRs) are the background of the stable and reliable business functioning. Also, there is a very favorable climate for investments with good economic conditions. As a result country hosts a great number of foreign companies.

Germany has a professional, educated labor force. This is a leading country that contains a great potential for investors and entrepreneurs. To compare with other countries' disadvantages Germany is better in dealing with enforcing contracts, resolving insolvency, getting electricity and construction permits and also is the most innovative nation in the EU.

Germany is concerned to be the most innovative country of EU and the fourth in the world rank. The construction industry, laser systems, nanotechnology, chemicals and automotive are very attractive and profitable sectors in the country. On the local market competition, quality of the product or service is decisive tool to get competitive advantage.

Overall, Germany has a favorable environment for doing business due to the corporate research and development. Also, for SMEs process of getting loan is relatively easy. Additionally, the economic and political situation are very stable and country is extremely powerful on the international arena. Such tools attract investors and what is more, Germany provides the strong investor protection. Being in such a good position, Germany not only receives FDIs but also acts as an investor in other countries' businesses. The country itself is associated with quality and has a great reputation among other national companies.

### **2.3.3 Opportunities for SMEs in Italy**

The Mediterranean location of the country brings important links of Italy with international customers. This location advantage is one of the reasons of investments into the country. Mostly FDIs comes to Italy from the EU and the USA, nevertheless Asian countries are also interested in investing there like China, Russia, and India. Last years these inflows increased.

The Italian SMEs are concentrated over 70% of the total employed population, with 37.4% working in enterprises with fewer than 50 people. Industrial enterprises in small business sector provide about 32% of the added value of products of large enterprises. Such shifts in the industry have been achieved largely due to the reform of large enterprises with the release of these small and medium-sized enterprises.

Italy is a country, where start - ups are gaining momentum of popularity. The majority of Italian citizens are employed in micro enterprises. There is also a large concentration of small and medium family-owned enterprises. One of the most famous is footwear sector, having around 30% of national workforce.<sup>49</sup> In addition to that, some of the biggest corporations can be under the control of one family such as Ferrero, Benneton, and Fiat.

Italy has a fast registering property process, although it can be expensive.

The country has good opportunities for SMEs in such sectors as life sciences, renewable energies, information and communication technologies, consumer goods, high-tech design and engineering products. Research and development sector are on the high level that allows bringing innovation with the higher efficiency. For SMEs the wine production sector is beneficial due to the already established Italian wine brand it is easier to export it to other nations. A huge attention is paid for Italian fashion. The next sector is tourism and every service provider connected with that area, like restaurants and hotels. Therefore the popularity of the industry creates a huge competition that simultaneously can make the business less profitable. The right positioning and unique idea will help the business to survive. It is crucial to remember the culture specifics of the country to be able to create emotional message for the customer to attract attention and create loyal clients.

Due to the fact that Italy is a country of family businesses, employees are rarely moving to another city looking for new opportunities.

#### **2.4 Ways of overcoming barriers. Supporting programs for SMEs in EU countries**

Nowadays, in a fast developing environment businesses should be able to react quickly to changes and barriers they face. Such mission is quite challenging as having been previously implemented once, that particular strategy can no longer be appropriate in the event of crisis. Because of that reason it is recommended to conduct frequent market analysis in order to learn from the competitors' mistakes and be prepared to overcome obstacles with minimal losses.

Several internal barriers can be eliminated after some period of business functioning on the market or after achievement of break-even point. For instance, the market research as well as target group analysis are time-consuming processes and require financial resource. Moreover,

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<sup>49</sup> Euronews. (2015, Sept 28). Future of SMEs: Europe's economic powerhouses. [online] Available at: <http://www.euronews.com/2015/09/28/smes-in-europe-innovating-and-investing-for-growth>.



the leadership positions and creation of a strong brand and image allows business to influence the price settlement on the market.

As it is quite difficult to find a qualified and cheap workforce, company can introduce internships and attract fresh graduates. Also, company with the long-term orientation strategy can invest more into employees to get higher level output.

Administrative barriers are unavoidable, however, European Commission and national governments provide a great help and support. It is difficult to underestimate the positive impact of SMEs on the economic environment. For that reason, governments and authorities try to ease the process of business establishment for businesses perspective.

Financial barriers can be eliminated by the creative idea and innovations that allow to get funding. It is possible due to the programs discussed in Chapter 1, paragraph 1.3.

Experience, together with several challenges, comes after some time of business functioning. Moreover, it depends on the managerial attitude to the business. To be successful, managers should be inquisitive and learn from the competitors' mistakes.

Undoubtedly every businessperson would like to increase sales. To make people buy more business should meet customers' needs and wants, show that the problem they have is connected with the company's product or service and can be solved by its purchase and usage. Analysis of the target group is crucial for demand evaluation. For deeper examination, it is always useful to create the personas. Such tool helps to understand the main motivation of the customer to buy company's product and shows the product features that should be improved.

Moreover, due to the fact that people get an enormous amount of information every day and mostly ignore it, communication tools should be different from the competitors, unique and creative.

Currently, people are used to make purchases via the Internet. For such clients delivery additional service are the decisive factors. Therefore, to be competitive on the market, it is crucial to satisfy and predict clients' wants and potential needs in advance. Customers are ready and are willing to pay more for emotions than for rational decisions.

Following the previous idea, long-term thinking should be present in business. Sometimes it is very costly to implement a certain idea, in the beginning, however, the future outcome can be very profitable. Additionally, as a part of today's competitive market, it is important to be the

first to implement this idea so that consumers could associate the product or service they buy with our company, not the competitor.

Similarly, the sustainability can be achieved due to the right management, team-building, and training. Also, outsourcing can help to release from the processes, which slow down the business by the excess of departments' responsibilities.

### **Supporting programs for SMEs in EU countries**

Support of government is very helpful force for SMEs to overcome borders. Antonio Tajani, the Vice-President of the European Commission said: "SMEs are key in ensuring the economic recovery of the European Union. This is why they should be encouraged wherever possible."<sup>50</sup> According to the Small Business Act introduction, SMEs have better conditions and access to loans and venture capital. In addition to that, in the EU the "Innovation Union" exists, which supports innovations, connected with solving the global environmental problems. Innovations are the force, which ease the expansion of SMEs beyond borders. Support can be also in form of export credit guarantees, technical support and pre-shipment financing.

Apart from the support provided by the European Commission, there are some individual incentives in Member Countries. For instance in France in 2016 an idea of Blockchain was established. The seven major European banks announced the signing of an agreement on the development Blockchain technology for small and medium-sized businesses. The project is open to all international partners and is aimed at facilitating the access of European businesses to capital markets and increase in speed, security, and transparency in post-trade operations.

The following programs of the elimination of financing barriers are soft loans for export activities that imply lower interest rates and prolonged period of repayment.

The table below presents the organizations that provide export insurance and guarantees for the following analyzed EU-member countries.

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<sup>50</sup> Erionet.org. (2017). EuroNet - How does the EU help small businesses? [online] Available at: <http://www.erionet.org/>.

Table 1. Programs for eliminating financing barriers

Czech Republic	Germany	Italy
<ul style="list-style-type: none"> <li>• The Export Guarantee and Insurance Corporation (EGAP),</li> <li>• CzechTrade,</li> <li>• Czech Export Bank.</li> </ul>	<ul style="list-style-type: none"> <li>• Export credit guarantee by the German Federal Government – Hermes cover</li> </ul>	<ul style="list-style-type: none"> <li>• The Ministry of Foreign Trade</li> <li>• Mediocredito Central</li> </ul>

Source: Ministry of Foreign Trade of Czech Republic/Germany/Italy

#### 2.4.1 Support of SMEs in the Czech Republic

The Czech SMEs usually get financing from the banks and do not take into consideration other funding possibilities. Such dependency from the banks makes businesses more vulnerable. For SMEs loans are quite expensive, while large businesses have much lower interest rates due to their stability. Indeed equity financing used much less than the average EU index.

Funding support in a country is organized with the help of the Czech Export Bank, which provides loan and guarantees issued by the government. Czech-Moravian Guarantee and Development Bank (CMZR) also provides financing to promote SMEs.

In 2015 Czech SMEs got an opportunity to get loans from Komerční Banka and Česká spořitelna, enabled by Horizon 2020. Consequently, more than 250 million EUR are available during the last two years for SMEs.<sup>51</sup>

Moreover, there is an interesting project for small business entrepreneurs that names CzechAccelerator. It is focused on specific start-ups that have a great possibility of three months exploration of foreign business incubators in Silicon Valley, London, Singapore and New York. The budget of the project is around 2,6 million EUR. Altogether Czech Invest is going to send there around 60 companies.

The main objective of the project to give SMEs chance to increase their competitiveness, gain useful connections and find investors. CzechInvest also helps SMEs via increase of their image

<sup>51</sup> Ec.europa.eu. (2017). News Alert | Research & Innovation. [online] Available at: <http://ec.europa.eu/research/index.cfm?pg=newsalert&year=2015&na=na-310315>.

on the media and raise of competitiveness on the market. The same project was implemented in 2011-2014. Nearly 24 million CZK were spent to provide support of 40 companies.

Starting the business in Czech Republic entrepreneurs should be aware of the Commercial Code that provides all the necessary legal texts for business establishment. Moreover, depending on the industry and size of business the support can be in a form of tax rate reduction, subsidies or already discussed financial support.

#### **2.4.2 Support of SMEs in Germany**

More than half of economic output is generated by the SMEs that is why they are a backbone of the country economy. In accordance with the mentioned fact, the German government is interested in SMEs promotion. It supports SMEs in two main ways: by direct support or by the financing of their researches. The great attention is paid to innovative ideas in businesses, which are provided by KMU innovative support.

The success of German SMEs (Mittelstand) lies in a high level of innovation, orientation on the international market and professional labor. It uses the principles of long-term relationship establishment, business stability, and reliability. SMEs are cooperating with the large enterprises that increase productivity and development of both parties.

Also, Germany has a program that aims to reduce investments costs for the business. It names the Joint Task Program for the Promotion of Industry and Trade (in German Gemeinschaftsaufgabe - GRW). The program supports all types of businesses and can provide cash support for SMEs up to 35% of the business project cost.

What is more, there are entrepreneur loans with the reduced interest rate. The most popular bank, which has such offer is the KfW Bankengruppe. Such program is mostly oriented on start-ups with the available loans up to 25 million EUR and fixed interest rate for nearly ten years. There are more opportunities from many development banks in Germany, which offers various loan programs to meet the needs of start-ups and perspective businesses.

Public guarantees are the other form of governmental support of SMEs in Germany, which can cover up to 80% of the borrowed sum. According to the amount required, location of the business and size different programs can be chosen. For guarantees, there are some fixed fees envisaged, which depend on the guaranteed amount.

As it was mentioned in SMEs barriers part, one of the challenges faced is connected with the labor force. The support is provided by Federal Employment Agency and German Trade and Invest. There are main areas of support in human resource sector:

- Assistance during the whole recruitment process;
- Training for new employees and advanced training. The company can receive up to two million EUR or cover half of the training cost.
- Wage subsidies – for permanent contracts (can be also in a form of grant up to 50% of the wage amount).

Moreover, there are some agencies that offer assistance in market analysis and help businesses to enter new markets. "Global Active Initiative" in Germany procures assistance in SMEs support, including fairs organization, also offers information provision and consultations.

Research and Development projects in Germany are supported by government and German states. They are focused on technological improvements and innovations and provide support in form of loans or grants. An example of such incentive is ERP Innovation Program that is ready to provide financial support up to 5 million EUR.<sup>52</sup>

For SMEs support, there is the Central Innovation Programme (ZIM). This funding program is focused mostly on the technology improvements and innovations. ZIM provides financial help for individual businesses and network projects aiming to raise German competitiveness on the market individual. For ZIM funding there is no limitation for SMEs, which according to German definition amounts up to 500 employees.<sup>53</sup>

### **2.4.3 Support of SMEs in Italy**

Italian SMEs are mostly functioning in the sector of wholesale and retail trade, business support services and accommodation services. Small and micro businesses are supported by the government. Moreover, the micro business is considered to be the most valuable.

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<sup>52</sup> GmbH, G. (2014). GTAI - Homepage. [online] Gtai.com. Available at: <http://www.gtai.com> [Germany Trade and Invest].

<sup>53</sup> Foerderinfo.bund.de. (2017). Funding for SMEs - Funding Advisory Service. [online] Available at: <http://www.foerderinfo.bund.de/en/funding-for-smes-1786.php>.

In Italy the consortium of seven large banks created a 300 million EUR fund to support growth of national SMEs. Due to the Horizon 2020, from June 2015 till these days Italian banks issued loans in a sum of 220 million EUR.<sup>54</sup>

Financial support is also provided by the Guarantee Fund. Italian government implemented some fiscal advantages for SMEs like tax credit for the investment of more than 10000 EUR or tax elimination on bonuses for workers, which ease the SMEs functioning on the market.

Italian profile is not very powerful among the EU countries. Still, the government is implementing new incentives to support local SMEs. To motivate potential entrepreneurs there were established following projects. For instance, in 2014 the EU Youth Guarantee scheme was introduced. It provided trainings for people under 29, which encouraged companies to hire young workforces in turn. In addition to that, a compulsory business practice in some companies was introduced for students of high schools. Such action allows them to gain experience till the graduation, which in future would help students to find a job. From the companies' side the advantage of additional low-cost workforce appears.

For businesses in tourism, social or cultural areas 1,5 million EUR were given under the "Self-employment program". Also, in order to simplify the administrative procedures, the online platforms were created: "Communicate", "Empresa in un Giordano", "PagoPa". This step allowed to realize payments on-line, get electronic invoices and get access to necessary information.

Due to the high level of corruption there exist the anti-corruption authority – ANAC. However, this problem still requires additional intervention.

In Italy exists a great differences between the firms' size and structure depending on the region, and government diversifies among the Northern, South, and Central region of companies' allocation. As a consequence, multi-regional support programs were offered for these regions, which included export financial funds as well as search and selection of some experts in export area.

For the enhancement of the internationalization the label "Made in Italy" received support of 232 million EUR. Moreover, internationalization process is supported by the "International

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<sup>54</sup> Ec.europa.eu. (2017). News Alert | Research & Innovation. [online] Available at: <http://ec.europa.eu/research/index.cfm?pg=newsalert&year=2015&na=na-010615>.

vouchers” and grants for SMEs consortiums. Such consortiums can get up to 400000 EUR grants if they consist of minimum five SMEs of one industry and are located in three regions of Italy.

Innovation is a strong area of Italian performance and a great attention is paid to the digital technologies. Italy encourages interest and skills of young generations in this sector and supports them via the special program "Eccellenze in Digitale" with the help of Ministry of Labour and Social, Policy.

Overall, each business faces difficulties on his way. The main factors that influence the business activity are human resources, finances, administrative barriers and entrepreneur experience. On the contrast, the opportunities and support of the SMEs on the EU and national level encourage entrepreneurs to implement their business ideas into reality. On the example of the Czech Republic, Germany, and Italy there were described the main obstacles for SMEs on the national level together with opportunities to grow. For the Czech Republic, the biggest problem is the lack of transparency and red tape, however, there are many opportunities due to the location and low costs of doing business. In Germany, bureaucracy is one the stumbling stones for SMEs, the level is higher than in the Czech Republic and the cost of doing business is high as well. On the contrary, there are many opportunities for innovations due to the powerful economy of the country. Italy is famous for micro family businesses, mostly in tourism and fashion sectors. The problem of the country is corruption and culture aspects.

In order to compare the difference of starting business between three countries there is a short instruction of the necessary and mandatory actions for the entrepreneurs. The main steps Entrepreneurs should follow to register a new company in the Czech Republic, Germany or Italy are provided below.

### **Starting a business in the Czech Republic**

1. Company's name uniqueness on database of Ministry of Justice.
2. Preparation and notarization of articles of association.
3. Confirmation from the bank about the capital held on the account.
4. Registration of business with the Trade Licensing Office.
5. Registration in the Commercial Register.
6. Registration in tax office.
7. Social security registration.
8. Health insurance registration.

Financial resources needed: 500 - 840 EUR. Period: 6 - 10 days

### **Starting a business in Germany**

1. Check of company's name in Chamber of Industry and Commerce.
2. Preparation and notarization of articles of association.
3. Initial capital deposit in a bank.
4. Submission of Commercial register by Notary Public.
5. Trading permits for certain businesses.
6. Registration in professional association.
7. Creation of a number for reporting to the Social Security Office.
8. Health and social insurance for employees.
9. Registration in local tax office.

Financial resources needed: 694 EUR. Period: 6 - 10 days

### **Starting a business in Italy**

1. Public deed of incorporation and company bylaws.
2. Accounting and corporate books purchase.
3. Authentication accounting and corporate books tax.
4. Certificated e-mail activation and registration.
5. Create tax identification number, VAT number. Registration with Social Security Administration and Accident Insurance Office.
6. Notification of Labor Office about employment.

Financial resources needed: 621+ EUR. Period: 4 - 7 days <sup>55</sup>

Overall there are no great differences among the countries between price and period needed for the business establishment. Italian business environment requires less procedures comparing with the other two analyzed countries. Germany has more complicated procedure for the SMEs establishment, whereas Czech Republic offers the cheapest price for business establishment. Still there are many differences, depending on the industry, location, company size and business idea, which that should be considered in each case individually.

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<sup>55</sup>Doingbusiness.org. (2017). Starting a Business in Czech Republic - Doing Business - World Bank Group. [online] Available at: <http://www.doingbusiness.org/data/exploreeconomies/czech-republic/starting-a-business/>.



### **Chapter 3. Business challenges in present environment.**

Nowadays, apart from the discussed threats and opportunities for SMEs there are some specific factors for businesses that are going to enter new markets. Entrepreneurs are focused on increase of profitability, company's growth and expansion of customer segment. Such ideas lead business people to the internationalization. Around 60 % of SMEs target their products and services on the foreign client. Moreover, almost all SMEs are planning to conduct business on the global scale.<sup>56</sup>In this chapter the process on entering foreign market is discussed.

#### **3.1 How small business goes international**

Operating on the international market expands customer segment and attracts investors. According to the John B. Cullen and K. Praveen Parboteeah, there are two main ways of business internationalization. The first idea is based on stages business passes in order to enter new market. Second - is foundation of a multinational organization through global start-up from the beginning. The most common is the first way as it seems to be less risky due to the gradual integration.

The highlighted steps of the steady internalization process consist of the following stages.

- The first stage is so called unconscious acting on the international market or 'passive export'. Organizations are not looking for the opportunities on the foreign markets, although are filling the international orders.
- The second stage is readiness for the opportunities on the international market. A specified manager is responsible for export sales seeking
- The third one is the liberation from the fear of risk of cross-border export. Managers in this stage are active seekers of export opportunities abroad. The supportive tool in current step is a reliable intermediary in the importing country.
- On the fourth step appears demand from the international market. To operate more effectively it is recommended to set up sales offices for the company, to provide services locally and shorten the communication time between supplier and customer.
- If until this stage company was successful, earning more and more, the next step is to establish production centers directly in the importer's area. Such decision is beneficial and risky as on the one hand, firms have advantages from the local

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<sup>56</sup> Shubhomita Bose (2016, Aug 26). International Customer, Survey finds [online]. Available at: <https://smallbiztrends.com/2016/08/small-businesses-going-global-survey.html>

adaptation, joint ventures, and direct investments. But on the other hand, such action requires a lot of financial resources and unfavorable consequences can ruin the company at all.

- The last stage names ‘transnational’, meaning network of transnational corporations.

In reality, the structure is not so clear, as the internationalization process is more blurred and flowing. Some stages can stream extremely fast, while others can pass for months or even years. Nevertheless, following the model assists companies in their business development and helps to move gradually with the elimination of risks on their ways.

Born-global firm is considered to be more complicated. Frequently, products from high-tech organizations and fast changing industries need to go international urgently. Such companies have such characteristics as flexibility, fast reaction on changes as well as innovations (that have a great impact on the business climate). Previous way was more suitable for “conservative businesses”, although this one is more risky and unpredictable. Therefore, the outcome of successful born-global company is higher due to the risks taken.

Going international is a process that needs preparation. There are some issues, which show that company is ready to enter foreign market. Firstly, the enterprise should have a product or service that is standardized and does not need global adaptation procedures during exportation to the different countries. Otherwise, product characteristics and marketing communication tools should be adjusted to each market.

Secondly, it is crucial to analyze if the company is able to meet customers’ demand and stay competitive among the local products on the foreign market. Karl Vesper claimed that certain level of company’s competitive advantage should exist before entering a new market, which is called “entry wedge”. If the price and quality are acceptable on the market and do not harm for the organization and its budget it will result in a good image for the brand.

The Internet access and the E-commerce provide a great support on the way of internationalization. Namely due to the web pages the purchase of products and services abroad became much easier on the multinational arena. It has low cost for entrepreneur as there is no need to establish the network of outlets. The customer can benefit from the ability to choose from the whole catalog of available products or services. E-commerce enabled the more competitive and fair environment among the international companies; harmonized and simplified transactions process and increase of international trade.

Internationalization brings benefits for entrepreneurs and industry, simultaneously increasing the country's competitiveness level. The opportunities and stimulus that motivates internationalization are combined into the following main groups:

1. Growth opportunities, expansion of the production line, increase of profitability, stronger and more stable market position, increase of the share on the market. The internationalization is the tool that leads to return maximization, which can be reached due to the economy of scale.
2. Knowledge and experience gained – related motives that are associated with the willingness to gain know-how to be successful in technological development. Also, new markets ensure companies with the newly available workforce. Such advantages raise the international competitiveness of the company.
3. Network/Social Ties and Supply Chain Links is a stimulus that highlighted the importance of the ties (family, social, business) in global market, which brings benefits and some privileges.
4. Domestic/Regional Market drivers, meaning that internationalization can rise in those regions, which have less favorable domestic conditions for business operation

According to the authors Kocker and Buhl, 2007, the investigated in this thesis countries have different motives of internationalization. Germany and Italy have a knowledge and relationship search motivation. The Czech Republic refers more to Network and Social drivers group. Nevertheless, it is hard to set the strict categories as motivation intertwines regardless of the country and more depending on the nature and personality of the entrepreneur.

OECD-APEC recognizes the main obstacles for SME internationalization taking into account member's view:

1. Insufficient level of staff competence for entering a new market.
2. The lack capital for export financing.
3. Lack of needed information and market analysis.
4. Underestimation of foreign business opportunities.
5. Lack of managerial time.
6. Inability to meet demand of potential client.
7. Adjustment of the product for foreign markets.
8. Unfamiliar business environment and level of competition.
9. Unfamiliar procedures of exporting and specifics in legislation.

## 10. Tariffs and non-tariff barriers.<sup>57</sup>

Apart from the mentioned, there are also more challenges, such as administrative procedures, technical barriers, transaction difficulties, exchange rate differences, competition that exists in both local and foreign markets. However, the influence of such factors is difficult to summarize as it depends on political and economic environment of the country, where the business is functioning; level of corruption and bureaucracy; lobbyism and etc.

Unfamiliar economic, social and cultural environment creates challenges for SMEs. For examples, high tariff barriers, sanitary and phytosanitary measures, technical standards, customs procedures are the most common issues that company should study before entering the market. However, other obstacles can be difficult to understand because of the lack of transparency. For instance customer preferences, specific government restrictions, marketing communication tools and other local specifics in business.

Identically, there are some recommendations for overcoming difficulties during internationalization process.

Due to the size, small companies are very flexible. SMEs have a great advantage to adopt their products or services to the changes in the international markets faster than large enterprises. There are fewer problems with red tape than for large enterprises, although these factors still slow down the process of entering foreign markets.

In order to overcome difficulties, SMEs can use various modes of entry foreign market. It can be export/import type that is usually organized with the help of intermediaries. Depending on the company's preferences intermediaries can act from on their behalf, earning predetermined fees. These can be commission agent, exclusive distributor, commercial representatives, brokers, piggybacking or export alliances. The last two suits the most for SMEs as piggybacking allows to operate as a part of the experienced big corporation; export alliances are the associations of small exporters.

Moreover, the company can use equity mode of entry like acquisition, joint venture, merger or FDI. However, these types suit more for companies that have a considerable market share and definitely not for start-ups.

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<sup>57</sup> Oecd.org. (2007). Glossary for Barriers to SME Access to International Markets - OECD. [online] Available at: <http://www.oecd.org/cfe/smes/glossaryforbarrierstosmeaccesstointernationalmarkets.htm>.

The last non-equity mode can be also attractive for entrepreneurs. With the help of franchise, license, production cooperation or management contract, entrepreneurs can get a great support in a form of predefined management, brand name, business process and other. Such modes allow owning a small business in a short period of time.

European Commission provides support for SMEs internationalization as well. It organizes consultations, issues guide materials in order to ease the process of entering new markets and prepares entrepreneurs for some possible barriers in advance. The guidebooks also provide some examples of the internationalization practices. Indeed the IPR Helpdesk provides assistance for SMEs that secures the company and improves the performance.<sup>58</sup>

Internationalization of the company depends on a lot on the entrepreneur. For the founders, it is crucial to understand the target market, its culture, purchasing behavior of the nation, values, and mentality. All these factors are integral components of success, which can be reached best due to the personal researchers and business traveling. Highly important is to find out if the product, which is supposed to enter the new market, meets the needs of potential clients and if it can solve their problems. Personal international experience is the best supporting force for international business as entrepreneur explores the market according to the priorities of his company. Secondary information from various sources can be insufficient or lack some information.

Creation of loyal customer segment can be powerful advantage of doing business across borders and help to overcome some difficult periods. This means that even if the competitor lowers price or have quite similar characteristics of the product, consumer will not switch the brand to which he or she is already used to.

In nowadays-competitive environment, it is highly important to have a comprehensive product, which means not only solutions to customers' problems but also some additional service to a product being sold like warranty, for instance, or post-purchase service that will keep seller in touch with the buyer. This will bring benefits to the company because feedbacks received lead to the further improvement.

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<sup>58</sup> Growth. (2017). SME Internationalization beyond the EU - Growth - European Commission. [online] Available at: [https://ec.europa.eu/growth/smes/access-to-markets/internationalisation\\_en](https://ec.europa.eu/growth/smes/access-to-markets/internationalisation_en).

Due to the introduction of new technology, company can simplify usage of the product and gain competitive advantage. What is more, access to the resources is quite an important factor. There exists a benefit for first movers to choose the location of the resources they prefer and negotiate price.

In fact, a big number of managers has negative attitude to the cross-borders process. That is the effect of the lack of experience and financial resources to the prompt entry of the international arena. Due to such reason, entrepreneurs decide to become stable on the domestic market and only after that enter new market.

Manager's experience, connections, and networks have one of the crucial impacts on the internationalization process. The founder should be familiar with the international market specifics, otherwise, the chance of failure increases. Another essential feature is a distinctiveness from others – niche orientation and more close relations with the potential and existing customers. In addition to that, positive attitude is essential for global start-ups.

The encouragement, readiness to adapt to the changes, flexibility and absence of fear to face risk are the tools that help the entrepreneur on the psychological level. Naturally, the risky decision should be analyzed attentively, taking into consideration unpredictable effects; however, it should be rejected at once the risk is found. There even exist a great proverb: "Nothing ventured – nothing gained!"

Global thinking without borders and doubts, convenience and faith in own strength are increase chances of success. Some people are used to set borders unconsciously, perceiving foreign nations markets too different, thereby limiting personal opportunities.

### **3.1.1 New way to enter foreign market for SMEs.**

The e-commerce market is a powerful force that enables all types of businesses to get faster access to foreign and global market. Consequently, it increases export revenue. The online portal Amazon is the best example of such opportunity. Amazon is an open market space, which helps SMEs to compete with the local brands and companies due to the great customer base. Moreover, the opportunity to compete with the large and well-known brand appears. Available in 12 languages, having subsidiaries in 13 countries, Amazon portal covers 34 types of products. Depending on the agreement, Amazon can provide variety of services, meeting the regulations of the countries; such as marketing, distribution and shipment. What is more, it provides loans for SMEs up to 75 000 USD.

Notwithstanding the fee that is paid for product placement on the Amazon portal, online shopping still is very beneficial and opens doors for the international trade and cooperation for many SMEs. Amazon allows to reach millions of customers all around the world without any special research and adjustment to the market. Such approach saves time of the entrepreneur, money that could be spent on the physical shop and provides quick market entry without any intermediary.

The competition on the portal can be tough but the additional attributes like discounts for the next purchase, shipping and after-purchase service create a noticeable advantage for the company. Today people are used to buy from the Internet due to the ability to compare products, cheaper prices and previous customers' feedbacks, which create even more trust and increase purchases. That is why business internationalization with the help of e-commerce market is aimed to success.

### **3.2 How to contact customer**

The difficulty can appear while searching for the international customer. Direct contact is quite time-consuming and sometimes impossible to realize. As it was mentioned before, there exist some different ways with the use of intermediaries, like joint venture partners, licensing, etc. However, each case is a unique one and depends on a lot of factors: product origin, problems it can solve, nations it matches, its usefulness and others.

Another way is to involve the consulting firms to promote the product on the foreign market. Due to the advertising agencies knowledge of local business environment, law and distribution channels, adaptation and promotion of the product can flow much faster, however, it can be expensive so the appropriate calculations should be made in advance to estimate worthiness.

In order to catch customers' attention and to reach the target audience, the communication tools should be implemented. For instance, personal selling, sales promotion - trade fairs are the best tools for B2B market but can also take place in the B2C market. There exists a possibility to meet potential customers and partners. Moreover, it is a great opportunity to study market and to understand the demand, analyzing and comparing competitors' products. Also, immediate feedback can be received. Due to the face-to-face communication the product characteristics can be described to the consumer in a best way. In addition to that, some catalogs with the more detailed information, brochures, and leaflets are cheap techniques of reaching potential customer.

Being a global company, functioning in a big market is a great advantage for the organizations as their brand is well known and do not need a lot of promotion. Even though, customers are still very different with various requirements. A helpful tool to understand potential clients' motivation is personas creation – ideal customer profile. It will help to understand and clearly define demands of target market as well as if the own supply can meet satisfy customers' wants. The important thing is not to be focused only on broadening the target group but also to keep loyal existing customers. Direct feedbacks with offers and complaints are extremely crucial in order to improve products characteristics, service, and marketing communication tools.

Consumer preferences have a great influence on a market change. The difference of customer's involvement impacts the decision-making process in a company. In today's fast changing society the main issue is to recognize customers' problems and solve them with the product of a company. However, the trial lies in the thing that people sometimes do not know what they want or they are copying from some other people or nations. Consequently, due to the high competition on the market, clients become more and more demanding. Even focusing on a limited target group each client is complex with some different specifics.

### **3.3 The analysis of marketing limitation**

As it was mentioned before a huge attention is paid to marketing that is a vital part of the company success. The entrepreneur should understand the target group that is going to be reached. Through market analysis peoples' interests, habits and preferences should be discovered. Nowadays, the social media provides a great help for marketers, as a lot of feedbacks can be found there. According to the drawbacks and advantages highlighted by users, company can always improve their products and even predict the future demand<sup>59</sup>.

For the effective marketing the analyses consumers' behavior is very important. During the internationalization process the target group can differ from the local one and marketing communication should be adjusted together with the product. The difference can be in language, values, culture, religion, color association, mentality and law. All these factors have a great impact on the internationalization success.

Receiving every day thousands of information people ignore almost all of them. That is why the message that the company is going to deliver should grab attention and be clear. High

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<sup>59</sup> Sitkins Patrick. (2015, July 17) 7 Vital Functions of Marketing For Small Business Prosperity.[online]. Available at: <http://www.business2community.com/small-business/7-vital-functions-of-marketing-for-small-business-prosperity-01275149#HdoE0syuwkGfDzuU.97>



importance is paid to the emotional side as consumers are ready to pay more for emotions than for product itself, furthermore, they should also connect in their mind certain emotion with exact product and brand. Moreover, people should understand what they should do after receiving the message, so "call to action" would be additional motivation and push to buy.

Promotion and selling should be based on the emotions as well. Without the encouragement and visible benefits, it is hard to conquer the public attention and raise the awareness of the brand. Another important aspect is service and after purchase feedbacks as well as customer care. Offering a bit more than everyone else can provide loyalty and future cooperation with customers.

In a chain of similar product categories people are price sensitive and in small business, it is quite an ambiguous function. On the one hand, it is a crucial factor of profitability but a high price on the introduction stage can scare a customer. On the other hand, setting low price will never make a company successful because of the small profit it could be difficult to develop and introduce innovations. Moreover, discounts or actions could be a solution, however, people become used to them and due to that reason they should be frequently changed. That is why assets of the own market opportunities are vital for each company to become successful and reach the maturity stage.

Moreover, loyalty is hard to reach as there are a lot of brand switchers. Companies should work hard to attract attention of clients and hold it off. Also, innovation is the force that rules business market and help business to stay competitive and expand.

In order to reach customer on the local and foreign market usually the following tools are used: public relation, personal selling, advertising and sales promotion. For the SMEs the most suitable are the last two. Advertising can be used with the help TV, billboards, leaflets, radio, internet, posters and others. The more creative the advertisement are the most effective. Sales promotion is used with the help of vouchers, discounts, presents and free samples. Such tool of marketing communication is aimed to increase sales.

#### **Chapter 4. Analyzes and example of business plan for SME.**

According to the higher provided analyses of the countries The Czech Republic is chosen to establish small business. There are several factors that influenced the decision. First of all, it has a beneficial location in Central Europe. Secondly, the cost of establishment of a company is approximately the same as the analyzed countries, however the operation processes is easier and cheaper to perform in the Czech legal environment. Italy has even more favorable environment for creation of a start up there, however, due to hierarchical family businesses, competition would be too strong. In addition, there is a high level of corruption. Germany, in turn, has a complicated red tape procedure and high cost of doing business, which can be a barrier for the company establishment. So the capital of Czech Republic is considered to be the most favorable place for small business.

Following the latest tendencies people are willing to spend money on emotions and to visit as more places as they can. A lot of economies benefit from tourism industry. To start a business in such sector is quite challenging due to the competition present on the market. On the contrary, the demand for service in tourism industry is growing and sector is developing.

There are many tourists in Prague and each year the number is increasing. During the high season, there are still problems to find the short-term accommodation that is why hotel business is an idea, which is aimed at success. Moreover, there are different types of tourists, who have various needs and preferences. Some people would prefer to pay more but require more comfort in turn; others are only care about the price, etc..

##### **4.1 FeelTravel Hotel – is an example of small hotel business in Prague.**

Below the business plan for the micro business is provided.

The mission of FeelTravel Hotel is to create an enjoyable atmosphere for guests, focusing on every individual, to deliver a memorable experience with the affordable price. Vision - to delight the guest with the soulful hospitality of the hotel.

The FeelTravel Hotel is for tourists with a limited budget who are willing to explore new places. It means not only popular and famous sightseeing but also some insight atmosphere and local culture specifics. Focus on service and individual demands. Not just to satisfy the customers but to create a pleasant atmosphere and make them feel more like citizen, not a guest. It is a micro business with a great potential to grow and expand on the local and nearest European markets.

## **4.2 Uniqueness and positioning**

Three-star FeelTavel Hotel in Prague. The hotel will be for people, who are enjoying inspirational traveling. Mostly, such travelers are alone or young couples, who are looking for something unusual. The comfort of the guests will be in the first place as well as their mood. It is going to be a quiet hotel with a twist. FeelTravel Hotel is offering to its guest's living room area, library and info guide on the reception concerning any possible question.

The location is not the center due to the financial reasons, although not far from it. City center can be easily reached in around 20 minutes by subway. The hotel will be done via the reconstruction of the existing building by the address Ke Koulce, Prague 5 – Smichov.

The rooms will be designed for couples – three twin rooms; for those, who travel alone – three single rooms; for a company – one six-bedded room. Altogether the 100% occupancy will accommodate 15 people. FeelTravel Hotel will provide it services 365 days a year. (See Appendixes 4-6)

Price range will be approximately the following: single room: 800 – 1300 CZK, Double room 1300 – 1800 CZK, And room for the group: 2300 – 2800 CZK. The hotel will not serve the breakfast to the guests. However, there are a restaurant and a small shop situated near the FeelTravel Hotel. Moreover, it will be possible to order breakfast for 260 CZK per person. Breakfast for vegetarians and lactose-free could also be available to order. Near the hotel there is no parking available.

Each room will have a shower with toilet, shelves but no TV. On the one hand, people are used to sleep while watching the TV programs or it seems easier for some to relax. On the other hand, foreigners usually cannot understand Czech language and it would be much better to go downstairs and to have a conversation with others. Still, the FeelTravel Hotel will offer free WiFi to the guests as it is important to be in touch with relatives, friends and colleagues.

The main objective of the new business is to reach the annual occupancy 80%. In order to reach the target, the business plan will be created and analyzed to prove that the project deserves to be financed.

The hotel will have some differential features. The stress will be on the enjoyment and infusion into the Prague atmosphere. Such idea is easy to implement due to the little number of rooms. Consequently, it will be enough time to pay attention to each guest and to meet their requests.

The hotel will not only provide accommodation, it will become an essential and remarkable part of the travelers' memories. Therefore guests should not expect something extraordinary because it will not follow any popular youth currents. As it was said before the hotel will be focused on the intangible aspects more.

In addition to that, to attract the attention of the potential guests, rooms will be colored with the different colors and the interior will slightly vary in the rooms. The style will be close to modern with some possible variances to art. Moreover, there will be a mutual living room for guests to get acquainted with each other and to share the emotions.

There will be also created a web page, for guests to make a reservation, look at photos and read feedbacks from previous visitors. Indeed, all the necessary facts about the hotel, services, location, contacts and prices will be there. To be on the same wavelength with the modern trends FeelTravel Hotel will have an account in the Instagram and Facebook so that people could be informed about the hotel day-to-day work and check updates. This is going to be kind of unconscious influence on the customer's awareness.

#### **4.3 Customer analyses**

Overall, the hotel guests can be divided into the four main groups: families, business travelers, seniors and backpackers. Based on such typology FeelTravel Hotels' guests will be mostly from the last group, however, there is some refinement as backpacker type is considered to be more sensitive to prices and less caring about the hotel itself. Therefore in such group of travelers, there are some people, who are still interested in a comfortable place, which is authentic and not banal. That will be our target group. In addition to that, due to the quiet area and private rooms, hotel can suit for families too. To be more concrete it is better to create a persona.

Persona - Mark is a 21-year-old student in Moscow Art Theater School. He has a girlfriend and few best friends. He is the oldest child in a family, having a younger brother.

His goals are to become a great actor and to work in theater Sovremennik. Also, he would like to meet the famous and professional actors such as Robert De Niro, Morgan Freeman, Jenifer Lawrence and Matthew McConaughey. He dreams to have a chance to speak with them a bit to understand what is the most important in his profession and to adopt the experience. That would become more realistic if Mark will travel and visit some Film Festivals.

In Russia Mark works in a modern theater and sometimes it is difficult for him to combine work and studies. Marks' hobbies are playing guitar and traveling to explore new cities and cultures.

This boy is afraid to live life like his parents, being bound by finances and limit his wants. Mark is going to do everything to be able to live and not just exist, waiting for a wage.

His motivation is to meet his idols! Moreover, to have the personal opinion about the countries due to the individual experience while traveling. Also, he is going to try to be the street musician in some places abroad. Mark does not have a lot of money and would not stay in luxury hotel while traveling, he prefers to stay alone in the room and tries to find each time some unusual places to be inspired by them as well. For Mark, there is the opportunity to meet creative people and to get some new visions of the life.

#### **4.4 Industry analysis**

Nowadays hotel industry became extremely popular especially in such international cities as Prague. Consequently, more attention is paid to the client satisfaction: loyalty programs, atmosphere and individual guest preferences. These factors are stressed to be able to compete with other similar service providers.

In hotel industry, there are hot seasons, when almost all hotels and hostels are 100% occupied and on the contrary, after the New Year, there is a dead season, when each business suffers from the lack of customers. Usually, on Christmas, almost all money is spent on gifts and people need time to save money for their vacations. Moreover, everyone would like to have a holiday when there is a good weather outside. That is why the end of spring, summer, beginning of autumn and state holidays are considered to be the hot days for hotel business in Prague.

There are nearly 2880 hotels in Prague with around 30 hotels in the area Prague 5 according to booking.com<sup>60</sup> The competition among three-star hotels is quite tough and clients demand the high level of service.

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<sup>60</sup> Booking.com (2017) [online] Available at <http://www.booking.com/city/cz/prague.ru>.

## **4.5 Competitive analysis**

### **4.5.1 SWOT**

#### **Strengths**

Although it is not going to be a new building, it will be totally reconstructed. The outside design will differ a bit from the neighbor buildings, and bigger windows will be done so that more natural light would be inside. The mutual living room will increase the interest in the hotel as there will be a place to have a conversation with the people of various nationalities. Moreover, a library will be provided.

To have more fun and get on with each other guests will be able to play some table games like Alias or Activity for free. Also, coffee or tea will be offered each morning as the gesture of hospitality. FeelTravel Hotel will be situated near the metro station, so there will be no problem to get to the center. In addition to that Ke Koulce is a small street not far from the river. The street is also quiet as windows are not directed to the main street.

What is beneficial for customers is the price, which will be similar to the average three-star hotel or even hostel price. WiFi will be free as well as the possibility to print something on the reception.

#### **Weaknesses**

On the contrary to the previous paragraph, due to the fact that the old building is going to be used, no noticeable features will be outside to grab attention and to create competitive advantage.

Unfortunately, there is no parking space, only in front of the building (for two cars maximum). As the hotel is focused a lot on feelings of the customer it will not be very suitable for business travelers.

Near the hotel there are no shopping centers or supermarkets, however, there is a shop Žabka, which can satisfy the urgent needs of the clients.

#### **Opportunities**

There exists a great opportunity to build a chain of the hotels after the successful functioning of the first one, which will allow to earn much more and increase turnover. The inner courtyard of the hotel can be purchased for parking space in future. The cooperation with some restaurants can be established to give customers discounts for dinners and lunches.

Creation of Facebook group and Instagram page with the frequent updates as well as some outdoor marketing communication will increase the interest of the hotel among the potential clients.

## **Threats**

Due to the fact that the hotel is new and not big it could be hard to attract customers and there exists a threat of a small occupancy. The most unfavorable situation is lack of customers due to the existing competition. (See Appendix 8)

The high capital cost can be dangerous for the small business.

### **4.5.2 Porter 5 Forces analysis**

#### **1. Customer power**

According to the report of Prague City Tourism, the most frequent guest of the Czech Republic capital are coming for the private trips not business ones. Many tourists visit Prague for the first time, around 87% are foreign and the rest are Czech. Also, the most common visitor arrival countries are Germany, the USA and UK.

Taking into consideration the nationality according to the statistical report, the most frequent visitors of Czech Republic and particularly Prague are people from the nearest countries like Germany, Slovakia and Poland; also Russian Federation, USA and others. (See Appendix 7). Because of the latest changes in cooperation with the EU with Ukraine, the visa-free regime starts from 11.06.2017. That means that a big inflow of Ukrainian tourists is expected in 2017.

Apart from the travel tickets, accommodation is the most expensive part of the trip.<sup>61</sup> The hotel will offer flexible prices, which will depend on the season and occupancy. This feature will be also attractive to the guests as the target group is price sensitive.

Customers are powerful in the tourism area and due to the high service supply, competition in the industry increases. Only during the high season, when almost every hotel has 100 % occupancy customer power is decreasing.

#### **2. Supplier**

It is not a problem to find a supplier for any aspects of the hotel business. As a result, their power is considered to be moderate.

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<sup>61</sup> Annual Report Pražská informační služba (2015) – Prague City Tourism [online]. Available at: <http://www.praguecitytourism.cz>

### **3. Threat of substitutes**

In a role of substitute can figure couch surfing that last days becomes more and more popular. Especially among young people this type of accommodation is famous, although not very safe. The biggest benefit is the free stay and possibility to meet new interesting people. But again it depends on a lot of the personality of the host and guest. Another cheap offer can be from the dormitories or hostels, which are not so safe also. However, the creative hotels are not very popular, there are much more coffees or restaurants in such sector.

### **4. Threat of new entrants**

A strong competition exists on the market, however, it depends on the size of the hotel as well. For example for big three-star hotels, the entry can be very costly, considering marketing strategy and legal issues fulfillment. Also, the building cannot be used for any other purpose without reconstruction on the chance of failure. Nowadays, each market player tries to find a niche in service provision to create competitive advantage and to satisfy customers' requirements. Therefore it is a difficult task to invent something new and unique, moreover, for the limited budget, some services are not affordable.

#### **4.5.3 Rivalry in the Industry**

As it was mentioned before there are around 2880 hotels in Prague and nearly 685 three-star hotels. In the near area, there are approximately 35 hotels (in Prague 5). Due to the fact that there are many hotels available as, analysis from one source can seem quite subjective. There will be examined three famous booking sites and their ratings, namely: Expedia, Booking.com and TripAdvisor.

There is no fixed rating for the hotels and even top three from each category regularly change their position. Also, there are a lot of other types of accommodation provided as residences or hostels. As a result, one hotel from each category was chosen for more detailed analysis.



Table 2. Rating of the three-star hotels in Prague 31.03.2017

	Expedia	Booking.com	TripAdvisor
Price	<b>A&amp;O Hotel,</b> Hotel Amadeus, Hotel Mira	Czech Inn Hotel, Hostel Lipa, Hotel Sary Pivovar	Hotel Sary Pivovar, Andel, Hotel Golf
Guest rating	<b>Remember Residence,</b> Hotel Pavilon, Smaragd, Hotel Bella	Loreta Hotel, Hotel Excellent, Hotel U Svateho Jana	Aparthotel City 5, Hotel Golf, Akcent
Center location	Central Hotel Prague, Hotel Dar, Hotel Melantrich	U Tri Bubnu, Hotel Dar, Hotel Melantrich	<b>Aparthotel City 5,</b> Botel Admiral, Hotel Anette

**1). Remember Residence** is a modern type of accommodation – fully equipped apartment with the kitchen, which also can provide hotel service – reception, daily cleaning, assistance etc. It is situated near the Charles Bridge in the vicinity of Kampa Park. There are 14 apartments with the original design. No mutual room like a living room or conference room. Most frequent guests are families and business clients. The hotel offers free coffee each morning for the guests and is focused a lot on the comfort of the clients. Moreover, the hotel offers a bonus for those, who are going to stay more than three nights – free transfer from the airport. Parking for the guests is near the Residence.

Rooms available are Luxury apartment, Comfort apartment, luxury apartment with one bedroom, Deluxe apartment with maximum five people in the room.

Prices are charged depending on the number of people accommodated, from 3645 – 4725 Kc per night. Breakfast is 190 Kc, which is not served directly in the residence, but in the near coffeehouse. According to the information provided by the receptionist Marketa Mansfeldova, the team is quite small five- ten people and residence is cooperating with the HR agency, which provides workers for them. <sup>62</sup>

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<sup>62</sup> Remember Residence home web page (2017). [Online]. Available at: <http://www.remember-residence.cz/en/>

Remember Residence is the strong competitor in the idea of hotel design. Moreover, their location is also in Prague 5, even closer to the center and the idea is very similar to the FeelTravel Hotel. On the contrary, the residence is more oriented on the category from higher than average social class representatives with a bit different demand.

**2). A&O Hotel Hostel (Prague 8)** is a German hotel chain, which has its branches in Holland, Austria, Italy and is going to enter more foreign markets. The types of rooms that are available in the hotel: Single, Twin, four-bedded family room and six-bedded family room. For hostel part, there are four-bedded and six-bedded rooms. Altogether there are available 358 rooms. The price is charged per room - in the hotel and per person - in the hostel. The average price in a Twin room is about 1500 Kc, including breakfast. In addition to that, A&O Hotel offers the conference room, terrace, laundry and dryer services, game zone (karaoke, billiard and small tennis) and 24/7 bar, although no secure parking.

According to the information from the Front Office Manager (Jiří Kládivo), there are many part-time workers on the position of receptionist, a kitchen worker and utility staff. Housekeeping is from the outsource company and only managers are in the full-time position.

This hotel is created for different types of customers such as business travelers, families, groups and young category of travelers. The average occupancy during the whole year is 60-65%.<sup>63</sup>

The hotel/hostel is a strong competitor in price for FeelTravel Hotel. However it is situated far from the center. Moreover, all A&O Hotels Hostels are standardized and due to the big number of rooms and bar it is difficult for them to pay much time for each guest.

### **3). Aparthotel City 5**

The hotel is also located in Prague 5. The accommodation can be provided from two to six guests per room. In each apartment, there is a kitchen corner and a fridge. Moreover, the hotel suits for families and has a special kid's zone as well. Parking is guarded 24 hours and costs 150 Kc per day. Additionally, laundry is provided. Breakfast costs around 100 Kc and café bar is open from 8:30 till 21:00.

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<sup>63</sup>A&O Hotel Hostels (2017) home web page [online]. Available at: <https://www.aohostels.com/cz/prag/>

Prices for accommodation vary from 1728 to 5130 Kc, depending on the season and the room. Types of the room are the following: Studio - for 2 people, Apartment for 2 – 4 persons, Apartment for 4 – 6 persons.

The hotel is a competitor in a comfort. It provides more facilities to the guests like kitchen corner and parking. Due to the apartments provided by the Aparthotel, guests can feel themselves almost like at home, not in a hotel; which is the idea of FeelTravel Hotel. Although, it is a bit more expensive and suits more for the family type of guests.

There is a great example, of a hotel/hostel with a similar idea as FeelTravel Hotel. It is a hostel **Lavender Circus** in Budapest. It was shown in one of the Ukrainian TV shows "Orel and Reshka" and became very popular. Due to its extraordinary and authentic design and comparatively low prices, it is almost always full and as a consequence profitable. There are two-floor rooms with a lot of details of the interior, walls painted with different pictures, which creates a cozy home atmosphere.

All in all, the competition is quite tough but depends a lot on the preferences of customers and their budget. During the search for the accommodation in a certain destination people are considering not only prices, location and facilities provided but also they are paying a lot of attention to the feedbacks from previous visitors. Due to this reason, more and more forces are directed to the service and customer satisfaction. Nowadays it is extremely important to have positive and motivated workforce so that they could deliver a good feeling and create a nice image of the hotel. Professionals are required everywhere even on the reception and for utility workers. Fluent languages, quick reaction and readiness to help as well as responsibility and reliability are the crucial features of each employee.

#### **4.6 Marketing plan**

Promotion is the driving force on the way to the success of this small business. The perfect scenario is when people know the brand and have it on the top of their mind. However, for the emerging business, it is not an easy task.

The thing is that there are already many competitors on the market, moreover, people are usually ignoring a lot of advertisings as there is a huge amount of information each brand wants to deliver to the customer. As a result, the communication campaign should grab attention, be memorable and informative, and motivate people to stay in FeelTravel Hotel.

The first step that can help in campaign creation is situation analysis. SWOT, competitor and environment analysis were made before in this thesis that created a better understanding of the position of FeelTravel Hotel. The main idea is to create a modern type of hotel, which is focused a lot on the comfortable physical and moral stay of the customers. To be competitive FeelTravel Hotel will be inspirational with the creative and sociable receptionists. The main target audience is people, who are keen on traveling and not focused on luxury, although on the atmosphere.

#### **4.6.1 Marketing communication**

The goal of the business is not only to enter the market but also to become profitable and recognizable among the customers. The target of the marketing communication itself is to increase the awareness of the potential customers, to raise a number of sales and to influence the perceptions of the visitors, to create strong brand.

Message strategy should be in line with the target group, reinforced by uniqueness and emotional message. A creative idea is a thing, which supports such strategy. It could be something showing the solution of the customers' problems – like lack of the big budget or need of the interesting authentic accommodation. Storytelling communication – about the created persona or customer's experience. Some opinion leaders could also be used and participation in some TV programs will definitely increase the interest of the potential visitors.

Concerning the media, it should be the combination of various outdoor types: billboards and ambient media that would be the best solution as it is not expensive and creative, which attracts attention. Billboards will appear in one month before opening with the invitation for visit. The opening day is supposed to be 1<sup>st</sup> of May and a small buffet table will be organized not only for guests but also for Prague citizens who will come. Such billboards will be on the highway to the airport and on the main train and bus station – Hlavní nádraží and Florenc. Ambient media is going to be used in the center mostly in Prague 1 with the use of benches, public toilets, public transport stations, so that even citizens would be aware of the hotel, to make recommendations to their friends and relatives. Ambient advertising can appear two months in advance.

Also, the hotel will have to advertise on the Internet so that people would be familiar with the name of the brand. A special attention will be paid to the social networks such as Facebook and Instagram to develop the brand name, to answer all the questions, show updates and receive feedbacks to in order to improve service. Also, the advertising on the online travel agencies (OTAs) is crucial as nowadays people are planning their trips via the Internet and use the most

popular websites together with the analysis of the feedbacks. The goal is to be in list of top 20 Small Hotels in TripAdvisor, one of the first hotel according to the price – service ratio on Airbnb, Booking.com and Expedia. On the entry stage and much more money will be spent to increase awareness. For the future, connections with travel agencies will be set up. For instance, Mary's Travel & Tourist Services, Prague International Travel Agency or Prague Gay Travel Agency. No TV advertising will be used as the hotel is focused more on the international auditory. Moreover, even Czech people are not influenced by the TV advertisements.

According to the SBA in the USA the recommended percentage of revenue spent on marketing is about 7%. As for the startup and SMEs, this number can vary from 3% to 20% depending on the industry. The more competitive industry the bigger budget should be spent on marketing.<sup>64</sup> The budget spendings on marketing are shown in a financial plan part.

Highly important is the feedback monitoring and checking not only the positioning on the FeelTravel Hotel but as well competitors. In the beginning, it would be great to ask each guest to leave their feedback to understand in more details what are the expectations and wants of the customers, in order to implement changes on the first stage to gain better effectiveness.<sup>65</sup>

Also, it should be taken into account that people tend to rely on the advice of their families and friends concerning many issues during the trip. Additionally, the Internet feedbacks are very influential power on the potential customer's decision nowadays, for instance Airbnb, Trip Advisor, bookink.com, and others.

#### **4.7 Distribution channels**

The main channels through which the rooms in a hotel are going to be sold are web pages like Booking.com, Own FeelTravel Hotel's page, Expedia.com, Agoda, Hostel.com and most important new trend is Airbnb. These channels are popular among travelers and give them more opportunities to find the most suitable hotel according to their demands, check feedbacks from previous visitors. In addition, travel agencies and tourist offices could be used as a distribution channel, although these types will be less popular due to the limited occupancy of the hotel.

For this advantages for customers, businesses should pay commission up to 15%. The effective rate of booking can be calculated so that to decide if it makes sense to use the mentioned

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<sup>64</sup> George Boykin. What Percentage of Gross Revenue Should Be Used for Marketing & Advertising? [Online]. Available at: <http://smallbusiness.chron.com/percentage-gross-revenue-should-used-marketing-advertising-55928.html>

<sup>65</sup> Lectures of Ing. Petr Král, Ph.D. – International Management 2016

channels. For instance, these OTAs definitely increase the level of sales. But taking into consideration the size of FeelTravel Hotel, after infant stage of the lifecycle there will be possible to reduce some of OTAs as people will be aware of the brand and will be able to make booking via FeelTravel Hotel's web page, which will decrease the costs of OTAs service and reduce overbooking in turn. Moreover, it will be even better to use discounts rather than pay commission to the OTAs.

As it was already mentioned the web page will be adapted for the mobile devices so that customers could make bookings directly without any troubles. Still, some advertising on the OTAs page, forwarding to the home page of FeelTravel Hotel will be always beneficial.<sup>66</sup>

#### **4.8 Revenue management**

Due to the right management and market review revenue of the business can increase or stabilize income during high and low periods respectively. The prediction of booked rooms, terms and demand can also be a tool in price setting. Such efforts will help to avoid overbookings by setting higher prices in hot periods and decrease in low ones. Taking into consideration that customer behavior is quite unpredictable the analysis of the trends in the whole industry and similar hotels will help to plan the sales. In the Czech Republic, the net occupancy of bed in a hotel with less than 25 rooms is 22,7%. (See Appendix 9). This index is calculated for the whole country and for Prague this figure is higher.

According to the previous description, the dynamic pricing will be used along with the on-line prepayments. Such action will secure hotel from the no show expenditures at least partly. The reason for that is the fact that sometimes guests are not informing the hotel about the cancellation of the reservation, which eliminates chances for new customers to book the room. Cancellation of the reservation three days before arrival will be for free, however, two and one days will be done with the fee.

#### **4.9 Operations plan and management team**

It is going to be a micro business with one manager, leading the hotel. Manager will combine the positions of accountant, sales manager and partly marketing department. The ambition is to enlarge the hotel and to have the chain in some neighbor tourist destinations. For the employees, there are going to be benefits as well to motivate people for work, such as free soft drinks, and

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<sup>66</sup> Alex Gaggioli (2015, July 30) Creating a Profitable Hotel Distribution Strategy [online]. Available at: <https://www.cloudbeds.com/articles/creating-a-profitable-hotel-distribution-strategy/>

premiums in case of good feedbacks from the guests. There will be also frequent staff meetings to discuss new ideas and express views of each employee as well as to have fun together to make close-knit collective.

As it was already discussed it will not be easy to combine all the managerial responsibilities, although such small business cannot afford more staff to be employed because of the budget limitation. Considering this fact, marketing specialists can be hired for some short period of time. Such strategy will work well on the stage of growth and for the beginning, secondary data will be used.

The top manager has the Master International Business and experience in accounting. In addition to that, experience of working in a hotel chain for four years on the position of Front office manager. Such background and experience will be supportive tools while creating the new company.

Overall, for the staff the hotel will need up to five receptionists, two housekeepers, one utility manager plus top manager.

Receptionists are going to have one shift per day from 7:00 till 19:00. It goes without saying, that it is always better to have staff with the experience but for the receptionist, work training is quite fast so student without experience will be also accepted. Moreover, there will be manuals for each shift, with the main tasks they should do as well as the description of some problematic situation and instruction for solutions. Housekeeping and utility manager will be from the outsourcing company. Housekeeping is going to work only morning shifts. All the necessary staff for housekeeping will be changed and renewed according to the occupancy. Also, as the hotel is not providing breakfasts, it will not be the responsibility of the receptionists to order a breakfast for the guest if needed. There are some practices for cooperation with the nearest restaurants or early daily delivery of croissants, muffins and sandwiches, that FeelTravel Hotel will develop as well.

#### **4.10 Financial plan**

Highly important part of the business plan and very responsible one is financing. To acquire start-up financial resources the hotel can use the loan from the bank. Czech bank CSOB is ready to issue loan for SME up to 8 million CZK with the maturity 15 years. Also there is a possibility to take a loan for the mortgage with the interest rate approximately 14,75%. The entrepreneur decided to buy a building and is going to take mortgage for 8 000 000 CZK for 20 years. Such

decision is influenced by two reasons. First of all, the entrepreneur is going to be on the market for a long time and would like to have a property, not to lose money with the rent payments. The purchase of the building will also certify the investor in serious intentions of the entrepreneur. Secondly, property is always beneficial as in case of failure it can be sold.

The second part will be equity financing, which will amount around 7 000 000 CZK. That is the capital from the business angel investor. According to the Czech Republic Angel Investors Association there are 2863 investors only in Prague. For instance: Jaroslav Trojan, Andrej Kiska or Daniel Jones.<sup>67</sup> Of course, they should not be from Prague and there is a possibility to find business angels from around the world, although because of the micro business we are going to start with it will be easier to reach to the person, to meet personally and discuss the investment issues. The sum needed is estimated by the calculations in the following table.

#### 4.10.1 Calculation of expenses

In order to understand the needed sum of the investment the establishment expenses will be calculated.

Table 3. Calculation of the main expenditures for the business establishment.

Capital investments	
Building	
- Purchase	13 500 000 CZK (see Appendix 10)
- Reconstruction	65 000 CZK per room = 455 000 CZK 250 000 CZK - lobby together with the staff room 30 000 CZK – painting of building side
Electronic equipment*	
- Computer, monitor, printer	100 000 CZK
- Cash register	
- Cameras	
- Telephone	
- Safe	
- Wifi modem	

<sup>67</sup> Czech Republic Angel Investors [online]. Available at: <https://angel.co/czech-republic/investors>



- Fire system	
- Coffee machine	
Furniture	
- Beds, sofa, tables, wardrobes, chairs, bathroom staff**	35 000 CZK per room = 245 000 CZK 250 000 CZK - lobby
Web-page creation	45 000 CZK
Overheads	20 000 CZK
Cost of business registration	14 500 CZK
Pre-opening expenses***	10 000 CZK
<b>Total</b>	<b>14 919 500 CZK</b>

\*The prices for the electronic equipmetn are based upon the current market prices.

- Computer – 22 000 CZK;
- Monitor – 6 000 CZK;
- Printer – 5 500 CZK;
- Cash register – 1 700 CZK;
- Cameras – 6 000 CZK;
- Telephone – 700 CZK;
- Safe – 3 500 CZK;
- Wifi modem – 1 500 CZK;
- Fire system – 30 000 CZK;
- Coffee machine – 23 000 CZK.

Together 99 200 CZK – approximately 100 000 CZK. The equipment will be switched on almost all the time and for this reason the quality should be high. Consequently, the prices of the electronic equipment are not the lowest but average on the market.

(Source Alza.cz)

\*\*The prices for furniture are also based on the current market prices.

- Bed – 15 000 CZK;
- Table – 1 000 CZK;
- Wardrobe – 3 000 CZK;

- Chair – 350 CZK;
- Shower – 5 000 CZK;
- Toilet – 3 000 CZK;
- Decor – 5 000 CZK.

(Sources Kika, Ikea)

The price of the furniture depends on the room type. The decoration is supposed to be expensive due to the idea of the hotel to differentiate each room from each other.

**\*\*Pre-opening expenses** are made as a reserve in case of unpredictable situation that can cause problems of the hotel functioning

Also the operating costs will show companies' expenses during its functioning. Operating costs consist of fixed and variable costs. Fixed costs are the expenses of the hotel that do not depend from the occupancy and season. For example: mortgage, utilities, salary, administrative expenses and taxes. Variable costs are associated with the fluctuation of expenses depending on the sales volume. These costs usually consist of room expenses, utilities, salaries of cleaning staff and utility manager, marketing expenses. In addition to that, some costs are mixed and names semi-variable. For instance, there can be no guests in a hotel, although it will still use electricity, heating and water. But when the occupancy is high, the utilities usage increases and utilities become variable costs. For deeper understanding the operating expenses assumption is provided.

Table 4. Assumption of the operating and non-operating expenses.

<b>Monthly operating expenses</b>	
Sales promotion	
- Via OTAs, billboards and ambient media	10 000 CZK
Utilities per month	
- Water	8,54 CZK, 0,1 m <sup>3</sup> per person per day, cost of 1 m <sup>3</sup> is 85,42 CZK <sup>68</sup> ⇒ 3 300 CZK per month

<sup>68</sup> Pražské vodovody a kanalizace (2017) [online]. Available at: <http://www.pvk.cz/vse-o-vode/cena-vodneho-a-stocneho/>

- Electricity	22,26 CZK 6 kWh per person per day <sup>69</sup> Cost of 1 kWh in Prague is 3,71 CZK <sup>70</sup>  ⇒ 8 500 CZK per month
- Heating	25 885 CZK per year (6977 kWh per year)  ⇒ 2 157 CZK per month
Total utilities for the whole hotel per month (incl. lobby)	15 000 CZK
Payroll per month*	
- Manager	15 000 CZK + provisions
- Receptionist	32 400 CZK, 90 CZK per hour
- Housekeeping	10 800 CZK, 3 hours per day, 120 CZK per hour
- Utility manager	4 000 CZK, needed once per week
Hotel stuff (toilet paper, shampoo, cleaning stuff, stationery etc.)	7 000 CZK
<b>Total operating expenses</b>	<b>94 200 CZK</b>
<b>Monthly non-operating expenses</b>	
Taxes	
- VAT**	15% <sup>71</sup> (34 249 CZK)
- Property tax <sup>72</sup> ***	1 220,4 CZK
Mortgage	59 000 CZK
<b>Total non-operating expenses</b>	<b>94 469 CZK</b>
<b>Total assumed expenses</b>	<b>188 669 CZK</b>

\*The intention is to employ 5 receptionists, who will earn not more than 10 000 CZK each. In addition to that, housekeeping and utility manager will be provided by the outsourcing

<sup>69</sup> Electric power consumption(kWh) per capita (2014). The World Bank [online]. Available at: <http://data.worldbank.org/indicator/EG.USE.ELEC.KH.PC?end=2014&start=1960>

<sup>70</sup> Energie 123.cz [online]. Available at: <http://www.energie123.cz/elektrina/ceny-elektricke-energie/cena-1-kwh/>

<sup>71</sup> Doing Business Czech Republic. The world Bank [online]. Available at: <http://www.doingbusiness.org/data/exploreeconomies/czech-republic/paying-taxes/>  
The reduced rate of 15 % for services such as accommodation according to the Check law

<sup>72</sup> Karel Englis, Property Taxation in the Czech Republic (2009 June 02)  
<https://www.expats.cz/prague/article/real-estate/czech-property-tax/>

company, which will pay social and health insurance for the employees. In such way the hotel will decrease payroll expenses by around 37%.

\*\*If the company's annual turnover exceeds 1 million CZK it should be registered for VAT.

\*\*\*Property tax (building) period is a calendar year. It is counted in accordance with the property size:  $290 \text{ sq.m.} * 5$  (coefficient for Prague estate)  $* 10$  (coefficient for business premises)  $+ 0,75 * 96,6 \text{ sq.m.} * 2$  (coefficient for each floor above ground floor) = 14644,9 CZK.

Building tax per month = 1220,4 CZK

In addition to the mentioned taxes, there is also a tourist tax, which is 15 – 30 CZK per person per day. Some hotels charge guests while check – in, other include the tax amount in the price. In the FeelTravel Hotel the travel tax is included in the price.

Table 5. Summary of the operating expenses

Fixed cost	
- mortgage	59 000 CZK
- utilities	5 000 CZK
- salary	47 400 CZK
- taxes	35 469 CZK
Total	146 869 CZK
Variable costs	
- marketing	10 000 CZK
- utilities	10 000 CZK
- salaries	14 800 CZK
- hotel stuff	7 000 CZK
Total	41 800 CZK

#### 4.10.2 Profitability calculation

For the income and profit calculation prediction of the occupancy is important in order to realize the volume of sales during the month and average per year.

As it was already mentioned the frequency of guests visits vary according to the tourist season.

Occupancy rate in:

- low season = 28% - 2 rooms;
- high season = 86% - 6 rooms;
- average annual occupancy is 4 rooms per day.

Table 6. Monthly revenue per room

	Price of room low season, CZK, per day	Price of room high season, CZK, per day
Single	800	1300
Twin	1300	1800
Family/Company	2300	2800
<b>Total per day for 7 rooms</b>	<b>8 600</b>	<b>12 100</b>
Occupancy rate	28% (2 rooms)	86% (6 rooms)
Total per day	2 408	10 460
<b>Per month</b>	<b>72 240</b>	<b>312 180</b>

According to the assumption there are the following business seasons in a year:

- High - May, June, July, August, September
- Low – February, March
- Medium – April, December, October, November, January

Table 7. Sales, depending on the season.

Season	Sales per season, CZK
High	1 560 900
Medium	961 050
Low	144 480
<b>Total per year</b>	<b>2 666 430</b>

- ❖ High season sales => 312 180 (Monthly sales during high season)\*5 (number of months in high season) = 1 560 900 CZK.

- ❖ The calculation of the medium season sales is based on the average price of the room  $(312\ 180 + 72\ 240) / 2 = 192\ 210$ , and multiplied by 5 months of the medium business season.  $192\ 210 * 5 = 961\ 050$  CZK.
- ❖ Low season  $\Rightarrow 72\ 240$  (Monthly sales during low season) \* 2 (number of months in low season) = 144 480 CZK.

Investors need to understand the ability of a business to generate income. Such process can be identified with the help of net operating income per month (**NOI**) = Revenue – Operating expenses.

$$\text{NOI} = 2\ 666\ 430 / 12 - 94\ 200 = 128\ 002 \text{ CZK (1 536 024 CZK per year)}$$

Another important index for investors to realize the profitability of the company is net operating profit after taxes (**NOPAT**) = NOI – Non-operating expenses

$$\text{NOPAT} = 128\ 002 - 94\ 469 = 33\ 533 \text{ CZK (402 396 CZK per year)}$$

#### 4.10.3 Break-even analyses and effectiveness calculation

One of the crucial indexes for the investor is the break-even point that shows the point, when the business becomes profitable. This index influences the investor's decision about the investment into the company.

a) Table 8. Break-even analyses of FeelTravel Hotel.

Number of rooms	7	Required total revenue	3 623 680 CZK
Development cost per room	65 000 CZK	Assumed rooms revenue	71,4%
Total development cost	14 919 500 CZK	Required rooms revenue(RRR)	2 587 307 CZK
Loan to coast ratio	53%	<b>Required revenue per room per day (RRR/365/7)</b>	1 013 CZK
Loan Financing	8 000 000 CZK		
Equity financing	7 000 000 CZK		
Interest rate	14,75%		
Interest payment	1 180 000 CZK		

<b>Operating expenses</b>	
Fixed cost	1 762 428 CZK
Interest expence	1 180 000 CZK
Variable cost	18,8%
<b>Break-even revenue</b>	3 623 680 CZK
$(1816800+1180000)/(100\% - 18,8\%)$	

In the calculation the variable cost is mentioned. It amounts 41 800 CZK per month and 501 600 CZK per year in turn. Variable cost amounts 18,8% of total revenue.

According to the data provided<sup>6</sup> the FeelTravel Hotel requires 3 623 680 CZK revenue to be able to meet the obligations. From such break-even revenue point the hotel starts to be profitable. This indicator helps entrepreneurs to analyze influence of cost and price changes on the profitability. Moreover, as it is seen from the example, due to the loan obligation the break-even revenue point period delays.

Required revenue per room = 1 013 CZK. As it is shows in table 6, the average price of the room in FeelTravel Hotel for low and high season is 1 467 CZK and 1 967 CZK relatively. So the hotel meets these requirements.

- b) To realize the effectiveness of the company and its profitability, the return on invested capital (**ROIC**) calculation will be done. It shows if the company generates value per unit of capital invested.

$$\text{ROIC} = \text{NOPAT} / (\text{Debt} + \text{Equity}) = 402\,396 / (8\,000\,000 + 7\,000\,000) = 2,68\% \text{ (Every 1 CZK invested generates 2,68\% of profit.)}$$

Usually business that generates around 15% ROIC after the first year has good chances to get investor. However, the problem of such a low index is that the entrepreneur decided to buy the building, not to rent it. Such decision greatly increased cost and reduced the possibility to generate more profits from the invested capital.

- c) Based on the previous calculation there is also a possibility to identify the average daily rate (**ADR**). The indicator shows the possibility to maximize revenue during high season and manage hotel operation during the low season. Moreover, ADR shows the level of hotel performance among the competitors.

ADR = Revenue earned from rooms sale/ Sold rooms

- 1) ADR per low season =  $72240 / 60 = 1204$  CZK
- 2) ADR per high season =  $312\ 180 / 180 = 1734$  CZK

The shown average charges per room are even a bit lower than the prices settled. Moreover, after the successful functioning and development it will be possible to increase the prices, charged per room.

#### **4.11 Summary of business plan<sup>73</sup>**

1. Location – 20 minutes from the city center, quiet street with the restaurants and shops close to the hotel, close to the river Vltava.

2. Target group – backpackers, price-sensitive tourists, people who are interested in the authentic type of accommodation and inspiring environment, some families.

3. Mandatory procedures and business permits – Czech government provides support in doing business via consultations and SMEs support programs. For such micro business, in the beginning, the business will not ask for help. However, after some time, when company will expand and go internationally certain support from EGAP will be important.

The first step is to get a license from the Trade Office. What else should be done – is business registration in Trade and Commercial Register. It takes around five days for the Trade Licensing Office for Trade Register and in Municipal Court in Prague with the fee for 6000 CZK for the first registration for Commercial Register. What is next is the registration for taxes within 15 days after entering of Commercial Register. For some consultations about these processes, there are such organizations as SOLVIT and Enterprise Europe Network that are ready to help.<sup>74</sup>

4. Hotel building – reconstruction of the existing building in a more modern style inside with the bigger windows size. Some rooms need additional bathrooms and toilets. Also, a lot of furniture and electronic equipment should be. The main reconstruction will be on the ground floor for the lobby and reception. Moreover, due to the planned unusual design, the artists will work for painting walls in a different manner.

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<sup>73</sup> All the assumptions are based on the interview with the Front Office Manager of A&O Hotel Hostel Strizkov Prague – Jiří Kladivo (Jiri.Kladivo@aohostels.com).

<sup>74</sup> BusinessInfo.cz (2017) Licences and permits, rules and regulation schemes. [online]. Available at: <http://www.businessinfo.cz/en/psc/start-your-business/licences-and-permits-rules-and-regulation-schemesrequirements-for-cross-border-provision-.html>



5. Type of financing: 8 000 000 CZK – bank loan, 7 000 000 – investments from business angel.

6. Staff and Training. There will not be a big problem to find receptionists. The labor market in Prague offers 90 CZK per hour on average for the part-time worker. Moreover, Prague is full of students, who are usually interested in part-time job. For the housekeeping and utility manager the outsourcing company help will be required. The trainings for the receptionist will last for two days staff meetings once in two months.

7. Opening - the best time is the end of the spring when the high season begins. The approximate date – May 1<sup>st</sup>.

8. Break-even point. To pay off to the investor it will take more time for the business as entrepreneur decided to buy the building. With the rent it would take around 3 – 4 years. In the given case yearly  $3\,623\,680 / 402\,396 = 9$  years. The period is so long due to high cost of the building purchase. The FeelTravel Hotel should work hard to stay on the market and survive difficult periods not to become bankrupt as many small and micro businesses.

9. Extra services – transportation to/from airport; breakfast order; help to find the places to visit, tours, restaurants, other trips, etc.

10. OTAs – Airbnb, Expedia, Hostel.com, Agoda and Booking.com,

11. Cooperation with local restaurant and city tours allows to attract more customers and earn more money.

FeelTravel Hotel will be average priced among three-star hotels in Prague and attractive due to its service and design. Along with these facts, it will be situated in a quiet area in Smichov area.

## **Conclusion**

Hence, after having considered the numerous benefits and drawbacks of small business, we can sum up the results. The main detected advantage of the SMEs is the ability to create additional job opportunities. However, it is crucial to analyze the destruction dynamics in order to realize the number of net new working places. Moreover, the quality and duration of created jobs in SMEs are very unstable. Indeed the company's embodiment and migration amid the size classes should be also taken into account.

For the economy, small business is a great innovative force. Start-ups and SMEs are the backbones of the country's development as they contribute a dynamic growth to economy. It goes without saying that large companies have much better grounds for research and development implementation. It allows them to reach the leading position as a result of good awareness of the market. Comparatively, SMEs can be more effective in innovations area because they exist in a more competitive environment and need to work very hard in order to survive.

SMEs and start-ups are very attractive due to the ability to make dream and unique idea come true. It is also the satisfaction of entrepreneur's ambition to lead and owe. Despite the comparative easiness of running small businesses, it is still a very bureaucratic process that acquires many efforts from the entrepreneur. In addition to that, due to the fast developing technology, it is crucial to implement the innovative ideas in own product to stay competitive on the market.

Unfortunately, small businesses can face many challenged on their way, such as legal, administrative, financial and cultural. Legal issues are mandatory and usually it is a matter of time and money spent. For this reason, a European Commission together with the national governments introduces a lot of supporting programs. Such support is also a motivation for potential entrepreneurs to be more creative and fundamental, paying attention to details and having a substantial target. Financial help is a great benefit for SMEs, however, it should be deserved. In order to get financing, business plans should be developed in a simple and informative way, carrying the unique idea that can contribute economic growth to the country as a whole.

Cultural differences for international business will not be a problem for the neighbor countries, however, it can be a trial when the entrepreneur decides to create the business in the country

other than his origin and with different values. That is why experience is an indispensable attribute for entrepreneur.

Together with mentioned issues, there is a step that is frightening all of the start-upers – the possibility of going bankrupt. That period between three and five years of business existence is the most unpredictable and dangerous for the small business. Scientists are saying that failure is rather a part of the business cycle than its end, business people should not be afraid of them so much. Conversely, entrepreneurs should be prepared to it and have a backup plan of actions.

For the business plan analysis Czech Republic capital has been chosen as the most favorable place to start a hotel business. Such factors as comparatively low cost, beneficial location, ease of market entry and red tape procedures were taken into consideration. The description of business plan was made according to the current situation on the market with the real examples and prices. As a consequence, it was shown that even for the micro business there are a lot of steps of preparation before the business functioning. Moreover, in reality, there are much more obstacles faced.

All things considered, it should be always kept in mind that everything big starts from something small. To develop and expand the business an entrepreneur should think out beforehand and make a lot of research in the beginning. Such way of thinking and predictions can help to prepare background for the company's growth. Unique idea, customer satisfaction, service orientation, readiness for improvements, cooperation with other businesses, skillful workforce and clever management lead the company to success and prosperity. Entrepreneurs should always remember that experience will come with time and only patience, persistence and perseverance can defeat all the obstacles.

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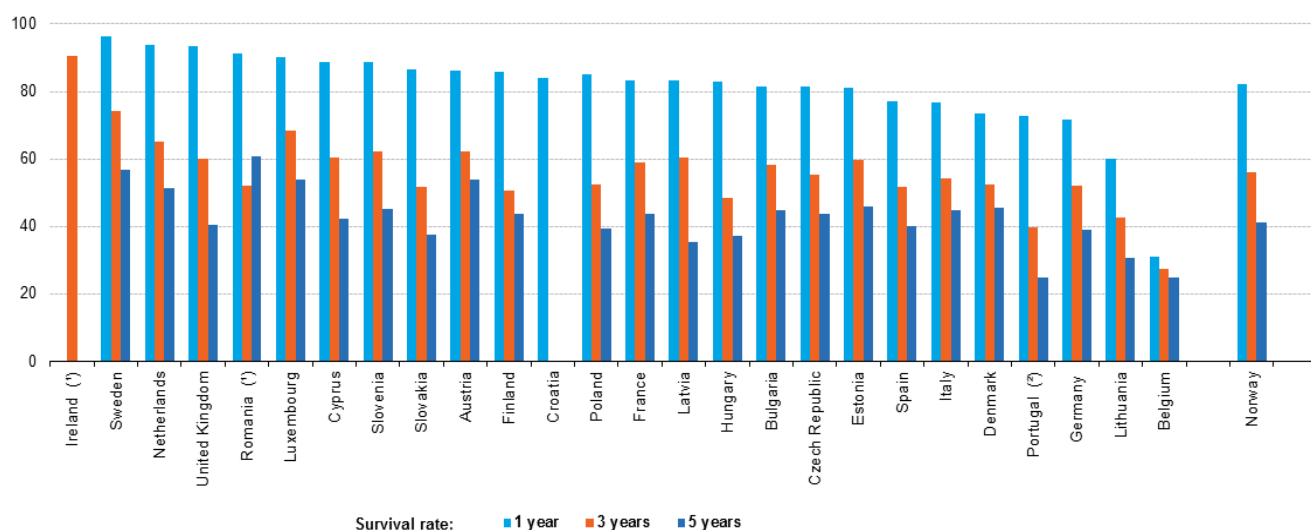


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## Appendixes

**Appendix 1.** Graph One, three and five-year survival rates of enterprises, business economy, 2014 (%). Source: Eurostat



(\*) Ireland (1 and 5 years): confidential data; Romania (3-years): break in series

(\*) Portugal: 2012 data for 5-years

Note: Greece, Croatia (3 and 5 years) and Malta: data not available

## Appendix 2. Labor costs per hour in euro, whole economy (excluding agriculture and public administration).

Source: Eurostat <http://ec.europa.eu/eurostat/statistics-explained/index.php>

	2004	2008	2012	2014	2015	2016	2016 Non-wage costs (% of total)	Change 2016/2015, %
EA-19	19.8	21.5	23.9	24.5	25.0	25.4	23.9	1.6
EU-28	23.0	25.3	28.3	29.0	29.4	29.8	26.0	1.4
Belgium	29.2	32.9	38.0	39.0	39.1	39.2	27.5	0.2
Bulgaria	1.6	2.6	3.4	3.8	4.1	4.4	15.8	7.8
Czech Republic (*)	5.8	9.2	10.0	9.4	9.8	10.2	27.0	3.8
Denmark (*)	29.6	34.6	39.4	40.6	41.2	42.0	13.9	2.1
Germany	26.8	27.9	30.5	31.4	32.2	33.0	22.4	2.5
Estonia	4.3	7.8	8.6	9.8	10.3	10.9	26.3	5.6
Ireland	25.5	28.9	29.8	29.8	30.0	30.4	13.8	1.3
Greece	15.3	16.7	15.7	14.5	14.1	14.2	24.2	0.8
Spain (*)	16.5	19.4	21.1	21.1	21.2	21.3	25.3	0.4
France (*)	28.2	31.2	34.3	34.7	35.1	35.6	33.2	1.5
Croatia	6.9	9.2	9.5	9.4	9.6	10.0	14.9	4.8
Italy (*)	22.4	25.2	27.7	28.3	28.1	27.8	27.4	-0.8
Cyprus	12.6	16.7	16.8	15.8	15.7	15.8	17.0	0.6
Latvia	2.7	6.0	5.9	6.6	7.1	7.5	20.6	6.4
Lithuania	3.2	5.9	5.9	6.5	6.8	7.3	27.8	7.5
Luxembourg	30.3	31.0	33.9	36.2	36.3	36.6	13.4	0.8
Hungary (*)	5.9	7.8	7.4	7.7	7.9	8.3	23.6	4.6
Malta	9.6	11.4	11.8	12.8	13.2	13.2	6.6	0.0
Netherlands	27.3	29.8	32.5	33.2	33.2	33.3	20.4	0.1
Austria (*)	25.2	26.4	29.7	31.4	32.4	32.7	26.3	0.9
Poland	4.7	7.6	7.9	8.3	8.6	8.6	18.4	-0.2
Portugal	11.3	12.2	13.3	13.2	13.4	13.7	20.6	2.5
Romania (*)	1.9	4.2	4.1	4.6	4.9	5.5	19.9	11.6
Slovenia	11.2	13.9	15.6	15.6	15.8	16.2	16.3	2.7
Slovakia	4.1	7.3	8.9	9.7	10.0	10.4	26.4	3.5
Finland	24.4	27.1	31.3	32.5	33.0	33.2	22.2	0.7
Sweden	29.0	31.6	37.3	37.3	37.4	38.0	32.5	1.7
United Kingdom	21.5	20.9	25.0	25.8	29.7	26.7	16.5	-10.1
Norway	30.1	37.8	56.4	53.9	51.2	50.2	18.1	-2.0

Discrepancies between the growth rates derived from the 2015 and 2016 values and the growth rates reported in the table are due to rounding.

(\*) Italy: data up to 2012 are not strictly comparable over time due to methodological breaks.

(\*) France: the aggregate shown for the whole economy for 2008 also excludes NACE Rev. 2 section P (Education).

(\*) Data for 2014 are taken from national sources.

(\*) Data for 2015 are taken from national sources.

(\*) Data for 2016 are taken from national sources.

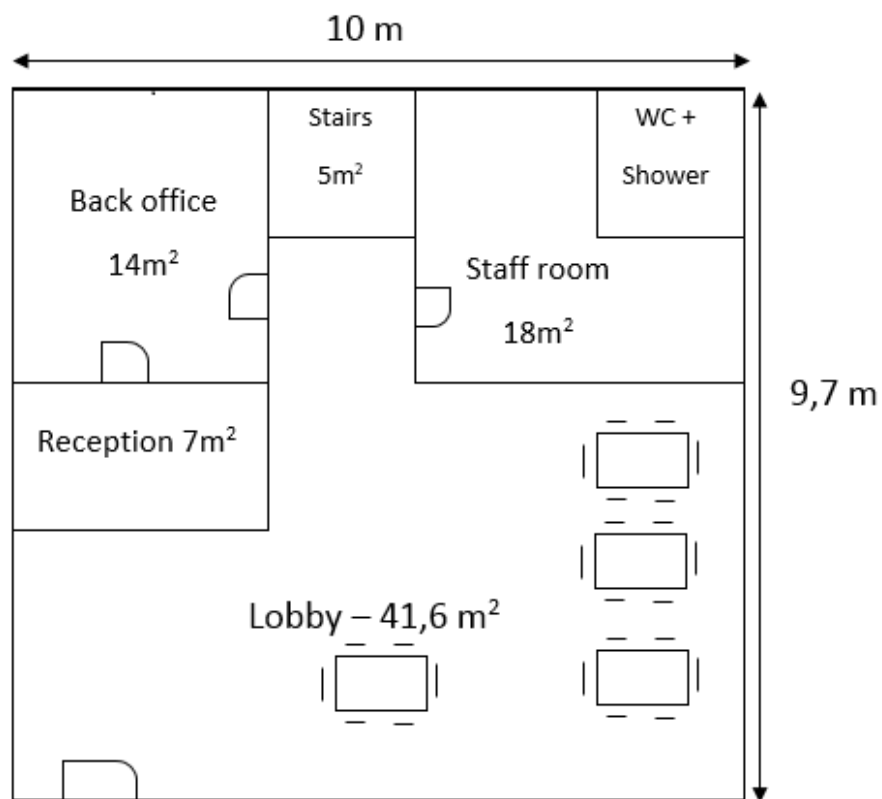
### Appendix 3. Evaluation of investment grade of individual countries.

Source: Czech National Bank – 24<sup>th</sup> April 2017

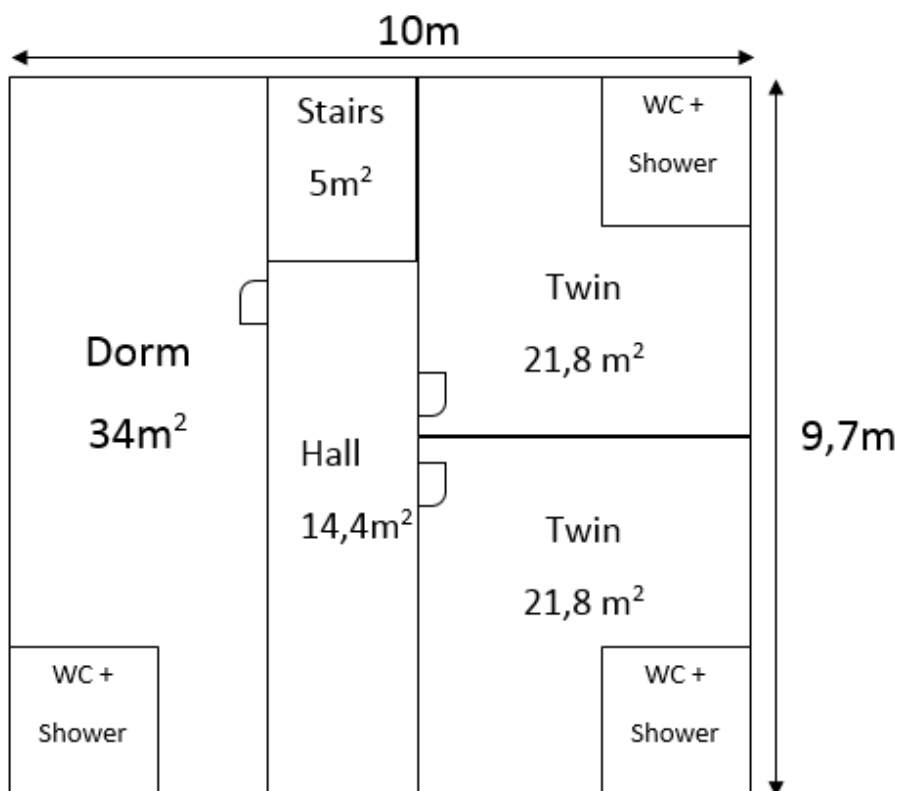
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MOODY'S		STANDARD & POOR'S		Fitch
Investment grades				
Aaa	Germany, Netherlands, USA, Switzerland, Norway, Denmark, Sweden, New Zealand, Canada, Singapore, Australia, Luxembourg	AAA	Germany, Norway, Switzerland, Singapore, Denmark, Canada, Australia, Sweden, Luxembourg, Hong Kong	Germany, Netherlands, Norway, USA, Switzerland, Singapore, Denmark, Sweden, Canada, Luxembourg, Australia
Aa1	Austria, Hong Kong, United Kingdom, Finland	AA+	Austria, Finland, Netherlands, USA	Austria, Finland, Hong Kong
Aa2	France, Korea, Kuwait	AA	Belgium, France, Korea, Kuwait, New Zealand, United Kingdom	Belgium, France, Kuwait, New Zealand, United Kingdom
Aa3	Belgium, China, Chile, Taiwan	AA-	<b>CZECH REPUBLIC</b> , China, Estonia, Taiwan, Chile	Korea, S. Arabia
A1	<b>CZECH REPUBLIC</b> , Estonia, Israel, Japan, S. Arabia	A+	Ireland, Israel, Japan, S. Arabia, Slovakia	Estonia, China, Chile, <b>CZECH REPUBLIC</b> , Israel, Slovakia, Taiwan
A2	Poland, Slovakia	A	Iceland, Slovenia	Ireland, Japan, Malta
A3	Iceland, Ireland, Latvia, Lithuania, Malaysia, Malta, Mexico	A-	Latvia, Lithuania, Malaysia, Malta	Latvia, Lithuania, Malaysia, Poland, Slovenia
Baa1		BBB+	Kazakhstan, Mexico, Poland, Spain	Iceland, Italy, Mexico, Spain
Baa2	Bulgaria, Italy, S. Africa, Spain	BBB		Kazakhstan
Baa3	Hungary, India, Indonesia, Kazakhstan, Romania, Slovenia	BBB-	Hungary, India, Italy, Romania	Bulgaria, Hungary, India, Indonesia, Romania, Russia, S. Africa, Turkey

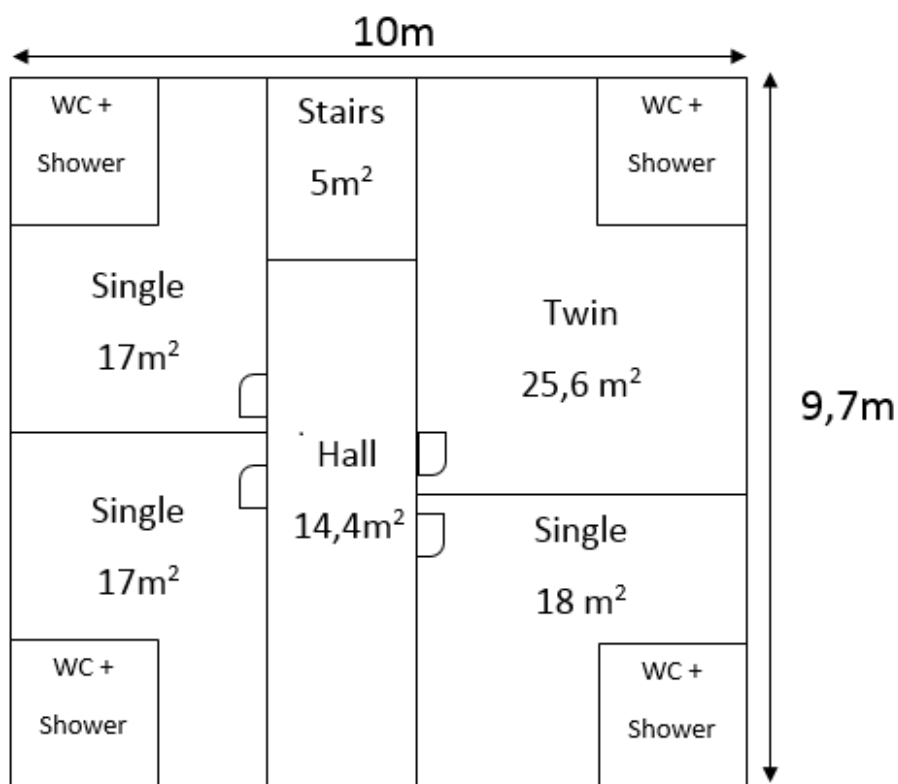
**Appendix 4.** Drawing of the ground floor of FeelTravel Hotel.



**Appendix 5.** Drawing of the first floor of FeelTravel Hotel.



**Appendix 6.** Drawing of the second floor of FeelTravel Hotel.



**Appendix 7:** Most non-residents arriving to the Czech Republic and staying overnight.

Source: Wikipedia

[https://en.wikipedia.org/wiki/Tourism\\_in\\_the\\_Czech\\_Republic](https://en.wikipedia.org/wiki/Tourism_in_the_Czech_Republic)

Rank	Country	2015	2016
1	 Germany	1,749,276	1,879,754
2	 Slovakia	564,496	645,788
3	 Poland	467,285	543,247
4	 United States	507,376	511,629
5	 United Kingdom	441,516	470,643
6	 Russia	432,768	406,410
7	 Italy	371,686	368,851
8	 China	285,404	354,799
9	 South Korea	N/A	322,108
10	 Austria	268,961	283,608
	Total	8,686,726	9,288,013

## Appendix 8: Hotels and similar accommodation establishments by size class, 2015 (%)

Source: Eurostat <http://ec.europa.eu/eurostat/statistics-explained/index.php>

	Total number of hotels and similar accommodation establishments	Less than 25 rooms (*)	From 25 to 99 rooms	From 100 to 249 rooms	250 rooms or more
EU-28 <sup>(2)</sup> ( <sup>3</sup> )	203 316	59.9	32.3	7.8	:
Belgium	1 557	:	:	:	:
Bulgaria	2 180	23.5	46.0	15.6	14.9
Czech Republic	5 992	77.5	19.4	2.6	0.5
Denmark	525	:	:	:	:
Germany	33 635	69.6	25.1	4.5	0.7
Estonia	414	:	:	:	:
Ireland <sup>(4)</sup>	2 438	:	:	:	:
Greece	10 111	52.3	39.9	5.9	1.9
Spain	19 718	61.7	25.9	8.9	3.4
France	18 328	:	:	:	:
Croatia	938	42.2	30.1	19.5	8.2
Italy <sup>(2)</sup>	33 202	54.8	40.9	4.3	:
Cyprus	786	53.4	27.4	15.6	3.6
Latvia <sup>(2)</sup>	332	61.1	30.4	8.4	:
Lithuania	418	60.3	32.5	6.7	0.5
Luxembourg	236	:	:	:	:
Hungary	2 185	66.6	26.5	5.4	1.4
Malta	161	21.1	37.9	27.3	13.7
Netherlands	3 525	:	:	:	:
Austria	12 625	:	:	:	:
Poland	3 723	51.5	40.7	6.7	1.0
Portugal	2 430	:	:	:	:
Romania	2 626	51.4	37.2	9.5	1.8
Slovenia	681	:	:	:	:
Slovakia	1 509	:	:	:	:
Finland	777	:	:	:	:
Sweden	1 992	19.3	45.8	22.2	12.7
United Kingdom <sup>(5)</sup>	40 272	:	:	:	:
Iceland	402	56.5	38.6	4.0	1.0
Liechtenstein	35	:	:	:	:
Norway	1 082	27.1	46.7	20.8	5.5
Switzerland	5 055	:	:	:	:
Montenegro	:	:	:	:	:
FYR of Macedonia <sup>(4)</sup>	233	:	:	:	:
Serbia <sup>(4)</sup>	676	:	:	:	:
Turkey <sup>(4)</sup>	3 125	:	:	:	:

Note: data transmitted to Eurostat on an optional basis and therefore not available for all countries; due to rounding, deviations can occur between total and subtotals.

(\*) Comparability of this data may be affected by the data collection thresholds since in many countries,

(<sup>2</sup>) EU-28 estimated shares based on 15 Member states' data representing 58% of all Hotels and similar

(<sup>3</sup>) The share for establishments between 100 to 249 rooms includes those of 250 rooms or more.

(<sup>4</sup>) 2014 data.

(<sup>5</sup>) 2013 data.

": - Data not available.



## Appendix 9: Net occupancy rates of bed places and bedrooms in hotels and similar accommodation establishments by size class, 2015

Source: Eurostat <http://ec.europa.eu/eurostat/statistics-explained/index.php>

	Occupancy rates of bed places					Occupancy rates of bedrooms				
	Total	Less than 25 rooms	From 25 to 99 rooms	From 100 to 249 rooms	250 rooms or more	Total	Less than 25 rooms	From 25 to 99 rooms	From 100 to 249 rooms	250 rooms or more
<b>EU-28<sup>(1)</sup></b>	44.4	31.0	44.4	56.6	63.2	:	:	:	:	:
Belgium	44.0	:	:	:	:	61.5	:	:	:	:
Bulgaria	37.0	16.2	22.0	33.7	48.4	48.7	20.6	28.7	41.6	66.3
Czech Republic	36.2	22.7	39.4	49.9	52.5	43.0	26.9	46.0	55.8	59.7
Denmark	47.0	:	:	:	:	61.0	:	:	:	:
Germany	43.0	31.1	44.7	51.1	52.6	60.2	:	55.5	65.1	67.8
Estonia	44.0	:	:	:	:	52.0	:	:	:	:
Ireland	52.0	:	:	:	:	68.0	:	:	:	:
Greece	49.1	24.6	44.0	59.3	63.7	46.8	24.0	42.3	56.7	60.7
Spain	58.1	30.7	49.9	64.3	72.9	62.0	34.9	54.7	69.7	76.7
France	47.0	:	:	:	:	59.0	:	:	:	:
Croatia	53.5	36.9	45.5	61.4	60.8	54.4	39.4	46.8	61.9	61.6
Italy	42.5	:	:	:	:	44.9	:	:	:	:
Cyprus	65.3	31.0	51.3	70.0	71.9	63.0	32.0	53.2	69.6	67.4
Latvia <sup>(2)</sup>	36.3	17.7	36.3	48.3	:	42.4	21.4	41.1	54.2	:
Lithuania	36.8	19.7	30.0	42.6	44.9	49.3	29.4	41.6	55.5	58.2
Luxembourg	39.4	:	:	:	:	45.6	:	:	:	:
Hungary	36.3	19.6	35.2	47.5	48.1	49.8	30.6	47.6	61.1	65.3
Malta	64.3	29.1	57.5	67.7	66.1	74.0	36.1	69.0	77.3	75.0
Netherlands	45.6	:	:	:	:	68.1	:	:	:	:
Austria	28.9	:	:	:	:	:	:	:	:	:
Poland	36.6	35.7	44.4	55.1	56.5	45.3	44.5	50.9	63.3	65.1
Portugal	44.1	:	:	:	:	48.2	:	:	:	:
Romania	33.8	:	:	:	:	47.4	:	:	:	:
Slovenia	44.7	:	:	:	:	49.5	:	:	:	:
Slovakia	29.5	:	:	:	:	35.5	:	:	:	:
Finland	38.9	:	:	:	:	51.1	:	:	:	:
Sweden	43.2	29.5	37.2	46.9	52.5	55.3	38.6	47.3	59.4	68.7
United Kingdom	:	:	:	:	:	:	:	:	:	:
Iceland <sup>(2)</sup>	44.6	33.4	38.4	44.8	61.5	52.4	38.2	42.2	52.2	79.7
Liechtenstein	27.6	:	:	:	:	36.9	:	:	:	:
Norway	37.3	23.5	32.3	41.3	39.5	53.6	35.5	46.0	58.9	56.9
Switzerland	41.7	:	:	:	:	51.5	:	:	:	:
Montenegro	35.2	:	:	:	:	:	:	:	:	:
FYR of Macedonia	23.0	:	:	:	:	37.2	:	:	:	:
Serbia	28.6	:	:	:	:	29.5	:	:	:	:
Turkey	51.2	:	:	:	:	:	:	:	:	:

Note: data transmitted to Eurostat on an optional basis and therefore not available for all countries.


<sup>(1)</sup> EU aggregates estimated for the purpose of this publication. Occupancy rates by size class: EU aggregates estimated on the basis on 13 Member states' data representing 47% of all nights spent in hotels and similar accommodation establishments in the EU.

<sup>(2)</sup> 2014 data.

<sup>(3)</sup> The rates estimated for establishments between 100 and 249 rooms include all establishments above 100 rooms.


": - Data not available.

## Appendix 10. Cost of the building Ke Koulce Prague 5 – Smíchov (03.03.2017)



**SREALITY.CZ** Přihlásit se Česky Seznam.cz

Vypis Předchozí inzerát Další inzerát



Zobrazit 15 fotografií v galerii

**Prodej činžovního domu 290 m<sup>2</sup>**  
Ke Koulce, Praha 5 - Smíchov [Panorama](#)  
**13 500 000 Kč (46 552 Kč za m<sup>2</sup>)**



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