

## **SMEs between Truth and the Political Approach The Future of the SMEs in Romania**

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**Abstract.** The paper deals with the idea that is it a great difference between the European approach for the SMEs and the Romanian one. The analysis of the paper is based on comparisons between EU27 as a whole and Romania and other representative Member States and Romania. This analysis is focused on the finding those ways of action in order to support the development of the SMEs in Romania and in the EU.

A distinct part of the paper analyses the impact of the global crisis on the SMEs in different Member States and in Romania. This crisis supports the idea that the SMEs represent the growth engines of the EU economy, but the national legislation is far away to be able to promote their development.

An interesting part of the paper is connected to the EU promises made in the last years with the revised Small Business Act and the EU 2020 Strategy connected to it.

Starting October 2011, a plan for the SMEs' access to finance involves the introduction of a long-touted initiative to facilitate the venture capital for the SMEs across the Europe.

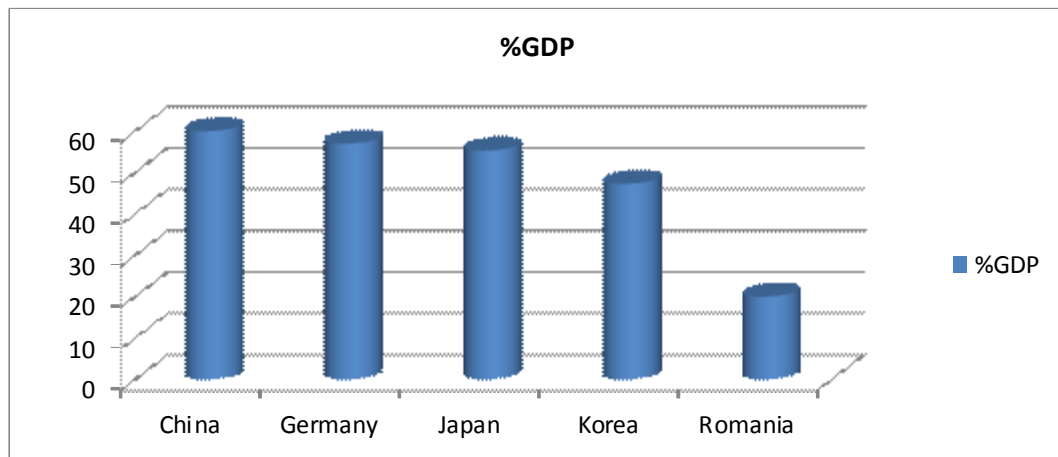
The main conclusion of the analysis is that the exit of the Romanian SME sector from crisis has to be based on political stability, reducing taxation, state aid and accessing support from the EU funds.

The analysis in the paper is followed by the latest pertinent official statistical data and diagrams.

**Keywords:** consolidation and austerity programmes, access to finance, convergence and cohesion regions, business environment top.

### **1. Introduction**

It is a unique approach to consider the SMEs as the main contributor to the GDP nowadays. The percentage contribution of SMEs to the GDP/total value added ranges from 60.0% in China, 57.0% in Germany, 55.0% in Japan and 50.0% in Korea (Normah M.A., 2007).



**Figure 1** SMEs contribution to GDP

During 2007-2010, the number of the European SMEs grew by over 2 million. The total number of SMEs in Europe is over 23 million (SME Performance Review, 2010).

SMEs' contribution to employment growth (84%) has been much larger than could be expected from their share in total private employment (67%), and 9.4 million jobs were created in the SME-sector between 2002 and 2008, for example (ec.europa.eu, 2010).

Nowadays, the SMEs support 50% of the GDP in high-income countries (Ayyagari et al., 2007). Moreover, about 75% of the formal workforce is employed by SMEs in the OECD countries (Thorsten et al., 2008). In 2010, the SMEs supported 57.9% of the value added and accounted for 67.4% of the employment in the EU27 (Dietrich, 2010).

According to the National Development Plan 2007-2013, Romania defines the 1<sup>st</sup> Priority as Increasing economic competitiveness and development of knowledge-based economy: the growth of the SMEs contribution to GDP by 20% still 2015. This contribution is far away from the EU average.

## 2. SMEs in the Central and Eastern Europe

SMEs represent a major player on the Central and Eastern Europe markets; they play the main role of the employer and the largest contributor to the GDP of the countries in the region. The financial crisis affected these players by evaporation of the internal and external demand, reducing the market liquidity and credit crunch, which had in many cases the role of a "death sentence" (Rosca M., 2009).

The global crisis beat many SMEs in the EU27 Member States. The only exception is Poland, where SMEs bankruptcies number is much lower. Romania is one of the most affected Member States, given that the first six months of 2009, for example, over 1/6 SMEs went bankrupt. These companies resorted to various cost reduction measures such as layoffs, wage cuts and reducing administrative costs, in order to stay on the market. All these measures are likely to remain without result if in the near future the demand will not return, and the banks will not open their doors to the credit.

In Poland, about 65%-70% of banks reduced the credit availability for the SMEs in the second quarter of 2009 (both short and long term) and planned to maintain drastic measures despite increasing demand for financing. The loans these companies benefited before the crisis remained only a memory nowadays. According to Thomson Reuter's news agency, 9 million Poles, or 70% of the workforce, are employed by companies with less than 250 employees. The SMEs achieved 50% of the Polish GDP on a market of 38 million consumers. The same SMEs support 15% of the budgetary revenues

from VAT and excise tax revenues. During 2008-2010, the SMEs bankruptcies rose, but in lesser extent than in other states. The SMEs sector was hit by the falling demand and the credit crunch and there are just few chances to have a better situation in 2011.

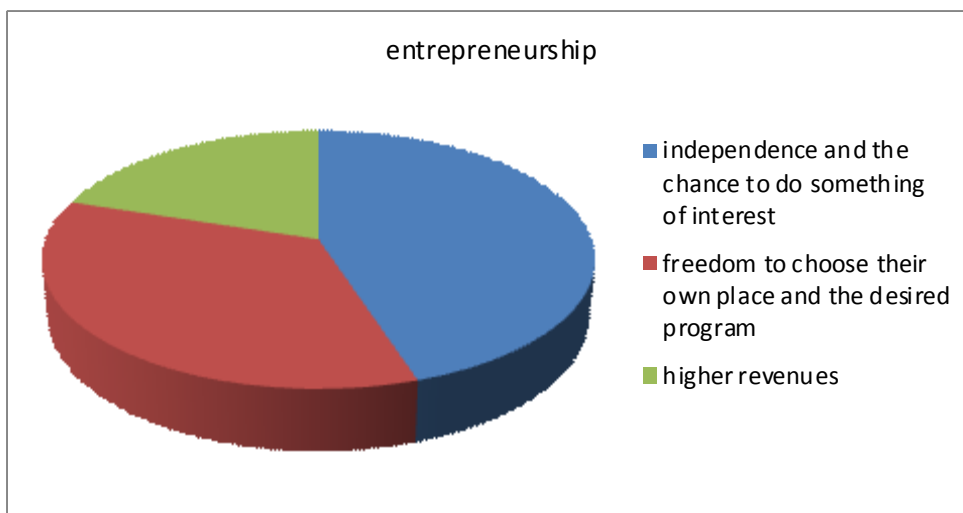
According to the Hungarian Statistical Office, 60% of the active labour (1.1 million persons) is engaged in the small sized companies with up to 249 employees. The SMEs sector's contribution to the industrial output is 26.1%, on a market estimated at 10 million consumers. The same SMEs cover 50% of the Hungarian GDP. In Hungary, the SMEs were affected by the evaporation of the demand and the reduced access to financing, but unlike Poland, the current situation shows no improvement. As a result, the industrial production continues to be 20% lower than in 2008, and the SMEs fell by a fifth.

In the Czech Republic, the high turnover to have a SME is 50 million Euros. The SMEs cover 80% of the Czech GDP and represent the main economic engine. But 20% of employees were redundancies in the SMEs during 2008-2010. The Czech Union of the SMEs announced that the access to credit is the main problem facing the sector. Lack of funding leads to the investment plans postponement or cancellation.

The Romanian SMEs covered 70% of GDP in 2010. Each year, 90,000 firms occur in Romania, while about 40,000 are out of business. Most companies faced falling sales between 21% and 50% during 2008-2010. In Romania, the difficult economic situation led to the number of bankruptcies increasing. Among the measures that companies are taking to relieve the economic crisis are: the administrative expenditures decreasing (36%), the employees decreasing (19%), employee incomes decreasing (9%) etc.

**3. The present European approach of the SMEs**

Europe has about 23 million SMEs, two thirds of the total private workforce and 80% of the new jobs. The European SMEs are about 99.8% of all companies, and they cover 58% of the VAT. About 92% of SMEs use less than 10 employees. The preference for entrepreneurship in Europe is 45%, while in America is 55%. Moreover, the positive perception of the entrepreneurs is less common in Europe than in the USA: 49% versus 73%.

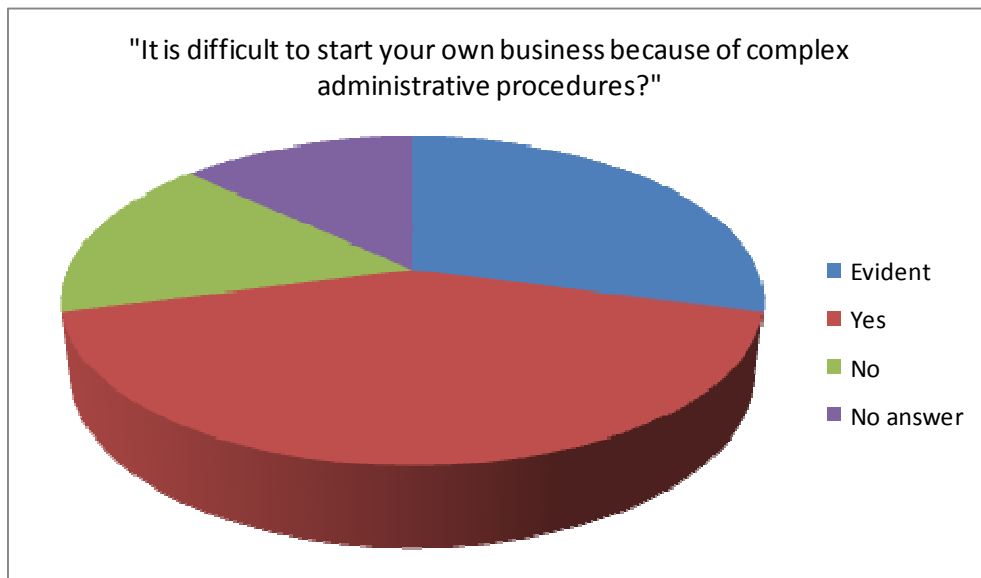


**Figure 2** European citizens incentive to entrepreneurship  
Source: personal contribution using a Eurobarometer survey

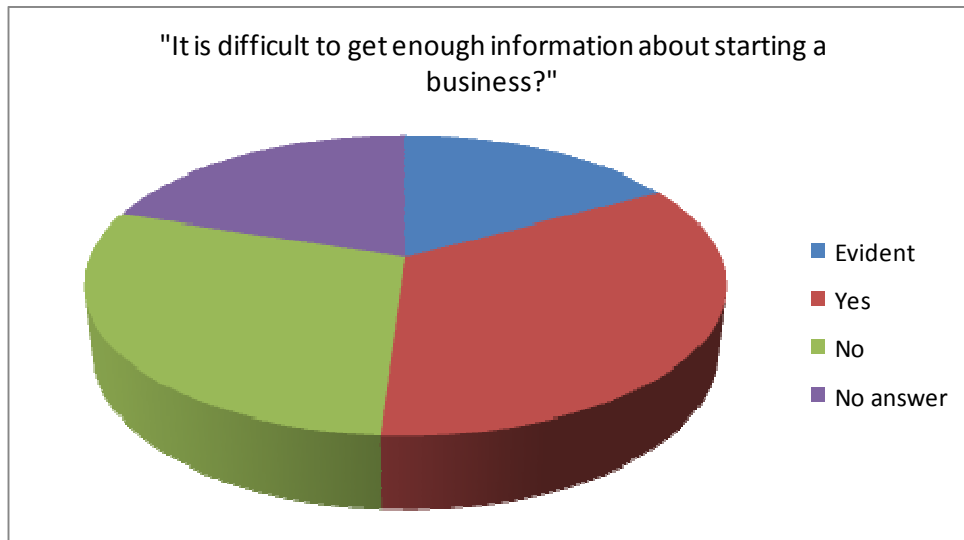
The European citizens feel that to become an entrepreneur is hard. A Eurobarometer study made in 2010 across the EU27 found interesting answers at some specific questions (Gubandru C., 2010).



**Figure 3** Answers to 1<sup>st</sup> question  
 Source: personal contribution using a Eurobarometer survey



**Figure 4** Answers to 2<sup>nd</sup> question  
 Source: personal contribution using a Eurobarometer survey



**Figure 5** Answers to 3<sup>rd</sup> question

Source: personal contribution using a Eurobarometer survey

In order to support the SMEs, was organized the European Week of SMEs in 2010, as a pan European campaign which took place in 37 participating countries. The events were organized at national, regional or local level by business organizations able to assist qualified organizations and by national, regional and local authorities from the participating countries.

In July 2011, the European Association of Craft, Small and Medium-sized Enterprises/SMEs discussed the future EU 2014-2020 budget in Brussels. This objective was proposed by a lot of significant institutes (the EESC, the European Commission, the European Investment Fund and the Polish Presidency of the EU).

According to this approach, an old idea was re-discussed: the revision of the Small Business Act. The need of a change in this Act is supported by key role played by the SMEs in the EU 2020 Strategy. If we want to extend this connection, we must talk about the EU budget, as well. The EU budget is able to support initiatives for innovation, resource and energy efficiency, for labour and training.

The great challenge is that the EU 2020 strategy cannot be implemented without important financial resources. Nowadays, the global crisis made necessary to reallocate resources in order to support the economic recovery process. These resources decreased under the austerity programmes focused on the public finances' stabilisation. Under the new economic context, the SMEs become the main engine of the economic recovery and the collaboration with them is more than necessary.

#### 4. SMEs in Romania

Romania dropped seven places in the World Bank's annual business top, up to position 72 of the 183, mainly due to the introduction of the "tax record" for the head office of a company before its registration (World Bank, 2011). The provision the expert financial institution referred was introduced in July 2010.

On the other hand, the introduction of the electronic payment system and the unified system of declaration of the social security contributions, the abolition of the annual minimum tax imposed on the companies and the insolvency proceedings shortening are listed as positive factors for business in Romania.

Among the criteria taken into account in determining the "ease" with which to do business, Romania stands the best in terms of access to the credit, which ranked 8 in the world. Romania ranked 63 in the world after easily setting up a new company, down from last year. Setting up a business requires an average of six procedures, takes 14 days, cost 3% of the average income per capita and requires a minimum capital of 0.8% average annual income per capita. The average annual gross income per capita which in Romania was, according to the World Bank report, 7,840 USD.

The access to electricity is one of the weaknesses of the business environment in Romania. Drawing power from a new company headquarters involves seven steps, takes 223 days and costs 556.9% of average income per capita. These entire the Romanian economy in the world ranked 165 in terms of ease with which companies can obtain electric power.

The fees payment is also a chapter in which Romania has problems, although the improvement done in 2010, now occupying position 154 in the world. The SMEs must make an average of 113 payments per year, which lost 222 hours, more than nine days, and transfer 44.4% of their profit.

The ease of obtaining a building permit is also problematic for SMEs in Romania, placing the domestic economy on 123<sup>th</sup> rank in the world. According to the World Bank report, the obtaining a building permit requires 16 steps, 287 days and cost 73% of the average income per capita.

Regulation of the insolvent improved significantly from an year earlier, but Romania remained in the second half of the league after this criterion ranking 97. The bankruptcy resolving takes three years and four months, costs 11% of the company assets and the recovery rate for creditors is only 28.6%.

Romania has a better rank (46 in the world) according to the investors' protection, due to the high transparency enjoyed by the companies' shareholders. The degree to which managers are held accountable and the ease with which the shareholders may bring lawsuits in court remain the points to this chapter.

The ease with which may be imposed the contract terms ranked Romania 56 places in the world, although one has to go through 31 procedures for this purpose, to lose 512 days and spend 28.9% of the debt they are trying to recover .

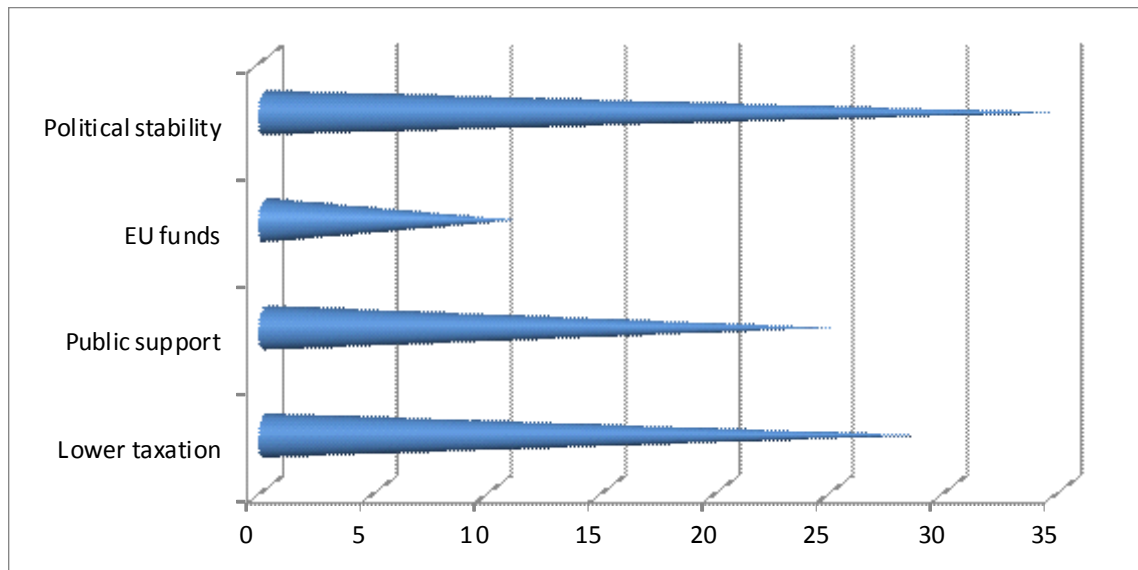
The property registration requires eight procedures, lasts about 26 days and cost 1.2% of the property value. The procedure is simpler in 69 countries.

Regarding the foreign trade, Romania ranked 72 in the world. The export requires 5 documents, lasts 12 days and cost 1,485 USD per container, while imports need 6 documents, 13 days and 1,495 USD per container.

Across the world economy, Morocco achieved the strongest improvement in the business conditions, managing the largest number of reforms, according to the World Bank study. Morocco thus went top 21 positions, to number 94. Moldova is the second best among the developments, climbing 18 places to 81. Singapore kept top position as the most favourable business environment, followed by Hong Kong, New Zealand, USA and Denmark. South Korea and Iceland managed to enter the top 10.

**5. Conclusions and solutions**

The National Union of the Romanian Employers conducted a survey during a sample of 2000 managers of SMEs with up to 100 employees, with a margin of error of 2.5% (UNPR, 2009). According to this survey, the managers believe that the political stability, the taxation reducing, the state support and the EU funds accessing represent the main ways for the SMEs to face the present global crisis.



**Figure 6** Out of crisis solutions  
Source: personal contribution using UNPR data

The representatives of the SMEs find it absolutely necessary "to pay particular attention to those businesses which are the initial and intermediate links of the value chain" and "to urgent the adoption of concrete and effective measures" able to ensure:

- a. SMEs placement at the heart of national policy, as an essential element of the economic system;
- b. improving the SMEs access to finance and lending by banks and unlock other financial organizations, including the facilitation of loans guaranteed by the state for entrepreneurs;
- c. taxation reducing and development stimulation of the new SMEs, including the one staying away from tax incentives to ease the financial situation of firms: VAT payment collection, lower social security contributions, lower excise duty on gas, and fuel;
- d. implementation of the EU's commitment to simplify the administrative tasks;
- e. creation and implementation of the Community instruments to promote capitalization, networking, investment and training of personnel in SME's;
- f. promoting and supporting the business services;
- g. ensuring adequate competition conditions for the SMEs in Romania reported to the European and the global market competition conditions.

All these above measures were stipulated into the National Forum of SMEs resolution (FNIMM, 2009).

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