

# OBJECTIVES AND DIFFICULTIES IN SME'S SECTOR IN ROMANIA

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## Abstract

*The topic of this paper keeps deep roots in the old economic thinking and will share between such basics and update data for Romania. On the one hand, the Marginalist 'perfect competition model' daring to link between 'welfare maximizing' and what ever-since regards 'small and medium size enterprises'(SME), and that basing on a real and simple mathematical demonstration of that time. On the other, the latter and today condition in a country like Romania in early 21st century, namely in a time of all compatibility dismantled between economic development and just SME here working. We'll also see below that SME cannot be missing, together with activities and their aspects that appear even surprising at the first sight. All facts and data here develop during the two years previous to the current pandemic (2018-2019). Data, including some analyses made, here come from National Institute of Statistics (INSEE), National Council for SME, both in Romania, plus the European Commission(EC) Manual. To equally be noted that these same data and analyses will make the basis for future research considering current health crisis and its impact on the Romania's business environment.*

**Key concepts:** *Small and Medium Size Enterprises (SME), Marginalism, Perfect Competition Model*

**JEL Classification:** *D0, D01, E22*

## Introduction

As in all economies, here, in Romania the SME sector stays a good weight in total GDP – its direct production -- and employment, contributes to market competition and to exports and helps innovation and technologies to develop. As compared to the large companies, SMEs prove more flexible behaviour, better reacting to business environment changes and to market demand. In fact, large companies fully benefit from SME services and remain, in a way, dependent on them. SMEs are geared towards meeting the needs of the local market, uses local resources, including labor, and beyond these proves able to encounter some social problems in their areas.

### 1. Literature review. Classic and neoclassic thinking

This topic might need recalling the *classic* and *neoclassic* contributions of the late 19<sup>th</sup> Century. More exactly, it is about the *Marginalist* Vilfredo Pareto's contribution, with his '*Perfect Competition Model*'. Actually, *Marginalism* is about three Schools of thinking in the Europe at that time: the Swiss one with Leon Walras and Vilfredo Pareto, the Austrian one with Wieser and Bohm-Bowerk and, of course, the British one with WS Jevons and A. Marshall (Andrei LC. *Economie* 2020, p. 66). Or, the author uses what is pretty rare in the general economic thinking, i.e. mathematical demonstration (we might be accustomed rather to mathematics of econometrics and modelling for specific aspects and areas, but not for so general economic principles – for which mathematics limits to descriptions).

Besides, Pareto focuses on the *efficiency* only, as later agreed, and limit to just one of the two criteria of welfare (actually, this is the Pareto (type) Efficiency that is different issue than the popular sense of the word and differently applies). Today all our students know this Pareto's theory-model of macro-efficiency associated to perfect competition. Viewed like this, *welfare* achieved might drag perfect competition into a genuine trend-alternative of the economy – i.e. and *perfect competition* bases on *small-medium size* and never influential firms all over (the market). According to such thinking fundamental, the firms' extending would be equivalent to their physical inequality, in all moments (statically), the one that makes the

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same with individual market influences and also ever destruct both perfect competition and *Pareto efficiency* bases.

Actually, this story is about two basic theories here arguing against each other and ends by here identifying two truths that are both vivid and apparently excluding one-another (this might be like the current largest theories of physics confronting each other: quantum mechanics and theory of relativity). The Pareto's one excels in proven accuracy and common sense – i.e. and even nowadays *small and medium size enterprises* (SMEs) do exist/survive and this as a majority in number in all national economies even one and half-centuries after the *Marginalism's* time. But the other equally couldn't be denied, either: firms are extending due to the (other) truth (the one) of the *economies of scale* – and this leads to the spread of large and gigantic companies world-wide. Or, it is already well understood that and how this other theory claims to be right – i.e. against those who might argue that the best job done would be on the other firms' size side. Nowadays economic progress might be seen as synonymous with large companies in progress and the developed economies of present do confirms this idea.

Then, small firms aren't likely to be influential, as individually, and today they aren't influential in their mass either. Despite that – i.e. here including that the real progress might remain on the opposite side --, *small and medium size enterprises* (SMEs) include in their reality their contribution to all: welfare, GDP and employment. Besides, the economic *competition* idea isn't dead either in the public conscience – the individual consumer's significance and firm's cost efficiency when competition in place are the same as in the classics-neoclassic time and view.

## **2. Concepts and criteria of the SMEs' definition**

There is no unitary definition for *Small and Medium size Enterprises* (SMEs) and even their nomination is variable. The *SME* term is used in the EU member countries; the same is ‚*small business*‘ in Anglo-Saxon areas, ‚*small entrepreneurship*‘ in Russian Federation and Ukraine as well as several terms are used in the US: enterprise "independently owned, independently managed and not dominated in the branch of activity".

Back to the EU, since its establishment in 1956 by the Treaty of Rome, it did enough express about this sector, about full significance and development of SMEs. The latest were viewed up to mid last decade as: (i) *micro-enterprise* for 1-9 employees; (ii) *small enterprise* for 10-99 employees; (iii) *medium enterprise* for 100-500 employees. At present three criteria of delimiting the SME category are about: average employees' number, business turnover and total assets. The entrepreneurs might now use a full *manual* for classifying companies in the categories here mentioned – i.e. micro, small and medium size. This manual issued by the EC so equally helps for European grant funds to be accessed properly by SMEs as correspondingly for their investments made. It is written in this Manual: *In order to characterize a company as SME belonging there is not only its size to be considered – i.e. number of employees, turnover and total written in the balance sheet. As for instance, a company might be small enough according to these, but there might be more resources accessed as significant due to some ownership, affiliation and/or partnership with larger companies that make it ineligible as SME.* Such a SME related analysis is becoming more and more casual, except for the following small Diagram information about firms:

*Middle size*: less than 250 employees; net annual turnover lower than 50 million euro; total assets less than 43 million euro.

*Small (size)*: less than 49 employees; both net annual turnover and total assets lower than 10 million euro.

*Micro(-firms)*: less than 9 employees; both net annual turnover and total assets lower than 2 million euro.

Actually there is not a standard definition for SME in Romania either, except for some regulations establishing optimum levels for either employees, or business turnover per individual enterprise. According to Law no. 175 of 22 May 2006 that regards stimulating and development of SMEs these last individually employ less than 250 people and make less than 50 million euro turnover.

As for the *number of employees* in a firm or company this stays the most used criterion for establishing /defining this firm's/company's size and size category. Nevertheless controversy comes up on this topic as well – e.g. Osteryoung & Newman (1993): it might be false the idea that an enterprise is always small when and due to its low number of employees; on the contrary, the same for that an enterprise always get larger as the result of hiring more people. And since this way such a considering – i.e. criterion of SME identifying – might loose some efficiency basing on just the number of employees *turnover* might take its place – i.e. as such a criterion. As for the last, turnover proves realistic and significant -- i.e. as available and/or easy to extrapolate (Gibson, van der Vaart, 2008). In context, the EC seems to have allowed the alternative options to number of employees considered for turnover's and total assets' thresholds.

### **3. The Romanian SMSE's behaviour**

The economic importance of SMSE's is the same in all national economies, here including the European and EU regions, and certainly here including Romania. The author of these lines agrees that the very 'idea movement' in favour of SMSE in Romania is of EU origin. Competitive industries and enterprises (firms, companies), jobs creating and economic growth basing on improved business environment belong to the EU agenda. European (EU) documents find that SMSE are 99% of total businesses in the EU area and responsible of 2/3 of jobs in the private economy of the EU area (*European Commission: Enterprises and industry*). Besides, the SMSE sector gives way to concrete EU policy objectives like: strengthening industrial bases, innovation and its promotion as support of economic growth, SMSE's promotion together with entrepreneurial culture and all this series could end in favour of domains like the EU market area and investments in space. The European Commission (EC) and European Bank for Investments (EBI) worked together to launch the so-called '*Plan for Investments in Europe*', in which context 360 billion Euro were mobilized for about 850 thousand SMSE to improve their financing accessing. In Romania, the *White Paper of SMEs* (*White book of SMEs in Romania*, 2019. *Research report XVII, 2019*) annual report met its 17<sup>th</sup> edition in 2019 with an update and deep description of this category of firms from several stand points of research and public survey (see the following Tables): difficulties and needs, especially financial needs, then financing sources, innovation implied, propensity for reimbursable funds, criteria they take into account in choosing their business partner. Or, this is then for strategy proposals and finally similar for the business environment – i.e. of the same year 2019.

*National Council of Small and Medium Size Enterprises* in Romania (CNIPMMR) drawn a study in partnership with Business Environment and Trade Office (MMACA) in 2019 on 788 entrepreneurs' and managers' responses of the whole country regarding quantity and quality of business environment, e.g. situation, trends and perceptions. See Table 1.and below.

**Table no.1 - Business opportunities of SMSE (as declared by)**

1	Foreign market demand growth	64.9%
2	New products assimilation	57.82%
3	Business partnership	55.66%
4	New technologies	49.46%
5	Penetration of new market spaces in domestic and/or foreign market areas	35.31%
6	Grants obtaining	30.86%
7	Digitization	28.17%
8	Exports and export growth	20.75%
9	Others	1.62%

*White book of SME in Romania, 2019.*

Most of SMEs see the foreign markets' demand growth the number one business opportunity. Innovation, new products and technologies assimilating as well as partnerships and more markets penetrating are about the same. On the other hand, grants accession for own business and investments, business' digitization and exportation were coming on the last positions of the same business opportunities.

**Table no.2 - The SMSE's activity dynamic (during the last two years)**

SMSE	%
More intense activity	14.28
The same activity parameters	35.48
Less intense activity	39.33
Bankruptcy	10.91
<b>TOTAL</b>	<b>100.00</b>

*White book of SME in Romania , 2019.*

.During the previous two years of the Sars-cov-2 pandemic (i.e. 2018-2019) SMEs participants to this study saw the same or lower activity levels than in the years before, except for 15% of them here mentioning, on the contrary, some growth or activity intensifying. Or this last is pretty balancing bankruptcies declared of the same period – i.e. no significant advance for the SME sector or just a stagnation for the 2018-2019 years interval.

**Table no. 3 - Major Difficulties of SMSE (declared by)**

1	employment, staff's maintenance and training	57.10%
2	bureaucracy	48.19%
3	inflation	47.1%
4	unfair competition	45.69%
5	declining domestic demand	44.74%
6	increase in wage related expenses	42.86%
7	excessive taxation	42.32%
8	instability of the national currency	38.14%
9	poor infrastructure	34.91%
10	corruption	33.96%
11	the cost of loans	28.17%
12	delays in collecting invoices	27.36%
13	excessive controls	26.55%
14	competition from imports	25.88%
15	difficult access to credit	22.51%
16	non-payment of bills by the state	19.27%

17	obtaining the company's consultancy and training	18.33%
18	knowledge and adoption of the <i>acquis communautaire</i>	16.85%
19	decrease in export demand	14.42%
20	more	0.40%

*White book of SME in Romania , 2019.*

Such stagnation might be viewed in the vicinity of difficulties just directly expressed by the SMEs in this given survey. The first range of these in the decreasing order belongs to the employed and employable staff, to its stability in place, to its professional profile and training attended – i.e. 60% of interviewed firms do mention this area of problems. Next impediment to the companies' development would be the bureaucracy – i.e. for half of those interviewed. Then there come: taxes (high), high bank credit interests, too high rise of wage and other expenses, too large delays in payments' collection on invoices issued to customers. Though, note that besides the difficulty degree here implied, all these items so far actually belong to the financial area of companies' activity – e.g. liquidities' scarcity resulting. Or, there might be at least another series of difficulties than financial, the ones of different profiles: infrastructure related, excessive tax control, lack of access to bank credits. Plus, as for the latest two they come into a vicious circle type relationship with the above already mentioned bank credits' high costs. Last, but not least, unfair competition of larger companies and not only and the hard competition of imports complete the circle of difficulties and determinants of the current stagnation of the Romanian SMEs' development.

**Table no.4 The SMSE's activity financing**

1	self-financing	69.54%
2	bank credits	25.88%
3	supplier credit	24.93%
4	grant funds	16.85%
5	leasing	13.34%
6	more	3.64%
7	loans secured by funds	2.16%
8	loans from financial institutions	1.75%
9	factoring	1.48%
10	issue of shares on the capital market	1.48%

*White book of SME in Romania , 2019.*

Recall from above the SMEs' declared difficulties related to bureaucracy, credits access and their high interest levels to be paid, this time for the hierarchy of *financing sources* of their activities. Or, the first in order here is the company's own resources – i.e. for 70% of those interviewed. This financing source is followed, although at a significant distance, by bank and supplier's credits – i.e. so declared by 25% of companies interviewed. Or, another immediate conclusion here regards the truth that neither the State, nor its banking system come up here with their specific aids, facilities or bureaucracy reducing.

**Table no. 5 -Forecasting activities of the SMSE, (as declared by)**

SMSE	2018	2019
Annual plans	39.77	37.22
Strategic approaches for 2-3 years	10.42	16.25
Strategies-plans for 3-5 years	8.30	9.86
No forecast	41.51	36.67
Total	100.00	100.00

*White book of SME in Romania , 2019.*

The inertial state in which this system of enterprises is situated also results from the fact that most of them – i.e. a little more than 70% of those interviewed -- did have neither annual development plans, nor forecasts for their future evolution at the time of the survey (2019). Though, there are companies with such plans and forecasts for 2-3 and even 3-5 years on in this country.

**Table no.6 - SMSE's objectives for the following years, (as declared by)**

SMSE	100.0
Moderate business expansion	56.58
Rapid expansion	10.64
Closing the business	3.08
Maintaining current dimensions	24.93
Size reduction	1.54
Selling the business	3.22

*White book of SME in Romania , 2019.*

As for activity objectives of Romanian SMEs the same CNIMMPS' study mentions as high as 56.58% of such respondent companies expecting some moderate business enlargement although not necessarily as primary activity objective, but as natural consequence of the whole activity. Actually, 10.64% of respondents thought at business' quick expansion mainly basing on some pattern of marketing plan related to products and/or services diversifying and so to new technologies attracted. Other entrepreneurs wish to rather maintain their existing business size – i.e. 24.93% of respondents to reduce it ; 1.54% to close it; 3.08%; finally sell it for some profit 3.22%.

*White Paper of SMSE* finds the main informatics technology items of these as being: PC (82.21%), the Internet (78.17%), e-mail applications (71.7%), the company's own website (35.58%), on-line transactions done (22.64%) and company's own Intranet network (16.31%). Only 9.57% of Romanian SMEs seem not to use any of these. These ones mostly are more than 15 years old (10.97%) and much less belong to the new ones (7.19%). And activities directly using the Inter- and intra-net are: communication with suppliers and customers (50%), information flows from business environment (40.43%), products' and services' promotion (36.39%), electronic transactions and payments (35.04%), communication facilities within organization (33.02%) and others (0.54%).

#### **4. Conclusions**

The last years prior to the current health crisis were the ones of investments' slowdown anyway and this for all main sectors: large and small companies and the public sector. Moreover, these investments don't seem to connect to consumer's needs. As the result the last redirected to imports with naturally harsh effects on the external trade balance and

balance of payments, although it was equally about a good economic growth in Romania – i.e. this based on consumption and imports, instead of home investments.

Gross fixed capital formation (GFCF), in its turn, correspondingly met low percentages, i.e. among the last by country ones in the EU area, while investments in tangible assets, as a distinct investments category, rather tried and succeeded to keep their value constant – i.e. technical capital replaced. Or this means less and less newly created economic value, the same for innovation. Plus, all these together with disturbing the external economic equilibrium, to which low performing of home firms in exportation gets added. The other performing of domestic firms, the one for the domestic area, looks equally embarrassed by the imports' competition.

*Business opportunities* appear rather generous in the SMSE zone – some of these above seem even contrary to the theory, the last see them rather on the big companies side, e.g. the last could be able to access them due to their *economies of scale*. The rate of firms following *growth-extension of activity (activities)* barely exceeds that of firms following their *bankruptcy. Activity reduction*, in its turn, seems more desirable than even keeping activity-production *parameters constant* – it is true that either such a destructive difference isn't too high, or SMSE are assumed to found of activity extension rather in theory .

*Difficulties* found are more numerous than business opportunities of SMSE, while though the series of such difficulties (19 items) looks to be almost all that these firms are really afraid of . It is equally interesting the way that the highest difficulty is identified in the own employment zone.

Most Romanian SMEs either lack *foresight* or prefer just annual plans for their activities. Extension of forecast terms is of decreasing concern of SMEs.

Self-financing seems to be the main *financing* way available to SMEs to make investments – plus, self-financing exceeds the other two credit financing ways, as cumulated, the bank and supplier credits ( *Ionescu A.,2018*)

In such a context it seems surprising and gratifying that *grants* equally do exist in the Romanian economic landscape and yet to a greater extent than some other activity and investments financing ways. Just think about this is a zone of not too much of : loans secured by funds, loans from financial institutions and factoring. Last, but not least, Romanian SMSE do not seem too much concerned about issuing new shares, either – e.g. in order to counteract difficulties, as above (Table 4).

The most relevant conclusion about Romanian SMSE might be that they prefer or are constrain by business environment and difficulties, to stay at constant parameters for longer time terms.

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