

# The Role of Internationalization Activity for the SME's Development – Case Study for Transylvania Region

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*The development of SMEs sector is essential for the future of Romanian economy. Despite of a continuous increase as number, ponder in the total economy and turnover still the small firms are vulnerable and limited in the international market. The entrepreneurs are precocious in the internationalization process of their businesses. In this context our paper is concerned with studying the entrepreneurs' motives for developing these activities and their behavior in this process. The conclusions are based on evidence collected from 260 SMEs from Transylvania Region, second as importance in this sector from Romania, after the Bucharest. The way of entry in the international market specific for Romanian SMEs is import activity having a strong impact for their development.*

JEL Codes: M16, M13 and F10

## 1. Introduction:

The economic reforms applied in Central and East European countries have to emphasize on the role of SMEs because they are able to create an important number of new jobs, to stimulate competition for larger firms alike, to create a diversified and flexible industrial environment, to stimulate innovation, to improve industrial relations and to provide a superior working environment for employees inside of a national economy. Based on these features, the SME sector was considered a key factor for assuring the restructuring of the old centralized economies and maintaining economic dynamism.

After 1989, the Romanian economy restructuring should be understood in the general context that of the transition from a state owned economy to a decentralized economy. This was possible only by stimulating a large number of entrepreneurs which increased the competition for the large companies, have implemented innovations and contributed in this manner to a more performing industry.

During the last eight years Romanian economy knew an accelerating pace of growth, with a 5 to 8 % rate of the GDP growth, which placing Romania among the most dynamic European economies. Due to this situation the volume of foreign direct investments grew substantially as the preparations for E.U. integration of our country intensified.

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In 2006, as a result of business environment improvement and of the positive effects of unique income tax quote, the volume of foreign investments grew with 57,5 % with a total of 34512 million Euros. More than 70% of this is direct investments in Romania, especially in industry, as well as Greenfield investments, financial operations, insurance and commerce (wholesale and retail). As a consequence, after the first year of E.U. integration the rate of economic growth was of 6%, industry maintaining a growing trend this being a sign of economy's reindustrialization process consolidation.

In Romania, more than 99% of the active enterprises are small and medium size enterprises, the largest share being in the commercial services sector. There is a strong polarization of the SMEs on fields of business. Thus the first 7 activities: wholesale trade, retail, construction, wholesale trade and retail, maintenance and repair services for companies, food and beverages and transport, made about 70% of the total turnover. Of the total number of SMEs, microenterprises remain a representative segment.

Tabel no.1. The evolution of the SMEs share in the Romanian economy

YEAR	2000	2001	2002	2003	2004	2005	2006	2007
Total of active enterprises	313508	317555	322188	359399	404339	442868	471952	499857
SMEs total	311077	315149	319816	357071	402090	440714	469919	487682
SME's share (%)	99.22	99.24	99.26	99.35	99.44	99.51	99.57	99.54
Microenterprises share in total SMEs (%)	88,03	87,39	87,2	87,02	88,14	88,34	88,01	88,01

Source: Territorial Statistics, INS, 2008, NASMEC, 2009

A study on the competitiveness of Romanian SMEs for 2006, conducted by the National Authority for the SMEs Council (NASMEC), has revealed the accelerated but not sufficient evolution trend of this sector. Thus, while in the EU, from demographic point of view, there are over 50 SMEs per 1000 inhabitants, in Romania we have around 26 SMEs / 1000 inhabitants, but according to zone the weight differs. In Bucharest the average is 48.56% of SMEs per 1,000 inhabitants, followed by the Nord-West, West and Center regions, with demographic intensities of over 25 SMEs/1000 inhabitants.

Regarding the development of SMEs, according to NASMEC, in the first half of 2007 the number of newly established companies over the first half of 2006 increased by 9.15%, the number of canceled companies subtracting by 74,18% during the same period. The results of SMEs in the first half of 2007 improved compared to the same period of 2006, the number of SMEs which have made profits increasing by 4-5%, while those who experienced loss subtracting by 0-5%. Positive developments recorded in the first half of 2007 both the investments made by SMEs (6-8%) and the exports volume of the private sector (12-15%).

2008 meant a reducing of the international activity for the Romanian firms, exports decreased by 24,3%, while imports with more than 37.4% compared to 2007. In January 2009 exports reached 1912.4 million euros while imports 2488.8 mil. Euros. Those who felt that the greatest decline were SMEs, whose export value in January 2009 represented a decrease of 47% from the previous year.

## 2. Literature Review

For long time the internationalization activity of small companies wasn't be seen as habitual and appropriate process for their development. This idea was indurated also by the fact that in many countries the internal market was large, offering real and profitable opportunities for SME's continuous growth. But the intensification of globalization phenomenon determined a shift in the SME's behaviour pattern. The importance of internationalization activity of a firm grows in the last 20 years along with global

competition all around. Others important factors which determined internationalization process were the integration of European markets, development of IT technologies, increase of e-commerce and transportation infrastructure. For this reason many researchers started to study this process from different points of view: strategic management, organization theory, international management, marketing and small business management.

Regarding the small firms international activities there are several classical areas of research like foreign market expansion and entry modes, motives which influence the international decision-making, which are completed by more recent topics like favorable and unfavorable factors for internationalization activity of the firm (Ruzzier et al, 2006), relations between import and export activity (Karlsen et al., 2003), factors with impact on firms' performance (Kuivalainen et al., 2004).

Known as so-called Uppsala internationalization model (Johanson and Vahlne, 1977), the dynamic theoretical model argues that the present state of the firm is the important factor in explaining future changes and subsequent stages which is represented by the firm's market commitment to foreign market and the market knowledge about foreign market and operation.

The market commitment is formed by two factors: the amount of resources needed to make the investment in the market and the difficulty for transforming them in practice. Developing international activities required also general knowledge about markets operations and market specific knowledge. In conclusion for getting this market knowledge the primary objectives of the firms is to hire personnel with international experience, able to interpret information from inside the firm and from the market. The change aspect was been see as a commitment decision to respond to uncertainty and opportunities on the market. The Uppsala model stated that firm's starts with less risky forms of internationalization in close markets and gradually increases its commitment and its geographical reach based on a process of experiential learning (Eriksson, 1997). According to this model, lack of knowledge is an important obstacle in the development of international operations and such knowledge can be acquired mainly trough operation abroad. The gradual acquisition of knowledge increase foreign commitment.

Holmund et al (2007) come with the idea that import activity could be considered as a vehicle to develop overseas business and suggest links between importing and exporting. They considered that imports activities are focused on operation while exports on marketing. Even if there is no consensus regarding ways to measure the effect of internationalization on SMEs performance, Mc Dougall and Oviatt (1996) remarked that firms which had an intensive international activity also reported a superior performance in terms of both relative market share and return on investment (ROI). Bloodgood et al. (1996) found that international activity was marginally significantly associated with ventures that reported higher profits. Even if a causal relationship between internationalization and firm's performance has not been established in longitudinal studies made by different researchers, one consideration come up for sure: starting activities in the international markets, especially export, drives to strategic approach of the business and deepen elements of planning.

### **3. The Methodology and research objectives:**

Our paper is concerned with studying the specific factors that influenced Romanian SME's behavior to be involved in international operations. As many Romanian entrepreneurs associate the Romanian accession to the European Union with new business opportunities, and based on other theoretical and empirical studies about international business and internationalization process our intention is to obtain answers to the following questions: Which is the order of appearance: importing or exporting operations?; Which are the main motives for developing those types of operations and

how much the entrepreneurs are interested to increase their intensity in the future?; What kind of changes is needed for the improvement of firm capabilities?; How do international operations contribute to the achievement of growth strategy and to firm development?

In this respect we analyzed the evolution of the SMEs sector from North-West Region of Romania and used secondary data from National Institute of Statistic, National Council of Small and Medium Sized Private Enterprises in Romania and National Agency for Small and Medium Sized Enterprises and Co-operatives. Furthermore, for a better understanding of this behaviour, we have conducted a survey based on questionnaire about the international activities of the Transylvanian SMEs with their entrepreneurs or managers.

### 3.1. Sample characteristics

Our sample comprises 226 SMEs from North-West Region of Romania ( Cluj, Bihor, Sălaj, Satu-Mare, Bistrița-Năsăud, Maramureș). Romania has a service oriented economy and this is shown also by our sample structure, the majority of the companies acting in the field of services (38.3%) and commerce (37.2 %). In terms of economic results, our sample companies have registered in 2008 an average turnover of 2.3 million Euros.

Table.no 2. The structure of enterprises based on activity and number of employees

Number of employees	Main field of activity			Total %
	Production %	Services %	Commerce %	
0-9	15.38	51.28	38.89	37.62
10-49	50.00	38.46	47.22	44.55
50-249	34.62	10.26	13.89	17.82

### 3.2. SMEs sector from Nord-West Region

North-West Development Region (Northern Transylvania) is considered, after the Bucharest-Ilfov Region, the most attractive in terms of economic development of Romania's regions. This is due to the labor market and wages, to foreign investment, and private environment and market competition and also to the input of modern technology. Relevant is that the service sector has come to occupy a large share of total regional economy, nearly 50%, with significant industries trade and tourism.

Regional economy is growing with a dynamic growth in recent years in sectors like construction, textile industry, industry of machinery and equipment. Here are nearly all industries and an increasingly important number of major foreign companies, some of them located in industrial parks in the region - Tetarom Cluj, Bors, Jibou and Satu-Mare.

The driver of exports and also the main importer in North-West Region (Northern Transylvania) is the Bihor county, followed by the counties of Cluj and Satu Mare, while the counties of Bistrita-Nasaud and Salaj, which are predominantly rural, take very little part in all foreign transactions of the region.

The development potential of the region is based on services and access to a well-qualified workforce, which led to attracting foreign investors which took over factories and have opened industrial parks in the area. Genuine drivers of regional economic growth small and medium enterprises are around 65,000 in 2006, 13.78% of the total number of companies registered in Romania, contributing with about 11% in the turnover achieved by SMEs in Romania. In terms of labor productivity, North-West region is in second place after Bucharest-Ilfov.

Tabel no.3. Turnover, number of employees and labor productivity in North-West Region

	Turnover (mill.lei)	Turnover structure (%)	Number of employees	Number of employees structure (%)	Labor Productivity (thousands lei)
Nord-West	39400	10.82	351242	13.61	112.173
<b>Total</b>	<b>364000</b>	<b>100.00</b>	<b>2580927</b>	<b>100.00</b>	<b>141.035</b>

Source: Romanian SMEs White Charter, 2008

#### 4. The findings and discussions:

Firm growth is one of the main motives for internationalization activities. After getting a significant market share in domestic market, firm increasingly look abroad for new opportunities. Many studies on export decisions show that firms are stimulated to exploit the potential for extra growth, profits and sales resulting from exporting (Leonidou, 1995). An objective for our research was to identify which are these motives for internationalization and what group of factors, proactive or reactive, plays a more important role in determining the internationalization process of the Transylvania's SMEs. In order to have a more specific and correct image of this aspect we detached factors which could be determinant for import and for export. Thus, for importing came in the first position the lack of domestic resources and the continuous increasing of domestic market. These reactive motives were indurate by some favorable factors identified by the firms in: lower prices on foreign market and closed cooperation with foreign partners.

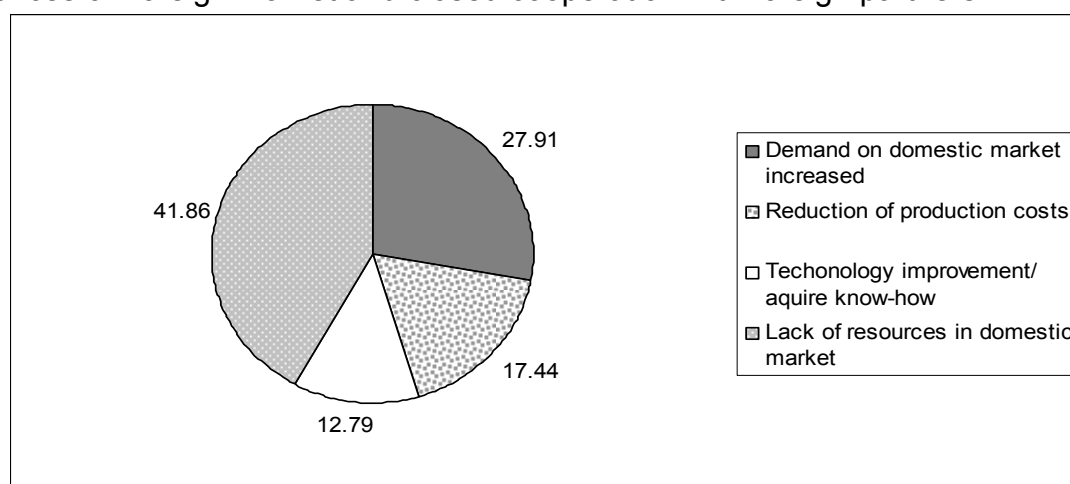


Fig.no.1. Factors determining import activities

Regarding the export activity of Transylvania SME's resulted that the main motives for starting this process are successful cooperation with foreign partners and growth opportunities of external market. In his studies Dunning has argued that it is inherent for firms, for increasing their international spread, to rely more and more on cooperative agreements. When firms entry into international marketplace they need to identify suitable partners abroad in order to get the complementary resources they need, as well as to save time and money. Our study's results reveal that the Romanian SME's are depending on chance to identify an external partner, having few information about the external markets e.g. competitors, consumer behaviors and needs, rates and prices etc. The entrepreneurs seem to have a more proactive behavior when they decided to start an international activity. Also in a high proportion they consider that for internationalization development play an important role the opportunities identified in the environment, as: firm capacity to increase production system and improvements in communication and transportation infrastructure.

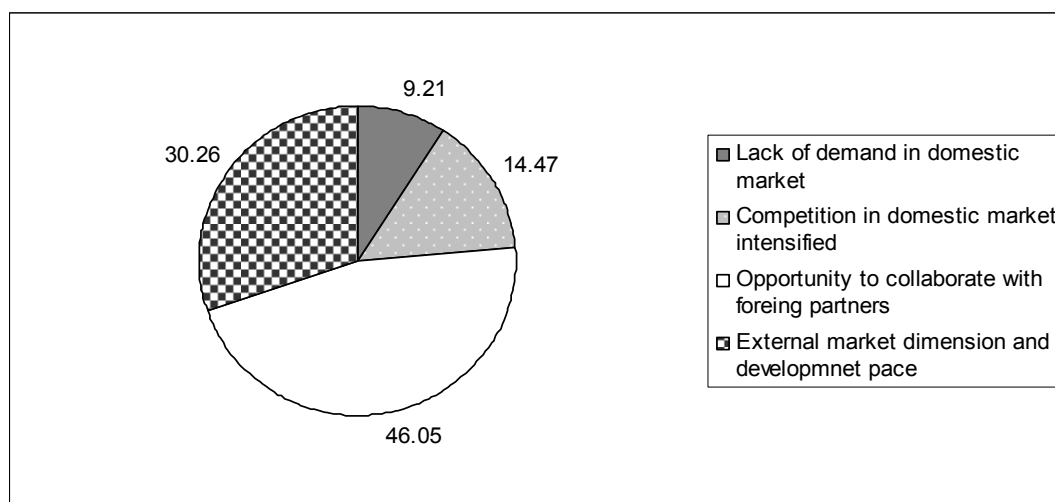


Fig.no.2. Factors determining export activities

Even if many researchers found out that the first international operation developed by SMEs is exporting, for our sample result the contrary, first action was inward operation for more than 70%, 28 have both international operations. In the top of the countries with which are developed these activities are: Italy, Hungary, Germany, Austria and Spain, countries which are also representative for foreign investments in our economy. Importing operation represent a large part of the Romanian SMEs businesses, thus for almost 44% of sample firms ponder of import in total turnover are more than 50%. The conclusion that import activity is much more developed by Romanian SMEs comparing with export is indurate by the higher average percent of the import activity in the total turnover of the firms of 51,4% than export with an average of 32,8%. For determining the relation between importing and exporting activities we tested the hypothesis about the appearance order, resulting a strong correlation between import and export.

Tabel no.4. Correlation between inward and outward operations

		First operation	Second export	Second import
N = 209	Correlation coefficient			
First operation		1.000	.710**	-.110
Second export			1.000	.101
Second import				1.000

\*\*Correlation is significant at the 0.01level (2-tailed)

This means that for those firms which started international operations with importing, this activity influences their capabilities and offers them an important international experiences for developing after that export activities or international cooperation.

Last 2 years brings important opportunities for the Romanian SMEs, which indicated in a high proportion (64%) a positive evolution of their overall performance. Also for the following 2 years the managers and entrepreneurs are optimistic 57% from them indicated as strategic priorities a moderate growth of the business activity. Our intention was to see also if this strategic development is connected with the international activity and for this reason we tested correlation between company's general objectives and the actual opportunities offered by international market

Tabel no.5. Correlation between inward and outward operations

		General objective for the next 2 years	Opportunities offer by the international market
General objective for the next 2 years	Pearson correlation coeficient	1.000	.231**
Opportunities offer by the international market	Pearson correlation coeficient		1.000

\*\*Correlation is significant at the 0.01level (2-tailed)

This favorable attitude toward international operations is bounded gathered with the advantages and economic results obtained until now, taking into account the fact that in the sample there are only SMEs which already deployed these activities. Therefore we tried to identify how did concur international operations to the firm's development and which are the main results observed by entrepreneurs. The turnover and profit rising came first in the respondents' opinion and the SMEs which developed export operations seems to identified an improvement of their performance in a higher proportion than importers.

Table no. 6. Advantages of international activities

	Mean (1very important-5)
Turnover increase	1.61
Profitability rise	1.90
Quality improvement	2.0
Product diversification	2.27

## 5. Conclusions

The results of our study show a strongly concentration of Romanian SMEs to import, entrepreneurs having as main motives the lack of resources and the increasing domestic demand. In a high proportion these companies declared as future intention engaging in export activities mainly for the opportunity to cooperate with foreign partners and due to the dimensions of international markets. This fear to enter in the international affairs with export operations is first of all a cultural trait for Romanian entrepreneur which didn't achieve until now enough experience in their business in order to be able to accept a higher risk. We think that Romanian SMEs need help for improving their knowledge of foreign markets, in attracting funds and also in improving their competitiveness to face to strong and global competition.

Despite of limited resources and lack of production and marketing capabilities many entrepreneurs are interested to expand their involvement in international operations. In today international markets more and more challenging the SMEs position depend on their capacities to reinforce and develop important strengths. For these results they are need to established an appropriate international business strategy and strive to various forms of cooperation both in domestic markets, including cooperation with larger companies, and also into external markets.

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