

# Management of Energy Costs for Sme's, Evidence From Kosova Economic Environment

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## ABSTRACT

This paper deals with issues of strategic management, particularly strategic planning of energy costs and their effect on the overall performance of businesses. It is based on empirical results of the original research survey Enterprise Surveys data for Republic of Kosova, performed via questionnaire surveys by the World Bank in three rounds during years 2005, 2009 and 2013. The analyses presented in the paper were conducted on the third round sample of organizations operating mostly in the SME sector in the Republic of Kosova.

Among typical obstacles to the economic environment we found also the energy problem, specifically the power outages that increase further the costs of power supply for SME's. These phenomena not only create a state of turmoil and turbulence in the competitive environment and generate changes in market conditions, but require changes and development in organizations. In these circumstances organizations are forced to adapt costly solutions, like generators or other tools to guarantee the customer satisfaction.

Therefore to achieve any competitive advantage, organizations must take in consideration the current economic environment.

The interdependence between the level of energy costs and enterprise performance criteria is examined with the use of some hypotheses. The results are commented and discussed.

*Keywords:* energy costs, business strategy, performance criteria, questionnaire research, SMEs

*JEL Classification:* D22, L21, L25, R11

## 1. Introduction

During the last years, Kosova's enterprises can be characterized by the effort to adapt on new emerging conditions which appeared after the outbreak of the global economic crisis in around 2007. Although economic revival is wistfully awaited, the recession still exists in the Kosova's economy with often fatal influence on many unstable enterprises. In these turbulent times strategic management and planning takes an important role, however is more or less neglected especially by the SMEs sector managers. And it is insistent more than ever to revise business goals and formulate them

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clearly to be able to steer the craft of business through ruffles of uncertainty and variable conditions.

Taking a retrospective look we see a number of shortcomings of the Energy cost used in vast majority of Kosovar companies:

1. organization of production and cost accounting are managed separately the gifted generate setting different objectives, often divergent;
2. the collection and allocation of indirect costs on the basis "keys", which are often inconclusive or inaccurate;
3. large gap between gathering information on costs and complete analysis leads to the impossibility of establishing and implementing practical measures to reduce operational costs;
4. do not delineate the costs of production in variables and fixed, which leads to reduced efficiency of cost analysis and diffusion responsibilities.

The process of strategic management includes usually basic and periodically repeating set of consecutive stages, through which the companies create, implement and control achievement of the long-term business objectives (Johnson, 2006; David, 2013):

- 1 strategic analyses,
- 2 formulation of strategy,
- 3 strategy implementation,
- 4 feedback, ex-post evaluation and correction.

Permanent implementation of this process together with recent updating of the strategy and reasonable planning period brings often the strategic predominance for the company.

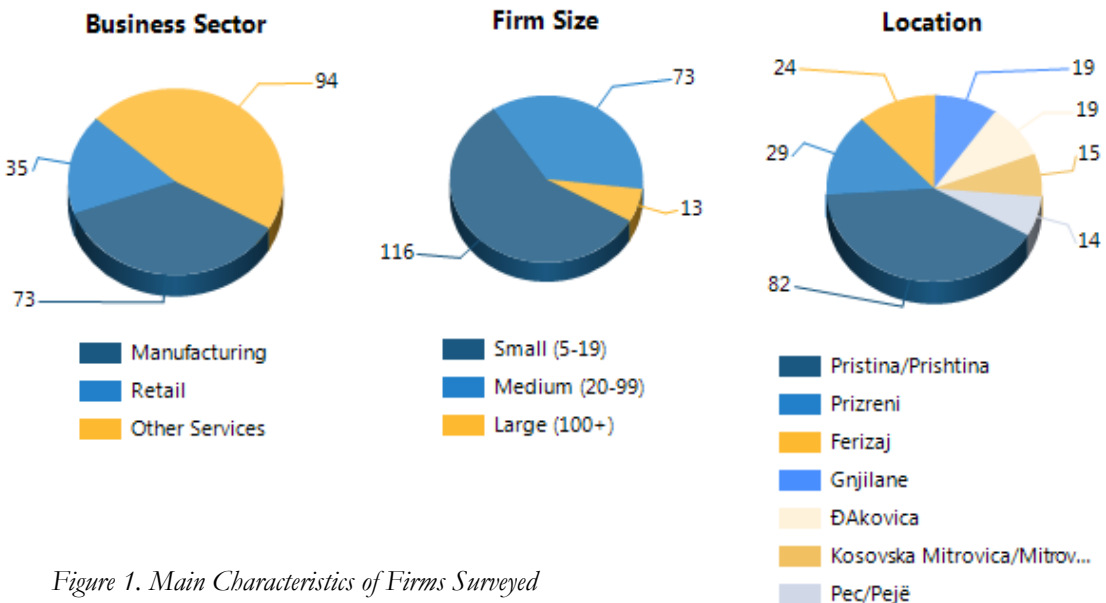


Figure 1. Main Characteristics of Firms Surveyed

Many researchers in the field of strategic management confess that this area is still paid by company management little attention. Managers often do not realize the significance and importance of strategic approach for business or they are not able to establish it. They are often overloaded by operational tasks that arise from everyday business practices and the bird's eye view to see the goals and challenges they face in a broader context is withdrawn from them. Moreover they are often not able or competent to carry out necessary inner-outer management analyses.

The paper presents the findings of research that show how important strategic management and planning of energy costs are and can help to strengthen the awareness of strategic management to Kosova's management community.

Business owners and top managers in 202 firms were interviewed from January 2013 through November 2013.

## 2. Theoretical Background

Although big companies create enormous output for the vitality of national economy in the changing global economic environment, which is characterized by continuous structural changes and enhanced competitive pressures, the important role of small and medium-sized enterprises (SMEs) is still increasing.

In the European Union SMEs are the backbone of the economy, employing more than 87 million EU citizens. SMEs generate every second newly created job and produce nearly 60% of the GDP of the European Union (EC, 2012). However, SMEs were increasingly afflicted by the crisis. Research shows that only 50 % of businesses survive the first five years of its existence and economic crisis definitely decreases this number. Estimated full 1,7 million jobs were lost in 2009 due to insolvency of companies, what represents an increase of 22 % compared to 2008. For Kosova there are not clear data of how many companies suffered from the Global Financial Crises, because the effect of this crises still persist on Kosovar Economy. Besides the Financial crisis the economical environment in Kosova suffers further from some persistent and pathologic infrastructural constraints.

Strategic cost management is a consequence of mutations that occur in the current environment and requires a permanent adaptation of tools and techniques so as to improve the strategic position of organizations. For management accounting information provided to be useful to managers in the organization's strategic objectives, management accounting system should be designed and used to follow the mission and competitive strategies of organizations, by conducting an analysis in relation to the economic environment, the costs associated with customers, competitors, etc..

In this context, we stop first at refining the concept of strategy. Ever, the strategy is the art of winning the war. It applies to the company, in so far as it fights against competitors when its survival is threatened.

For optimal transposition of the strategy, organizational restructuring operation is required. This involves choosing, distribution and organization of human, material and financial means necessary to achieve the overall strategy, highlighting the differentiated structures and mechanisms for the following subsystems:

- the accounting and management control;

• heritage and power of decision for piloting.

Subordinated financial constraints which determine independence and survival, the company can not be managed without economic measurement device. This should be abandoned in favor of economic technical language. Also, to connect positive environmental changes must prove that the company has to heritage, employment and capacity and hierarchical decision-making activities (difficult decision courage, leadership and empowerment of people's resources).

If you are provided two preconditions, effective strategic management at all levels requires strict completion of four stages. The concept of American authors are:

a. formulation of strategies;

b. communication of these strategies throughout the organizations;

c. development and implementation of tactical solutions to achieve these strategies;

d. development and implementation of controls to monitor the success of implementation stages and, therefore, to achieve strategic objectives.

In the SME sector, the role of management is always derived from the size of the organization and the role of the owner. Primary importance of management function is not by Zich (2010) determined so much by the fact that management has unquestioned responsibility for the formulation and implementation of strategy as the assumption that competitiveness is created or at least affected by all management activities in terms of features and functions of management with a focus on resources, competencies and processes. Size of organization however, does not necessarily reduce the level of strategic management importance. In large enterprises responsibility for strategic management takes the entire department of analysts and competent managers, but in small businesses the primarily strategic manager role takes usually the owner.

According to Volberda et al. (2010) strategic management based on long-term forecasts, helps the company to anticipate future challenges and opportunities. The term strategy is closely linked with the objectives that it tracks. According to Kotler and Keller (2007) strategy should express the basic idea of which way the company goals will be achieved. The importance of strategy for innovation development and competitiveness of firms emphasized many authors in the last years, e.g. Glaister (2008), Skokan (2010), Volberda et al. (2010), David (2013).

The application of strategic management in the Kosova business environment is still at a very low level. The ability to succeed in constantly changing environment demands highly competent management in which Kosovar companies have significant gaps especially in terms of lack of strategic thinking and awareness.

### 3. Methodology

Most surveys were administered using the Enterprise Surveys Global Methodology of the World Bank as outlined in the Methodology page<sup>1</sup>, while some others did not strictly adhere to the Enterprise Surveys Global Methodology. For

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<sup>1</sup> Enterprise Surveys (<http://www.enterprisesurveys.org>), The World Bank.2015

example, for surveys which did not follow the Global Methodology, the Universe under consideration have consisted of only manufacturing firms or the questionnaire used have been different from the standard global questionnaire. Caution should be done when comparing raw data and point estimates between surveys that did and did not adhere to the Enterprise Surveys Global Methodology. For surveys which did not adhere to the Global Methodology, any inference from one of these surveys is representative only for the data sample itself.

Regional averages of indicators are computed by taking a simple average of country-level point estimates. For each economy, only the latest available year of survey data is used in this computation. Only surveys, posted during the years 2009-2015, and adhering to the Enterprise Surveys Global Methodology are used to compute these regional and "all countries" averages. Descriptions of firm subgroup levels, e.g. how the ex post groupings are constructed, were provided in the Indicator Descriptions document.

Statistics derived from less than or equal to five firms were displayed with an "n.a." to maintain confidentiality and should be distinguished from "." which indicates missing values. Also note for three growth-related indicators under the "Performance" topic, these indicators are not computed when they are derived from less than 30 firms.

Standard errors were labeled "n.c.", meaning not computed, for the following:

- 1) indicators for all surveys that were not conducted using the Enterprise Surveys Global Methodology and
- 2) for indicator breakdowns by ex post groupings: exporter or ownership type, and gender of the top manager.

#### 4. Results and discussion

In this paragraph data obtained from different interviews are shown through the answers in the main questionnaire. Most important charts and tables are presented and commented.

**Table 1.** General Indicators of the Survey

| Indicator   | Kosovo | Eastern Europe & Central Asia | All Countries <sup>2</sup> | - |
|---|--------|-------------------------------|----------------------------|---|
| Age of the establishment (years)                              | 14.0   | 13.1                          | 15.9                       | - |
| Proportion of private domestic ownership in a firm (%)        | 99.4   | 93.7                          | 88.6                       | - |
| Proportion of private foreign ownership in a firm (%)         | 0.3    | 4.9                           | 9.1                        | - |
| Proportion of government/state ownership in a firm (%)        | 0      | 0.8                           | 0.4                        | - |
| Proportion of a firm held by the largest owner(s) (%)         | 94.5   | 85.1                          | 83.0                       | - |
| Percent of firms with legal status of publicly listed company | 0      | 1.7                           | 2.9                        | - |
| Percent of firms with legal status of                         | 54.4   | 85.2                          | 40.6                       | - |

| privately held Limited Liability Company                  |      |     |      |   |
|---|------|-----|------|---|
| Percent of firms with legal status of Sole Proprietorship | 41.4 | 9.8 | 39.5 | - |
| Percent of firms with legal status of Partnership         | 3.4  | 1.1 | 8.1  | - |
| Percent of firms with legal status of Limited Partnership | 0.3  | 1.3 | 6.5  | - |

Considering the young life of the Kosova's Independence, we note that the relatively older age of the firms is an indicator of persistence in the market. Anyway the Foreign Direct Investments are still modest in the economical system due to uncertainty of business environment. Generally family own business occupy the panorama of the business background, with highest percentages in the region and further.

After being presented with a list of 15 business environment obstacles, business owners and top managers in 202 firms were asked to choose the biggest obstacle to their business.

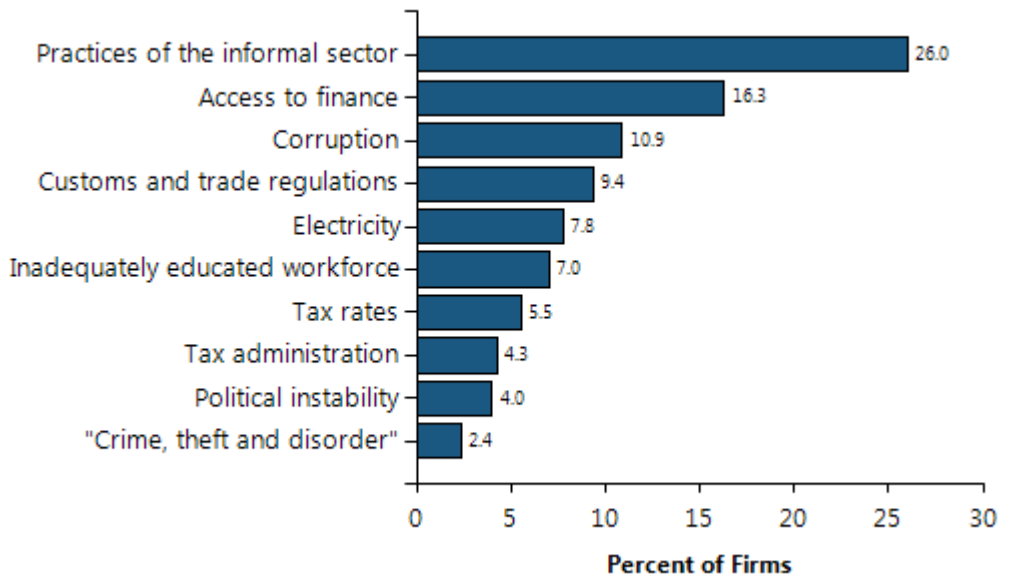


Figure2 List of 15 business main environment obstacles

The Kosovo economic environment is full of uncertainties for the local and international entrepreneurs. All though in the top list of biggest obstacles (Fig. 2) we read Practices from the informal sector, access to finance and corruption, still electricity is an important constraint, combined with other energy obstacles.

**Table 1.** Main energy indicators compared to other surveys

| Indicator  | Kosovo | Eastern Europe & Central Asia | All Countries <sup>2</sup> |
|--|--------|-------------------------------|----------------------------|
| Number of electrical outages in a typical month  | 10.7   | 2.0                           | 5.5                        |
| Duration of a typical electrical outage (hours)  | 1.9    | 1.2                           | 2.7                        |
| If there were outages, average duration of a typical electrical outage (hours)               | 2.5    | 3.5                           | 4.5                        |
| Losses due to electrical outages (% of annual sales)   | 6.9    | 1.2                           | 2.5                        |
| If there were outages, average losses due to electrical outages (% of annual sales)          | 10.1   | 2.9                           | 4.5                        |
| Percent of firms owning or sharing a generator   | 65.0   | 21.3                          | 33.1                       |
| Proportion of electricity from a generator (%)   | 8.1    | 2.5                           | 7.4                        |
| If a generator is used, average proportion of electricity from a generator (%)               | 13.6   | 11.9                          | 18.9                       |
| Days to obtain an electrical connection (upon application)                                   | 58.8   | 26.6                          | 30.6                       |
| Percent of firms identifying electricity as a major constraint                               | 49.5   | 17.9                          | 33.6                       |
| Proportion of products lost to breakage or spoilage during shipping to domestic markets (%)* | 0.3    | 0.8                           | 1.1                        |
| Percent of firms identifying transportation as a major constraint                            | 22.7   | 8.5                           | 20.0                       |

Source: *Enterprise Surveys* (<http://www.enterprisesurveys.org>), *The World Bank*. 2015

One of the most objective indicators in the survey is the presence of generators in the firm: Percent of firms owning or sharing a generator 65.0% of the total. This shows the real threat that power outage can present to the firms. In monetary terms the power provided by generators is much higher than the electricity price from the public utility provider

## Conclusion

Presented paper is focused on importance of strategic management and strategic planning related to energy costs. There were shown results of original questionnaire research performed mostly in SMEs of Kosova from the Enterprise Surveys data of the World Bank 2013. Data were characterized from the point of geographical view, the economic activity structure, period considered by strategy and the year of last strategy update. Strategy forms were confronted with size (number of employees and annual turnover), legal status and six selected performance parameters.



We can summarize most important finding of presented item like that: Bigger companies pay less attention to management of energy costs and have more often prepared cost effective solutions than smaller enterprises. Enterprises who did prepare brief, partial, concise strategic document proved only in 40 % of observed performance parameters better results than enterprises without written business plan, so there is necessary to put impact on proper strategic planning in all significant business areas. Our findings are supported from retail SMEs with high strategic clarity will outperform those with moderate strategic clarity, but SMEs with low strategic clarity outperformed those with moderate strategic clarity.

Criticizing traditional cost management, we emphasize that traditional cost management no longer meet the needs of management working in a newly competitive environment. These methods have lost their importance because, emphasize the company's internal environment and not oriented to the environment and external conditions and, in fact, are not the set of information needed by top management of the company, managing business in a competitive environment.

It is therefore necessary to improve management accounting mentality and achieve a more realistic optical about cost management and strategy. In this respect, strategic cost management helps them through the development and use of strategic management accounting techniques related to aspects of external information needs to cope with uncertainty and economic environment to support the decisions of a strategic nature.

The limitations of the paper are based in limited geographical scope of obtained data. Unfortunately the survey was not able to cover reasonable number of SME's of Kosova Republic with comparable sample size. In other hand the size of data group is relatively large. Shortcomings of utilized methodology are also in frequency of size groups, where we've got mostly micro and small enterprises (10 to 50 employees). These limitations nevertheless in our opinion do not outclass importance of presented findings, which come from real life conditions.

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