

SMEs – THE MAIN PILLAR OF ANY ECONOMY

Adrian UNGUREANU¹, Anca UNGUREANU²

¹ *Spiru Haret University, Faculty of Economic Sciences Bucharest, 46 G Fabricii Street, Bucharest, Romania, Phone: 0722699064, Email: adrian.ungureanu@siveco.ro*

² *Spiru Haret University, Faculty of Economic Sciences Bucharest, 46 G Fabricii Street, Bucharest, Romania, Phone: 0729446523, Email: se_ungureanuan@spiruharet.ro*

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Abstract

Micro, small, and medium-sized enterprises (SMEs) account for 99% of EU businesses. They provide two-thirds of private sector jobs and contribute more than half of the total added value created by EU businesses. SMEs play an important role for economic and European growth, producing 60% of the European GDP. In addition, SMEs play a major role in the innovation process and thus constitute an important element for a knowledge-based economy. At European and national level, various action programs have been adopted to support SMEs, with the aim of increasing the competitiveness of SMEs through research and innovation and improving their access to finance.

Keywords: *SMEs; competition; innovation; job creation.*

JEL Classification: M10

Introduction

Micro, small and medium-sized enterprises play an essential role in the European economy. They represent a source of entrepreneurial skills, innovation and job



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creation. In the European Union, in 2015, approximately 23 million SMEs provided around 90 million jobs and represented 99% of all enterprises, according to data provided by the European Parliament. [<https://www.europarl.europa.eu/factsheets/ro/sheet/63/intreprinderile-mici-si-mijlocii>, European Parliament, 2019]. SMEs operate mainly at national level, relatively few of them are engaged in cross-border commercial activities within the EU. However, regardless of their scope of action, SMEs are subject to EU law in various fields, including taxation competition and company law. The definition given by the SME Commission can be found in European Parliament Recommendation 2003/361/EC.

Literature Review

In 1996, the European Commission adopted a recommendation establishing the first definition of SMEs. This definition has been applied throughout the European Union. On 6th of May 2003, the Commission adopted a new recommendation, taking into account the economic development since 1996. This recommendation entered into force on 1st of January 2005 and will be applied to all policies, programs and measures initiated by the Commission for SMEs. For the Member States, the use of the definition is voluntary, but the Commission recommends that they, and the European Investment Bank and the European Investment Fund, use it widely. The new definition is more appropriate for the different categories of SMEs and takes into account the different relationships between companies, helps to promote innovation and develop partnerships, while ensuring that only the companies that need help will be the target of public programs.

The definition given by the European Commission, in 2015, for SMEs is the following: “The category of micro, small and medium-sized enterprises (SMEs) is made up of companies with less than 250 employees and whose annual turnover does not exceed EUR 50 million, and/or whose total annual balance does not exceed EUR 43 million.” (Excerpt from Article 2 of the Annex to Recommendation 2003/361/EC).

In Romania – according to the Romanian legislation (Law No. 346 of July 14th, 2004 with subsequent amendments and completions): “For the purpose of the present law, the enterprise means any form of organization of an economic activity and authorized according to the laws in force to perform acts and deeds of commerce, for the purpose of obtaining profit, under conditions of competition, respectively: commercial companies, cooperative societies, natural persons who carry out economic activities independently and the family associations authorized according to the legal provisions in force.”



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Small and medium-sized enterprises (SMEs) are the engine of the European economy. They lead to job creation and economic growth and guarantee social stability. In 2015, over 23 million SMEs provide 90 million jobs across the EU. Nine out of ten enterprises are SMEs, and all SMEs generate two out of three new jobs. SMEs also stimulate entrepreneurship and innovation throughout the EU and are therefore crucial for boosting competitiveness and employment.

SMEs in the European Union still have lower productivity and slower economic growth than those in the United States. In the United States, surviving enterprises increase their workforce on average by 60% during the first seven years of existence, while in Europe, the number of employees increases from 10% to 20%. SMEs still have to deal with market failures, which worsen their operating conditions and competition with other actors, in areas such as finance (especially venture capital), research, innovation and the environment. Thus, about 21% of SMEs report that they have problems with access to finance and in many Member States this percentage is much higher for micro-enterprises. Also, European SMEs that successfully innovate are fewer than large companies. The situation is aggravated due to structural difficulties such as lack of managerial and technical qualification, as well as the remaining rigidities in the labour markets at national level.

The role of SMEs in the European economy has been repeatedly recognized at the highest political level. The European Council, in March 2008, strongly encouraged an initiative called the “Small Business Act” (SBA) for Europe, which aims to further the growth and sustainable competitiveness of SMEs, and called for its rapid adoption. The review of the European market also insisted on the need for further initiatives to better adapt the single market to the current needs of SMEs, in order to enable them to achieve better results and increase profits. Last but not least, the public hearing and the online consultation, organized to prepare the SBA, confirmed the need for a major policy initiative aimed at fully unlocking the potential of European SMEs. This is why the Commission has taken a decisive step forward by presenting an initiative in favour of SMEs, called the “Small Business Act” (SBA) for Europe.

Theoretical Background

In a single market without internal borders, it is essential that measures to encourage SMEs be based on a common definition, in order to improve their consistency and effectiveness and to limit distortions and competition. This is even more necessary given the interaction between national and EU measures to support



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SMEs in areas such as regional development and fundraising. Financial markets often fail to secure the necessary financing for SMEs.

In recent years, some progress has been made in improving the availability of financing and loans for SMEs, by providing loans, guarantees and venture capital. European financial institutions – the European Investment Bank (EIB) and the European Investment Fund (EIF) – have stepped up their SME operations.

Dynamic entrepreneurs are particularly well placed to take advantage of the opportunities of globalization and accelerate technological change. Therefore, the ability of specialized institutions to capitalize on the growth and innovation potential of small and medium-sized enterprises (SMEs) will be decisive for the future prosperity of the EU. In a changing global landscape, characterized by continuous structural changes and increased competitive pressure, the role of SMEs in our society has become increasingly important as creators of employment opportunities and key actors in the prosperity of local and regional authorities. Dynamic SMEs will strengthen Europe in the face of uncertainty caused by current globalization. This is why the EU has placed SMEs at the centre of the Lisbon Strategy for growth and jobs, especially since 2005, the year in which the partnership approach was used, with tangible results. The needs of SMEs are set among the priorities of EU policy and transposed in reality by the vision of EU heads of state and government since 2000 – to provide SMEs with the best environment in the world.

SMEs not only contribute to the wealth of local economies, but from a socio-economic point of view, in some economies, SMEs also play an important role in determining social changes, slowly contributing to the development of market economies as opposed to planned savings. They generate a change in the image of entrepreneurship: repositioning small business owners, moving them from the sphere of associations without a future to potential successful companies.

However, over 30 years of globalization have made markets increasingly competitive, by increasing the difficulty of doing business successfully, but also opened markets to opportunities due to increased fragmentation, which allows companies to specialize their offer to appeal to different and more demanding customers. Small businesses face the big challenge imposed by their limited size: a limitation in available resources. [Cacciolatti & Soo Hee, 2015]

Seeking to improve the competitiveness of SMEs is not only about understanding problems confronting businesses in this sector; it is also about a better understanding of how to overcome these barriers. Much research has focused on SME



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competitiveness and has sought to identify factors, which make some SMEs successful, while others fail to grow or go out of business. [Jones & Tilley, 2003]. SMEs operate in very different national and local environments and are themselves of a very diverse nature (including artisanal enterprises, micro-enterprises, family-owned enterprises or social economy enterprises). Policies targeting the needs of SMEs should therefore take full account of this diversity and fully respect the principle of subsidiarity.

Paper Content

The role of SMEs in the European economy has been repeatedly recognized at the highest political level. The European Council, in March 2008, strongly encouraged an initiative called the “Small Business Act” (SBA) for Europe, which aims at further enhancing sustainable growth and competitiveness of SMEs, and called for its rapid adoption. The Single Market Review also insisted on the need for further initiatives to better adapt the single market to the current needs of SMEs in order to enable them to achieve better results and increase profits. Last but not least, the public hearing and the online consultation, organized to prepare the SBA, confirmed the need for a major policy initiative aimed at fully unlocking the potential of European SMEs. This is why the Commission has taken a decisive step forward by presenting an initiative in favour of SMEs, called the “Small Business Act” (SBA) for Europe. At the basis of the European SBA is the belief that achieving the best possible framework conditions for SMEs, implies first and foremost that the importance of entrepreneurs is recognized by the company. Although a multitude of factors is hypothesised to impact on business outcomes, there is no consistent pattern to the characteristics, which contribute to business competitiveness, success and growth. [Gibb, 1996] The general climate prevailing in a society should lead people to consider with interest the possibility of creating their own society and to recognize that SMEs contribute substantially to job growth and economic prosperity.

In order to create an enabling environment for SMEs, it is therefore essential that the perception of the role of entrepreneurs and risk-taking change in the EU: the entrepreneurial spirit and the willingness to take risks should be applauded by policy-makers and the media, and encouraged by administrations. In general, the dominant policy should be the one that creates favourable conditions for SMEs [Heitor, 2019], based on the belief that the rules promulgated must respect the majority of those who apply the principle: “Think small first.” The SBA builds on the strategic



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achievements of the Commission and the Member States, creates a new strategic framework that integrates existing business policy instruments, and is particularly inspired by the European Charter for Small Business and Modern SME Policy. In order to implement this ambitious strategic agenda, the Commission proposes a genuine political partnership between the EU and the Member States, respecting the principles of subsidiarity and proportionality.

In 2018, micro-enterprises in Romania concentrated only 14% of revenues, compared to 26% 10 years ago, although their share is 96%. Large companies – although they represent as weight only 4% of the total active companies – have reached to concentrate 86% of the revenues, according to the information provided by the Association of Financial-Banking Analysts of Romania (AAFBR). [<https://www.aafb.ro/>] Small companies have suffered because their low competitiveness has been outpaced by the fifteen consecutive increases of the minimum wage in the economy, over the last decade, fuelling the rising costs.

The analysis regarding the evolution of microenterprises active in Romania shows a modest increase, in 2018, of the profitability of companies with incomes below one million euros, these registered constant losses in the period 2008-2014 (57 billion lei), while the profits reported in 2016, 2017 and 2018 were very modest, of almost 7 billion lei, according to the same sources (AAFBR).

According to Ziarul Financiar [www.zf.ro], Romania is in the last place in the EU after the number of SMEs, with 29 businesses/1,000 inhabitants, half compared to the European average. Almost 500,000 SMEs are active on the local market, out of a total of over 25 million small and medium-sized enterprises at EU level, shows the latest analysis of the European Commission valid at the level of 2018. SMEs account for 99.8% of all EU firms in the non-financial sector, with a similar share in Romania.

“The importance of SMEs in the economies of the member countries varies greatly. For example, the EU average in 2018 was 58 SMEs per 1,000 inhabitants, but at the level of member countries there were strong variations, from 29 small and medium-sized enterprises in the case of Romania, to 115 in the Czech Republic,” according to one European Commission annual report. The local market is not only the last place, but also far from the next ones, namely Germany (35 SMEs per 1,000 inhabitants) and Great Britain (38 SMEs per 1,000 inhabitants).

What is interesting to note, however, is that the countries in the region of Central and Eastern Europe, those with which Romania is “struggling” in terms of



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development, average wages or GDP per capita are actually much better placed in terms of regards the indicator of the number of SMEs per 1,000 inhabitants.

According to the data provided by the National Institute of Statistics, [Intreprimeri mici si mijlocii in economia romaneasca, www.insse.ro, 2019] we have the following situation, regarding the contribution made by SMEs in the main branches of the Romanian economy:

1. **SMEs contribution in industry:** At the end of 2017, a number of 54,186 small and medium-sized enterprises were operating within this sector. The profit registered in the industry, at the level of 2017, was 25,206 million lei, of which 6,305 million lei were obtained by small and medium-sized enterprises.

2. **SMEs contribution in construction:** At the end of 2017, within this sector, a number of 52,792 enterprises were operating, of which 52,716 were small and medium-sized enterprises. 83.7% of total turnover was made in small and medium-sized enterprises.

3. **Contribution of SMEs in trade:** During 2017, a number of 172,238 small and medium-sized enterprises and 197 large companies, respectively, operated. Of the total, 172,435 enterprises, 99.9% were small and medium-sized enterprises. In 2017, 69.5% (380,109 million lei) of total turnover was achieved in small and medium-sized enterprises. From the total of 937,588 persons of the personnel, as of 31.12.2017, SMEs had a share of 77.0% (722,026 persons).

4. **Contribution of SMEs in services:** During 2017, there were 244,813 small and medium-sized enterprises and 541 large enterprises respectively in this sector. Of the total, 245,354 enterprises, 99.8% were small and medium-sized enterprises. In small and medium-sized enterprises, 68.9% (180,358 million lei) of total turnover was achieved. Of the total of 1,569,734 persons of the personnel number as of 31.12.2017, small and medium enterprises owned 68.3% (1,071,587 persons). Of the total number of personnel of 361,144, as of 31.12.2017, small and medium-sized enterprises owned 88.0%.

A set of four principles to guide the conception and implementation of policies at both EU and Member State level are essential to deliver added value at Community level, to put SMEs on an equal footing and to improve the legal and administrative framework throughout the EU:

1. Creating an environment in which entrepreneurs and family businesses can thrive and where entrepreneurship is rewarded;

2. Providing the opportunity for honest entrepreneurs who have failed to quickly get a second chance;



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3. Defining the rules according to the “Think Small First” principle;
4. Ensuring the responsiveness of administrations to the needs of SMEs.

Conclusions

The importance of SMEs derives from the following features: it offers new jobs, promotes innovation and flexibility, is practically set up in places where staff are improving and from where they can then move to large companies, stimulate competition, help the smooth functioning of large companies for which they provide different services or produce different subassemblies, manufacture products and provide efficient services.

Long-term success for any SME means that the innovation of new products, services and processes must be emphasized. Owners must strive to create a dynamic entrepreneurial culture, in which there is a constant emphasis on the importance of regular access to new knowledge, resources and information.

In this way, SMEs in all sectors can improve their prospects for long-term survival.

SMEs create jobs more efficiently than state investments, with a much lower cost than the budget and with a much greater social impact, because they involve family members and other local people. That is why the authorities must take the necessary measures to support this sector: to increase the amounts allocated for the programs for setting up and developing SMEs, to simplify the procedures regarding their access to the sources of financing, to create a debt rescheduling system. The development of small and medium-sized enterprises represents Romania’s chance to restart the engines of economic growth.

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