

## **Strategies for Internationalization of Romanian SMEs. Focus on the European Market**

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### **Abstract**

*The theoretical part of this paper is focused on presenting the main strategies of internationalization that can be used by SMEs in order to diversify their markets and enhance their profitability. The empirical research is aimed at presenting and analysing statistics regarding the performance of Romanian SMEs in relation to the average of overall EU SMEs. The purpose of this paper is to analyse the activity and performance of Romanian SMEs in relation with SMEs from other European countries. A set of concrete recommendations are formulated for creating a better economic and legal environment for small and medium enterprises from Romania that have set the objective of extending on other European markets or are in the process of internationalization of their business.*

**Keywords:** Small and medium enterprise (SME); Romania; European market; internationalization;

**JEL Codes:** D21; F23; L21;

### **1. Introduction**

The accelerated process of globalization in recent decades has determined the world economy to become increasingly integrated, strengthening the global business environment, beyond national and regional environment (Daniels, 2015). Globalization is defined in several ways, each reflecting a particular scientific or ideological position on the meaning of the concept. Two main approaches can be distinguished: globalization as a set of interdependencies - growing in recent decades - between national economies; the theory is based on considering national economy and the nation state as the basic structures of the global world and globalization as a progressive process of integration, mainly in the economic field, in a single system, structured on several levels: local (national), regional and global.

The internationalization of a company can be considered as a process with several stages, of progressive involvement in international affairs. A general model of this process includes four main stages - the internationalization of trade, the internationalization of production, company internationalization, globalization of business - each of them corresponding with specific forms of transactions and motivations. However, depending on its resources and objectives, a company can engage more or less deeply and sustainably into the international business environment (Popa, 1997).

The integration of European market, liberalization of markets, the evolution of ways of communication and exchanging information, the development of transport corridors and

technology are factors that have opened new horizons and created the proper framework for new business opportunities, not only for multinational companies operating globally but also for SMEs. The current opportunities and the pressure to internationalize are two sides of the same coin. Large companies fear they may not survive unless they become players in the international market, while smaller companies see a chance to develop faster if they extend outside the country.

## **2. Literature Review**

In recent decades, SMEs are considered to be key factor for growth, employment and economic competitiveness. According to OECD (2000) approach, SMEs are defined as entities with independent legal entities (non-subsidiary, independent firms), with a maximum number of employees; this number varies from country to country but usually the upper limit is 250 employees (North American classification, 500 employees). In other cases, financial criteria such as turnover or balance (balance sheet valuations) are used to define SMEs. The OECD estimates that small and medium companies represent about 95% of all firms (business) and have 60-70% of the employed workforce (Johnson and Turner, 2003).

According to Hollensen (2014) SMEs have three basic characteristics: the manner of organization - employees of SME work directly with the company owner / manager / entrepreneur, and they are easily influenced by them; risk taking - inexperience or lack of information about foreign markets involve decision making under risk conditions; flexibility - easy communication with customers allows the company to react in real time to their needs.

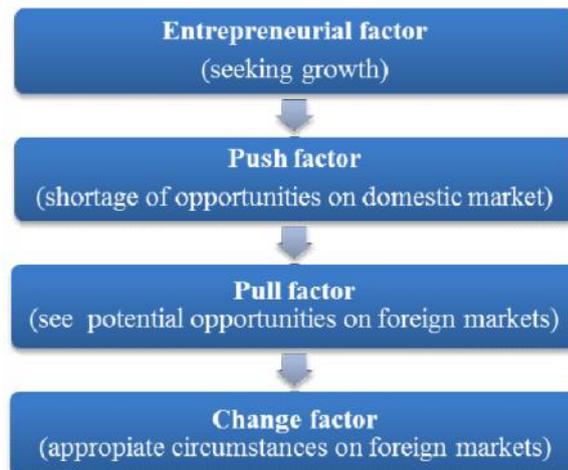
### **2.1. SMEs and the Internationalization Process**

The involvement of companies in international affairs is the result of management decisions, which are based on a number of reasons. In this regard, in the literature, a distinction is made between two types of motivations: proactive and reactive (Popa, 1997). Reactive motivations are the company's response to the pressures coming from the business environment, such as growing competition, decreased domestic sales, excess of production capacities, proximity to customers. Proactive motivations are based on the voluntary commitment of the company to international affairs in order to capitalize on comparative, strategic or competitive advantages. In the category of these factors we include: access to resources, cost reduction, technological advance.

According to Jansson (2007) the benefits of internationalization are mainly the opportunities to find new customers and benefit from economies of scale. Jansson (2007) stated that: "more home-market oriented small and medium-sized enterprises (SMEs) are internationalizing their business operations thus becoming more global".

The main motivation underlying the decision of SMEs internationalization is the increase of the company's competitiveness, mainly through access to new markets. In a report published by the OECD (2000), four factors that favour the internationalization of SMEs, are identified: entrepreneurial factor (seeking growth) – is the determining factor related to the manager's orientation to new markets; push factor – linked to the company's inability to increase on the local market; pull factor – identifying external market opportunities (a positive factor); chance factor, connected with taking advantage of new opportunities in a foreign market (see Figure 1).

**Figure 1: Internationalization Factors**

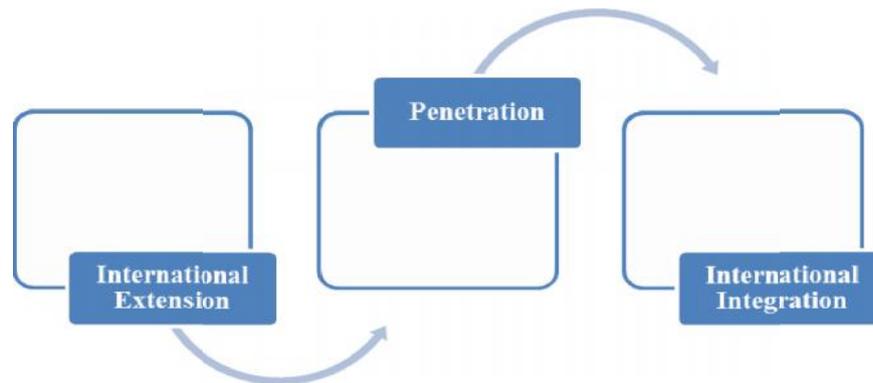


Source: Krzysztof, N., Daszkiewicz, W. (2012): Internalization of SMEs: Context, Models and Implementation, Gdańsk University of Technology, Gdańsk, p.15.

## 2.2. Internationalization Theories

The literature review revealed several approaches to the process of internationalization:

- **The Uppsala internationalization process model.** A model that focuses on the dynamic process of internationalization of a company is Uppsala model, called Model U. The main objective of applying Uppsala Model is to forecast the company development in foreign markets. Two elements underpin this model: the notion of sequentially attributed to the internationalization process and the concept of “physical distance”.
- **The theory of transaction costs.** One of the most important concepts used by Coase (1937) is the cost of presence on the market of companies. This concept will experience a significant development, being operationalized as the transaction cost. Williamson (2009) defines transaction costs, comparing them with frictions arising with the motion of objects in space: ex ante transaction costs - the identification of the relevant prices, negotiating contracts, advertising; ex post transaction costs - monitoring the behaviour of co-contracting parties, recovering damages if a party does not comply with its obligations, etc.
- **Dunning's eclectic paradigm** (1988, 1998) is a benchmark for analyzing the benefits arising from the internationalization process. Thus, Dunning has identified three types of advantages: specific benefits (economies of scale, diversification), location advantages (market size, infrastructure) and advantages of internationalization (keeping product quality, reducing operating costs in the market). The developed model is focused on the benefits induced by internationalization and less over the development process of companies' internationalization.
- **Network theory.** From the perspective of the network theory, the internationalization process is viewed as a consolidation of existing relationships and/or creating new relations on the international market, with exploitation, in addition of organizational and economic dimensions, of the social component of the network and the human dimension (see Figure 2).

**Figure 2: Network Approach to Internationalization**

Source: Johanson, J., Mattsson, L.G. (1988): Internationalization in industrial systems: A network approach, In: Hood, N., Vahlne, J-E., (eds), Strategies in global competition. Croom Helm, London, pp. 194-213.

- **International entrepreneurship theory.** According to McDougall and Oviatt (2000) international entrepreneurship is defined as “combination of innovative, proactive, and risk-seeking behaviour that crosses national borders and is intended to create value in organizations”. International entrepreneurship theory is based on the following statement: “individual and firm entrepreneurial behaviour is the basis of foreign market entry” (Mtigwe, 2006). Technological advance, easier access to information and better communication between representatives of countries can help SMEs to enter on foreign markets. The main factor of these theories is the entrepreneur.

In the internationalization process, the company has several options: the first option is the development of existing markets - the least demanding option, used for companies that operate on large competitive markets; a second option, the company can decide to develop on nearby new markets, similar in terms of business models with the ones on which they already operate - typically chosen in this case is the export option; a third strategy is developing a range of similar products to be sold on similar international markets - in this case, the company can opt for a strategic alliance: the establishment of joint ventures or licensing (Belu and C r gin, 2008).

### 2.3. Types of internationalization strategies

Companies that compete on the global market have to face two types of pressure: those related to costs and those related to location. On one hand, they have to achieve lower costs for outsourced production, internationalization being justified if it improves the company’s profitability. On the other hand, they must meet specific conditions in the host country, be sensitive and responsible in relation to local requirements (locally responsive) in order for the implantation abroad to be sustainable. However, local adaptation may incur additional charges – for commercial or technical differentiation of products that takes into account the local business environment (consumer preferences, business practices, distribution channels, competition conditions, government policies) - which conflicts with the imperative of increasing profitability.

In practice, taking into account the available capacities and the proposed objectives, each company will develop a strategy that would combine in a personal manner, on one hand, the pressure to reduce the unit costs through standardization with the need to adapt supply to the characteristics and dynamics of the market, by differentiating and on the other

hand, immediate gain with economic sustainability and the local, regional and global dimensions of the international business. Furthermore, if we consider the two conditions/restrictions of internationalization, in relation to the coordinates of defining international strategy, we can distinguish four basic strategies: international, multinational, global or transnational. Of course, the company that operates on the global market can adopt one of the basic strategies or may use a mix of elements from these strategies depending on the specific of the company, industry or business environment.

E-commerce is a way of internationalization that provides several advantages for SMEs. This solution reduces the costs of exchanging information, advertising and promotion, market research etc., increasing at the same time, the degree and extent of exposure of the company's image and its products to the general public. At the same time, the Internet enables SMEs to address global markets as well as the niche markets, easier and faster. In addition, SMEs are more flexible in terms of organizational structures than large corporations which manifest tendencies of rigidifying and bureaucratization. Higher flexibility and speed of response can compensate for the shortcomings determined by more limited resources. E-commerce companies, operating in the virtual field are released from spatial and temporal barriers that get in the way of efficient and rapid expansion of international operations. Digitization and virtual interaction are distinctive elements of the new economy.

### 3. Case Study: The Internationalization of Romanian SMEs in the European Union

A report of the European Commission (2015) showed an upward trend in the number of SMEs, which reached 21,646,395 in 2015, 93% of them being micro-enterprises (companies with less than 10 employees) with a number approximately 90 million employees. SMEs generate 58% of the added value generated by non-financial sector in the 28 EU countries (see Table 1).

**Table 1: Evolution of Active SMEs Performance in the EU28 Economy**

Year	2008	2009	2010	2011	2012	2013	2014	2015
Number of SMEs	21261849	20974190	21755376	21901107	21810243	21614919	21564839	21646395
Number of employees	90806273	90332632	89933916	90077618	89297328	88843465	88981523	89585622
Added value (ml Euro)	3622465	3273275	3425857	3570666	3626206	3666778	3769518	3899312

Source: European Commission (2015): Annual Report of European SMEs

The added value of SMEs operating in the European Union is produced mainly in industry (26.1%) and trade (19.2%), followed by other relevant sectors as professional scientific and technical activities (9.9%), construction (7.8%) and hotels & restaurants (3.4%). Other activities with smaller individual weights cumulate 33.6%.

According to a survey carried out by questioning a number of 9480 SMEs from 33 European countries on the process of internationalization, over 40% of SMEs were involved in activities that go beyond national borders. The results range from 30% of SMEs carried out imports, 2% of them have realized FDI, while 4% of them plan a way to internationalize their business. By internationalization of SMEs more jobs can be

created than if the companies would remain on the domestic market and imports are necessary for SMEs to become exporters. In order to be internationalized, SMEs can raise the level of preparedness through “e-learning system”, a new tool available to them to promote best practices, to raise awareness, to encourage cooperation between economic operators and national authorities for adding some practical elements to European legislation.

Another recent study conducted by The Economist Intelligence Unit (EIU) for DHL Express showed that most of the SMEs see growth opportunities internationally and expects that in the next five years, up to 50% of revenues their be obtained from foreign markets. Some barriers were identified for smaller companies that want to grow globally, such as political instability, cultural factors and inadequate infrastructure; excessive bureaucracy and lack of transparency of the system in which they operate and administrative costs remain reasons which discourage SMEs to enter new markets. Also, the study shows a gap in international activity among SMEs from developed markets and the ones from emerging economies: almost 69% of total SMEs from the group of most developed seven nations of the world (G7) conduct business on international markets compared to only 46% of total SMEs in BRICM countries.

According to the same study, five out of six SMEs (84%) believe that cultural barriers are the most important factor to be taken into account when the decision to enter a new market is made, which explains the tendency of small and medium to choose markets they are familiar with. From this point of view, SMEs from the group of countries BRICM will seek opportunities to expand into similar markets (emerging), while the SMEs from G7 countries are active in developed economies: 32% of G7 SMEs operate in Western Europe vs. 7% of BRICM SMEs; 15% of SMEs from BRICM have activities on the markets of Russia and CIS, compared to only 3.6% of SMEs from the G7; also, 18.5% of SMEs from BRICM operate on markets of South America compared to only 4.6% of SMEs from the G7.

According to a study (EIM/GDCC, 2009) on internationalization of SMEs supported by the European Commission, a considerable number of European SMEs are engaged in international activities, but only a small percentage involved in internationalization beyond the domestic market. The same study shows that the main barriers to internationalization can be classified into two categories: internal and external barriers (see Table 2).

**Table 2: Barriers to Internationalization**

Internal barriers	External barriers
The company's capacity	Business environment
High costs of internationalization	Lack of capital
The price of the company's products or services	Lack of adequate support from the state
Quality of the company's products	Lack of information
Qualified staff	High costs or complexity of documentation for transport
Specifications of products	Other laws and taxes in foreign countries

Source: own study

**Romania.** SMEs in Romania play a less important role than in other European countries, if we consider our country is on the last place in UE28 by the density of active SMEs and 17th place in terms of contribution to the added value created by SMEs. However, Romania has a remarkable good percentage on the number of employees that work in SMEs, leading to rank 8 of UE28.

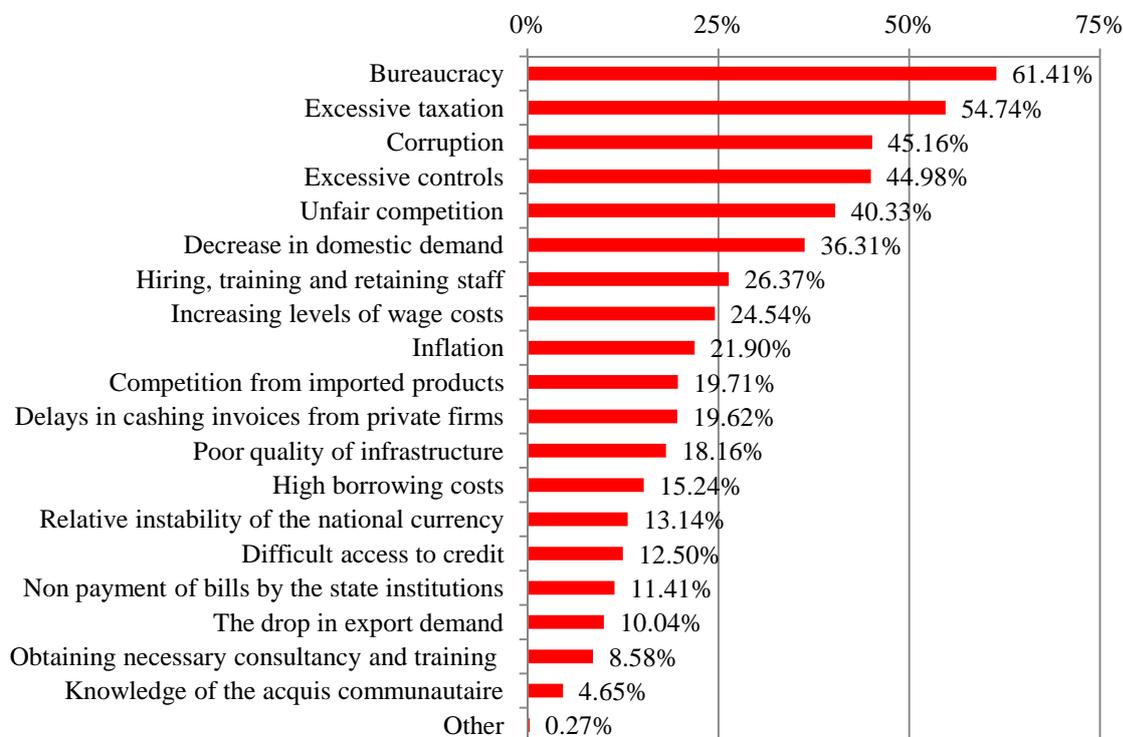
**Table 3: The Main Indicators of SMEs in Romania vs. EU28**

Type	Number of enterprises			Number of employees			Added value		
	Romania		EU 28	Romania		EU 28	Romania		EU 28
	count	%	%	count	%	%	bn. EUR	%	%
Micro	373944	87.40	92.40	931091	22.90	29.10	7	13.40	21.60
Small	44682	10.40	6.40	939499	22.90	20.60	9	16.30	18.20
Medium	7669	1.80	1.00	848216	20.90	17.20	10	19.70	18.30
<b>Total SMEs</b>	<b>426295</b>	<b>99.70</b>	<b>99.80</b>	<b>2708806</b>	<b>66.70</b>	<b>66.90</b>	<b>26</b>	<b>49.40</b>	<b>58.10</b>
Large	1455	0.30	0.20	1349456	33.30	33.10	26	50.60	41.90
<b>Total enterprises</b>	<b>427750</b>	<b>100</b>	<b>100</b>	<b>4058262</b>	<b>100</b>	<b>100</b>	<b>52</b>	<b>100</b>	<b>100</b>

Source: European Commission (2014): SBA Fact Sheet Romania.

Romania's economy is dominated by small and medium enterprises, but has proportionally fewer microenterprises than the EU as a whole, respectively 87.4% in Romania, compared to a rate of 92.4% in the EU. Despite an increase in the number of start-ups in recent years, the impact of microenterprises on the economy is still lower than the SME average, as they provide about 23% of existing jobs in the private sector and only 13% of value added in the economy (see Table 3).

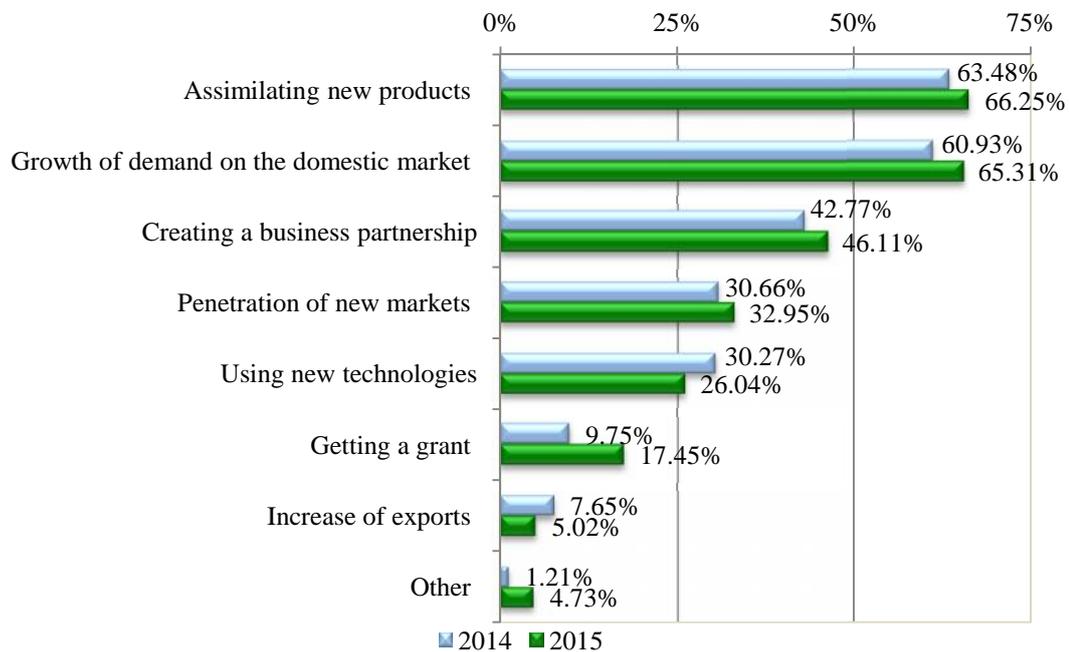
In Romania, a survey conducted by Post Privatization Foundation in 2015 revealed three aspects regarding the contribution of Romanian SMEs to the performances of SME sector in EU28: the lowest in the EU density of active SMEs (21 SME / 1000 inhabitants), 8th at the contribution in the total labour force of European SMEs (3%) and a 0.7% contribution to total value added, respectively 17th place in the EU28.

**Figure 3: The Major Difficulties Faced by Romanian SMEs in 2015**

Source: by the authors, using data from CNIPMMR (2016): Carta alb a IMM-urilor.

The latest research report conducted by CNIPMMR, SMEs White Paper 2016, based on 1096 interviews with entrepreneur's shows that the main positive effect of Romania's EU accession on SMEs is better access to foreign markets (45.99% of companies). The research also identified the main problems faced by SMEs in our country, namely: bureaucracy (61.41%), excessive taxation (54.74%) followed by corruption (45.16%) and excessive controls (44.98%). Other results: 81.66% of SMEs do not intend to access structural funds in the future; only 0.18% of enterprises received approval for the submitted project and approximately 71.99% of the investigated SMEs finances their economic activities by own sources. For a complete picture of both positive and negative aspects of the Romanian economic and political environment that influence the activity of SMEs see Figure 3 and Figure 4.

**Figure 4: Main Business Opportunities for Romanian SMEs in 2014 and 2015**



Source: by the authors, using data from CNIPMMR (2016): Carta alb a IMM-urilor.

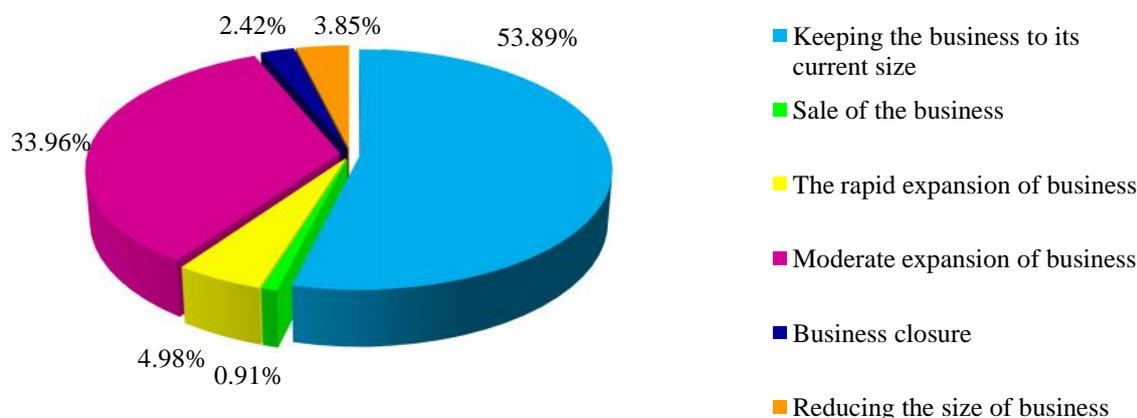
All these factors should be taken into account by Romanian governmental authorities so that they can implement the right economic and social policies for the development of SME sector in Romania. Based on the research conducted in this paper, some recommendations can be formulated for the next period, with the scope of improving the conditions for development of Romanian SMEs.

First of all, national programs should be implemented in order to facilitate the selling and distribution of Romanian SMEs products and services. There has already been an initiative regarding the obligation for large supermarkets and hypermarkets to commercialize Romanian agricultural products in a percentage of at least 51% on their shelves. Though this law was voted by the parliament it was very controversial among the retailers, some of them claiming that it was almost impossible to implement. We consider this to be just the first step in a long line of measures that can encourage the activity of Romanian SMEs, without limiting or discouraging any other companies from the EU. The importance of promoting national products on the Romanian market should be explained through local advertising campaigns that can influence the mentality of people.

Another important direction of action is that of proper access to financing for Romanian SMEs, both through national grants/European projects and credits. Sometimes the desire for growth of a Romanian small business is suppressed by the limited access to financial resources, which are vital both for motivating young well trained staff and for technologic development. Without proper financing, no start-up has high chances to become a very profitable business. Only rare great ideas can achieve success without medium or high funding available. We have to create a modern economy that can allow equal chances to success, to both genius idea and common ideas of people who want to make a difference, by offering good products or services, where they are required and at a fair price to the consumer. Innovation comes not only from great minds but also from practice and long tradition in a certain sector of activity. Good ideas for new or developing business should have the chance to receive financing either through national or European projects either through financial instruments offered by banks. The key to success is transparency for the important elements and less bureaucracy which often smothers good ideas with too much paperwork, making it impossible for untrained people to obtain financing. Another important instrument which is at the disposal of the government is the fiscal policy. We consider opportune to have more fiscal facilities for SMEs, as their development may bring more contributions in the future to the state budget.

The main Romanian SMEs objectives that were identified through a market research conducted by CNIPMMR in 2015 are presented in Figure 5.

**Figure 5: Main Objectives of Romanian SMEs for 2016-2017**



Source: by the authors, using data from CNIPMMR (2016): Carta alb a IMM-urilor.

As we can observe from the results of this research, most SME's managers do not have a positive vision on the future of their business, as less than 5% think they will experience a rapid expansion and over 50% of them think they will remain at the same size in the next couple of years. We believe that with the appropriate policies, they can be convinced that the economic environment in Romania can offer them a good chance for a sustainable development of their business.

## 4. Conclusions

Factors promoting globalization that directly impact SMEs are essentially the following: switching to the tertiary economy (economy based on services); changing the role of location in conducting business (geographic and economic flexibility), and the development and convergence of new technologies.

Small and medium companies, faced with increasingly intense competition in the local market have the choice to “internationalize” domestically through integration in the network of companies with international dimension through various forms of outsourcing - like production on order, subcontracting etc. - either to expand internationally (actual internationalization) both on its own and through alliances and cooperation with other companies of a similar nature.

Even though large companies have the dominant share in international business, small and medium enterprises lately represent one of the most dynamic components of internationalization.

Small and medium enterprises in Romania appear as a fragile segment of the overall European SMEs, presenting serious problems of competitiveness and big development gaps compared to the average performance of EU28 SMEs, gaps that were magnified in the post-crisis period.

Active measures should be promoted by the Romanian government and local authorities in order to encourage the development of SMEs by offering real support, as fiscal facilities, financing instruments and simplifying the bureaucracy that can act as a barrier to entering on the market.

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