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**SMEs, TERRITORIAL DEVELOPMENT AND  
NETWORKING: THE CASE OF ROMANIA**

**Daniela L. Constantin**

**ACADEMY OF ECONOMIC STUDIES OF BUCHAREST  
ROMANIA**

**E-mail:** [dconstan@hotmail.com](mailto:dconstan@hotmail.com)

## **1. Introduction**

The regional dimension of the transformation processes undertaken in East European countries is a new field of research and one of the sources of 'new combinations' in regional science (Geenhuizen and Nijkamp, 1995). The elements of the structural reform, namely the institutional and legislative framework for the market economy, the reform of enterprise structures, the physical structure for a competitive economy, human capital and attitudes entail specific concerns at regional level in terms of restructuring regional economies, regional policy instruments in an acute shortage of financial means context, regional institutional framework and the question of decentralisation, the impact of European integration, the new role of local communities, etc..

As many researchers have noticed, the experience of former socialist countries shows that transition deepens regional disparities because the factors that used to control the economy are replaced by market forces that are gradually freed up. The speed of reform is finally responsible for slower or faster increase in regional disparities. In the case of Romania the pace of reform was rather slow in the first six-seven years (Green Paper, 1997). But the basic question is whether a period of growing interregional disparities a process of spatial economic convergence will start in longer run. This means that the regional question is not simply a static allocation problem, but also one referring to dynamic long-range qualitative conversion phenomenon. As long as a convergence trajectory will not be automatically followed, an active regional policy is necessary. This policy must be integrated in a complex outlook, which combines the need for local identity, self-reliance and development with the challenges and opportunities of globalisation processes seen at both national and international level, with the aim of the future integration in the EU structures in view.

A major issue in this general framework is applying regional policy in a decentralised context that focuses on regional (local) efforts to foster socio-economic development: in other words, on endogenous development. The main idea in this view is that development is above all a local matter: "The success of a region will in the end depend upon on its autonomous capacity to take matters in hand, to organise various actors around common goals, to adapt and to successfully adjust to outside pressures. Ultimately, the sources of development lie in the region itself, in its people, its institutions, its sense of community, and, perhaps, most important of all, in the spirit of innovation and entrepreneurship of its population" (Polèse, 1998).

Directly related to this approach, the question of small and medium enterprises (SMEs) is a basic one. As demonstrated by the experience of Western countries, for more than twenty years SMEs represent an important source of local and regional dynamism. The economic recession and the accompanying changes in production organisation revealed the vulnerability and deficiencies of the large companies, proving that they are no longer the only engine of development (Maillat, 1990). The economic reform occurring in Central and East European countries also emphasizes the role of SMEs: this sector is considered to have a key role in restructuring the old centralised economies and maintaining the economic dynamism. SMEs should be able to create a significant number of new jobs, to improve industrial relations and to provide a superior working environment for employees, to create a diversified and flexible industrial base by creating a pool of entrepreneurs willing and able to take risks, to stimulate competition for small and large firms alike, leading to an energetic enterprise culture, to stimulate innovation (Armstrong and Taylor, 1993).

From regional viewpoint the main question is whether SMEs have a similar effect in each region. The answer is negative: “The presence of SMEs in a region does not necessarily mean development or revitalisation. The arrival of SMEs in a region may be the result of the corporate strategy of large companies (for example, vertical dis-integration). Because SMEs depend on outside entities, in this case they do not help to generate ‘autonomous’ local dynamism. Nor is the existence or emergence of independent or local SMEs in a region necessarily the sign of a specific regional dynamic. True, these SMEs provide jobs, but they do not provide the region with the chance to control its development. Indeed, if local dynamism based on SMEs is to manifest itself, one condition has to be met: SMEs have to belong to a territorialised network” (Maillat, 1990).

The most successful model is that of SMEs organised in local production systems of the NEC type (NEC is the acronym of North-East and Central Italy where the model has flourished most). It implies a dense network of interdependences between enterprises (usually but not always specialised in a particular sector) as well as links, relations, exchanges between them and other agents acting in the region (like banks, higher education institutions, research institutions, training centres, consulting firms, sectoral associations of producers, chambers of commerce, local public administration, etc.). At the same time the recent evolutions, reflecting the growing regional awareness and the growing efforts to shape regionally based alliances, networks and

neighbourhood cooperation (Funck and Kowalski, 1993), in relation with changes in the competitive scenario of the international economy lay the foundations for further development of SMEs within interregional and international networks.

Starting from these overall considerations this paper aims to explore the main features and the significance of the SME sector development for addressing the regional question in Romania during the transition period and to identify the first signs and the perspectives of SME territorial networking phenomenon. It also aims at analysing the usefulness and the relevance of this concept and those directly related to it (local entrepreneurship, local milieu) for regional policy purposes.

## 2. The actual state of SME sector in Romania

For a better understanding of the role and results of SME sector development since 1990 a presentation of the general context of the Romanian transition has been considered necessary.

The political turmoil in the last ten years made a real advance of reform very difficult, Romania being severely criticised by the EU and international financial institutions for the drawbacks in restructuring and privatization, the incapacity to eliminate losses within the economy, the lack of real changes in public administration. All these phenomena are reflected by the evolution of the key performance indicators between 1990 and 2000 (Table 1).

Table 1

Key economic performance indicators in Romania between 1990 and 2000

Indicator	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Nominal GDP (USD bn)	35.1	28.9	19.6	26.4	31.5	35.7	35.5	34.6	36.8	34.0	36.7
GDP change (%)	-5.6	-12.9	-8.8	1.5	3.9	7.1	3.9	-6.9	-5.4	-3.2	1.6
GDP per capita PPP (USD)	na	na	na	na	5550	6210	6630	6330	6050	5970	6240
Industrial prod. change (%)	-19	-22.8	-21.9	1.3	3.3	9.4	6.3	-7.2	-13.8	-8.0	8.7
Unemployment (end-year, %)	0.4	3.0	8.2	10.4	10.9	9.5	6.6	8.9	10.4	11.8	10.5
Average monthly wage (USD)	138.6	97.6	82.6	103.1	109.8	138.3	138.4	121.8	153	127.7	na
Inflation (%)	5.1	170.2	210.4	256.1	136.8	32.3	38.8	151.4	40.6	45.8	45.7
Trade balance (USD bn)	-1.7	-1.3	-1.4	-1.1	-0.5	-1.6	-2.5	-2.9	-3.5	-1.9	-2.7
Foreign direct investment stock (USD bn)		0.0	0.1	0.2	0.6	1.0	1.2	2.4	4.5	5.4	na

Foreign debt (USD bn)	1.2	2.1	3.2	4.2	5.6	5.5	7.2	8.6	9.3	9.2	na
Population (m)	23.2	23.2	22.8	22.7	22.6	22.6	22.6	22.6	22.5	22.5	22.4

Source: *Business Central Europe*, December 2001

Three sub-periods can be identified within this decade, namely: 1990-1992 (the beginning of transition), when the GDP recorded a serious drop; 1993-1996, when a macrostabilisation programme was applied, with positive consequences upon economic growth, unemployment and inflation rate; 1997-2000, when the economic decline (until 1999) represented the first result of the massive restructuring and privatization process (too much delayed in Romania) undertaken in this period, being followed by a slow recovery starting with 2000.

Within this general context the evolution of the Romanian sector of SMEs expresses a variety of conditions and causes, the following being the most relevant (Annual Report, 1998): the absence of such a sector before 1990; the legal framework for setting up this kind of enterprises; the incentives provided at the beginning of the process; the speed of restructuring and privatisation of the state firms.

Thus, unlike other former socialist countries where some private activities could develop within the centralised economy, the private initiative development in Romania started in fact in March 1990, when the first act in this direction was issued.

In general terms the support offered to SMEs up to present has focused on several directions such as: the stimulation of setting up new firms; the development of the existing ones; providing consultancy services, etc., all these directions considering both financial and non-financial assistance. Without being exhaustive, making mention of some supportive measures over the last decade can be relevant for the scope of these efforts:

- provision of loans with subsidised interests (from the unemployment fund) to SMEs hiring unemployed workers;
- a programme of subsidized credits carried out through the former Romanian Agency for Development;
- guarantees for private entrepreneurs;
- projects financed by the Romanian Fund for Social Development;
- investment grants offered by Phare via the Economic and Social Cohesion component;

- subsidies provided by the EU within the RICOP programme for industrial restructuring and professional reconversion and grants via FIDEL programme (Local Initiatives for Economic Development Fund);
- loans on commercial basis initiated by international financial institutions (World Bank for exports and investments in food industry, ERDB also for exports);
- the Romanian-American Fund for supporting private initiative, with capital investments as the main destination;
- business incubators;
- consulting centres which have been created using both internal and foreign funds and assistance (From UNDP, Phare, USAID, Know-How Fund of the British government, German, French, Dutch governments, etc.);
- encouraging the cross-national links between SMEs, universities, research institutes with the support of the Framework Programme Five of the EU, etc.

The importance of this sector for revitalizing the Romanian economy is also highlighted by setting up, at the end of the year 2000, of the Ministry for SMEs.

As a result of these concrete measures and actions the SME sector has recorded a significant dynamism. In the year 2000 the total number of SMEs (fewer than 250 employees in Romania) was 781327, representing 99.6% of total active enterprises and accounting for approx. 46.9% of total employment and 55.9% of turnover. Considering the capital ownership type 97.4% of total SMEs are private, 0.3% are state-owned and 2.3% are mixed firms. In general terms, the private sector contributes 65.5% to GDP, 65.7% to exports and 70% to imports. As regards the SME distribution by size, 93.6% are micro-firms (up to 9 employees), 5% are small (10-49 employees) and 1.4% are medium firms (50-249 employees).

The structure of private sector by activity also reveals some interesting aspects:

- one of ten firms mainly perform an industrial activity;
- every eight commercial firms correspond to one in industry and every 34 to one in construction sector;
- 88% of micro-firms belong to commerce and service sector, while 59.5% of medium firms belong to industry and constructions; the share of industrial medium firms is increasing;
- within industrial SMEs those belonging to food, light and wood industry prevail (more than 57% of total industrial SME number); still, chemistry and machine-building have recorded a significant growth in recent years.

Related to these facts it is useful to explore the opinion of SMEs with regard to the obstacles they have had to face for their development. They mainly refer to (Annual Report, 1998, Report on Private Sector of SMEs, 2000):

- the uncertainty of the political framework;
- the incomplete, immature and continuously changing legal and institutional framework;
- the adverse macroeconomic framework: high rate of inflation, price instability, low level of demand;
- financial aspects: high tax level, difficulties with access to financial sources (high interest rates to bank credits);
- infrastructure aspects (including lack of premises), relationships with governmental organizations and access to new technologies;
- human capital quality-related problems;
- insufficiency of agreements with foreign entrepreneurs and business firms, etc.

The international experience shows that, in order to improve the existing situation, the governments establish objectives and plans applicable to the whole business sector, regardless the firm size. Sometimes policies and programmes specific to SMEs can be added to these general measures.

The overall objectives take priority, have a common content in majority of cases and are essential to SME development as well. They focus on:

- ensuring a stable fiscal and monetary framework, including reasonable levels of interest rate, with inflation under control;
- the development of a financial market system able to stimulate saving process and to offer mechanisms for transforming savings into investment;
- applying adequate policies for competition protection;
- human capital development;
- ensuring a favourable climate for new firm formation and the development of the existing ones;
- encouraging co-operation and partnership between firms;
- applying clear rules with regard to ownership and contract discipline.

In addition to the overall economic policy the Romanian government has adopted by the beginning of 2001 special measures in order to stimulate the SME sector such as: exemption from paying custom tariffs for equipment and know-how, from paying profit tax provided that profit is reinvested, lessening bureaucratic chain and so

on. Though, besides opinions for and against, doubts have been formulated with regard to proper running of these measures.

In conclusion the most important action for supporting SME sector consists in encouraging business environment and overall economic development.

### **3. Territorial distribution of SMEs and their role in territorial development and networking**

For grasping the facts revealed by this distribution it is first necessary to mention that Romania's administrative-territorial structure comprises one regional level – the counties, named “judete”, corresponding to NUTS3 level of the EUROSAT (there are 41 counties plus Bucharest municipality) and one local level (cities, towns, communes). Also, according to the Regional Development Act 151/1998 eight development regions, corresponding to NUTS2 level have been established on a voluntary basis (without being administrative units) in order to ensure the regional development policy elaboration and implementation framework. Each region comprises between 4 and 7 counties (excepting Bucharest-Ilfov region).

The territorial distribution of SMEs generally reflects the discrepancies in terms of county size and economic development level but also reveals facts describing the specific conditions of SME sector development\*.

Thus, more than 20% of SMEs are concentrated in Bucharest. The same city holds an even higher share in constructions and services (26.2%, respectively 26.3%) but its share is under 20% in commerce and only 16.1% in industry.

The number of SMEs is directly correlated with the county size (in terms of population) and the level of economic development. Eight counties which have – each of them – more than 3% of total number of SMEs hold together 28.4% of this number (Bihor, Brasov, Cluj, Constanta, Dolj, Iasi, Prahova, Timis). Most of them are big and well developed counties. The same eight counties have 21.1% of industrial SMEs, 33% of construction SMEs and 29% of service ones. At the opposite pole eight less developed counties (Ialomita, Mehedinti, Tulcea, Salaj, Teleorman, Vaslui, Calarasi, Giurgiu) account for less than 5% of industrial SMEs, which represent less than 1% in each of these counties. This fact demonstrates a high polarization of SME sector in

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\* This paper concentrates on comparisons at county level, the regions being more homogenous in terms of main economic and social indicators.

industry and construction. The distribution by county of commercial SMEs is more homogenous, the share varying between 0.7% (Salaj) and 4.1% (Cluj).

The sectoral distribution of SMEs at county level brings about new facts. For example, in Bucharest the commercial and service SMEs prevail (61.2%, respectively 22%). The share of industrial SMEs is only 6.8%, compared to 9% at national level. In respect to SME sectoral structure at county level is important to point out that the share of industrial SMEs within the sectoral distribution of SMEs at county level is conditioned neither by the county size nor by their economic development level. Data suggest that the industrial SME share is rather influenced by the available resources of each county. This confirms the orientation towards those SMEs able to turn to good account the natural advantages of local economies, in accordance with endogenous development principles. Thus, some counties which are not among the most developed ones have a higher share of industrial SMEs compared to the national average due to wood industry (Covasna, Harghita, Maramures), light industry (Arad, Neamt, Satu Mare), food industry (Alba, Bistrita-Nasaud, Sibiu) which have found there favourable conditions for their development.

Considering the circumstances specific to the transition period the commercial SMEs are predominant in all counties. A tendency of negative correlation can be noticed between the share of commercial SMEs and SMEs in service sector.

These structures can suffer significant changes only in so far as the private sector of SMEs is consolidated within a sustained restructuring process.

These possible developments can also determine a real, more intense SME networking at territorial level. So far, even though studies especially devoted to this phenomenon have not been undertaken, a series of clues about the actual state of SME territorial networking in Romania can be drawn from two surveys organised by the Romanian Centre for SMEs for specific purposes: one of them is a special study regarding the barriers to SME sector development, the other one concentrates on barriers to SME sector's exports (Annual Report, 1998). As the evolution of the SME sector in the last years has been quite slow the results of these surveys can be considered relevant for the present situation as well.

The barriers to SME sector development have been classified into several groups, as follows: barriers to supply activities, barriers to delivery, barriers related to production and technical endowment, barriers related to labour force, to financing SMEs, institutional barriers.

The barriers to supply activity, identified in the responses of 44% of firms (among them construction and industrial firms are above the average) are presented in Table 5.

Table 5

Barriers to supply activity	
Barrier:	%
Price	47
Quality	42
Availability	35
Supply frequency	33
Lack of short run financing	31
Romanian regulations regarding imports	26
Quality of specialized labour force	25
Management quality	21
Foreign regulations regarding the exports to Romania	15

Source: *Annual Report*, CRIMM, 1998, p.57

As the main problem seems to be the input price/quality relationship, the input markets have been studied thoroughly. The location of the suppliers shows that the majority of inputs is obtained from Romania (either from the own or neighbour county or from other counties), followed by Western Europe, Eastern Europe, Near East and North America. The correlation with SME dissatisfaction regarding input price and quality suggests that the entrepreneurs consider the quality of Romanian inputs less acceptable, especially related to their price. It is significant that many firms that import their inputs have chosen Western Europe as the main source. These firms have few complains with the quality of products even though the supply prices are generally high.

In order to identify the causes that have lead to mentioning the input availability as the third important barrier the number of suppliers for the firm's main activity has been analysed (Table 6). It has aimed to clarify whether the low availability of inputs is a real constraint or it is a result of weak knowledge/abilities in marketing of the entrepreneurs.

The answers received highlight that the majority of firms complaining about difficulties with the access to the needed inputs depend on a reduced number of suppliers, especially service and industrial SMEs.

Table 6

## Number of suppliers for the firm's main activity

Number of suppliers:	%
one supplier	5
two suppliers	6
three suppliers	8
four suppliers	7
more than four	74

Source: Ibidem, p.58

The microfirms have the least number of suppliers, owing to the lower level of their activity. In turn, small firms have a greater number of suppliers compared to the medium firms. The answers provided suggest that small firms are more flexible in their marketing activities than the medium ones. The situation can be explained by the fact that small firms are generally newly established firms whereas the medium firms are partly former state firms, recently privatized. Consequently, they still have strong ties with their traditional suppliers, many of them being state enterprises.

The share of firms with difficulties in product/service delivery is similar (44%) to that of firms with supply difficulties. There are not significant differences in sectoral terms; from size viewpoint medium firms have more delivery problems. The hierarchy of barriers to delivery is presented in Table 7.

Table 7

## Barriers to delivery

Barrier:	% of responses
Insufficient or unstable market demand	86
Too high competition	81
Low publicity funding	60
Romanian regulations regarding exports	59
Labour force quality	55
Other countries' regulations regarding Romanian exports	38
Lack of links with foreign partners	30

Source: Ibidem, p. 59

The insufficient or unstable demand ranks as the first obstacle, inducing the need of analyzing the location of delivery markets of the interviewed firms. It shows that only 10% of the firms in the sample have export activities (oriented to Western Europe, Eastern Europe, Near East, North America), the other ones distributing their products on the domestic market, especially in the own county or neighbouring counties.

Construction firms operate on the domestic market only, whereas industrial exporter firms account for 14% (the highest share). The latter are mainly medium firms. Micro and small firms have a lower share in exports (2%, respectively 8%).

Firms which have established mid and long-term export contracts have not complains with regard to delivery market instability. On the contrary, owing to Romanian economy's fluctuations and sharp variations in population's purchasing power, the domestic market appears to many of the investigated firms unstable and insufficient compared to their own capacity of product/service offer.

The need to strengthen their competitive position has stimulated many SMEs to introduce innovations in their current activity. In average, more than half of them declared that the emphasis has been put on new product and new technology-oriented innovations (Table 8).

Table 8

Technological innovations	
Type of innovation:	%
New products	31
New technologies	27
New quality control procedures	6
None	41

Source: Ibidem, p.66

The most active firms from innovation viewpoint seem to be the medium-sized ones. A possible explanation consists in the bigger financial power of these firms.

Although the sampled firms do not claim that their innovations are at high international standards, the answer provided as a whole demonstrates the dynamic concern of SEMs with this activity and their efforts to face market conditions even with limited resources and, in many cases, without any governmental help.

The whole analysis leads to the conclusion that Romanian entrepreneurs seem to emphasize the technological aspects of their business rather than management and quality aspects, which still remains an important drawback.

Going further, the study on the barriers to exports of SMEs brings about additional facts on SMEs sector development and networking.

In 1995 and 1996 the export sector was one of the most dynamic sectors of the Romanian economy. In 1995 and 1996 SME exports were around 4 billion USD,

respectively more than 6 billion USD. The private sector accounted for 51.4% in total exports. The export share in total income by firm size and by sector are presented in Table 9 and Table 10.

Table 9

The share of export in total income by firm size (%)

Firm size	1995	1996
Total	83	89
Micro	33	39
Small	22	65
Medium	92	95

Source: Ibidem, p.77

Table 10

The share of export in total income by sector ( %)

Sector	1995	1996
Total	83	89
Industry	93	94
Services	23	16
Commerce	37	44

Source: Idem

It can be noticed that all categories of firms recorded an increase of export share in total income, with a major change for small firms (from 22% in 1995 to 65% in 1996), demonstrating their big development potential.

From sectoral perspective, the share of exports in service SMEs decreased in favour of commerce. Industry maintains approx. the same share in the two years and this is much higher than in other sectors.

The share of exporter firms with mixed capital in total sampled firms (Table 11) demonstrates the interest of foreign partners in investing in Romanian exporter firms. This preference is essentially based on the possibility of a more rapid investment payback as well as on a more advantageous negotiation of contracts and prices on foreign markets.

The commercial firms have the highest share among the exporter firms with mixed capital. Most of them are set up with foreign capital involved in business from the very beginning, especially in order to export to the home countries of those investors.

Table 11

## The share of exporter firms with mixed capital by sector

Sector	Entirely Romanian capital	Mixed capital
Total	64	36
Industry	69	31
Services	68	32
Commerce	55	45
Construction	100	0

Source: Idem

The higher share of commercial firms also influences the distribution by firm size. As commercial firms are usually small, this distribution records a high percentage of this type of firms (Table 12).

Table 12

## The share of exporter firms with mixed capital by firm size

Firm size	Entirely Romanian capital	Mixed capital
Total	64	36
Micro	68	32
Small	60	40
Medium	67	33

Source: Ibidem, p.78

As concerns the origin country of foreign investors, the big majority comes from Western Europe plus Turkey and Greece (70%), followed by Eastern Europe (12%), Near East (12%), North America (3%) and Far East (3%).

Most of mixed capital exporter firms' managers declare that foreign partners' presence has had a favourable role not only in finding delivery markets for their products/services but also in technology transfer and managerial capability improvement.

If the answers to the innovation-related question in the general sample are compared with those of the export firms, it can be noticed that the latter have a better situation, with a special remark for mixed capital firms (Table 13).

Table 13

Innovation by type		
Type of innovation	% of total SMEs	% of exporter firms with mixed capital
none	41	31
new products	31	40
new technologies	27	36
new quality control procedures	6	11
others	4	3

Source: Idem

According to this table, the share of firms that have not introduced any innovation decreases; in turn, there is a significant increase in the share of firms which have introduced new technologies, products and quality control procedures. These data emphasize the positive role of foreign-domestic firm partnership in Romanian firms' development.

The geographical distribution of the exporter firms' suppliers reveals that these firms have to make bigger efforts for finding the necessary inputs compared to the general sample of SMEs (Table 14).

Table 14

The geographic distribution of exporter firms' suppliers compared to the whole sample

Location :	% of total SMEs	% of exporter SMEs
Own/neighbouring county	81	58
Other counties	64	70
Eastern Europe	11	25
Western Europe	28	63
Near East	3	5
North America	2	1
Others	1	0.3

Source: Ibidem, p. 79

Exporter firms have to co-operate to a greater extent with suppliers from other counties or to import. Western Europe ranks as the first of foreign suppliers (with a very high share, 63%) that is explained by the preference for quality inputs as well as by the traditional relations with certain countries and their geographical location (much closer than other developed countries, in North America and Far East).

The situation by sector shows that 73% of industrial firms co-operate mainly with West European suppliers; in service sector this share is 59% while in commerce is 54%.

The geographical distribution of foreign markets for delivery of final products/services has recorded an important change: Western Europe has a share of 71%, compared to Eastern Europe (36%), whose countries used to be traditional partners of Romanian firms.

Considering the firm size, microfirms record the highest share of exports to Eastern Europe (45%), whereas small and medium firms export predominantly to Western Europe (with similar percentage, 74%).

The survey also shows an interesting distribution of exporter firms, namely by the modality of finding foreign business partners: 47% - by personal connections; 23% - helped by the foreign associate in their firms; 16% - using information provided by various publications; 9% - helped by the chambers of commerce; 5% - other ways (participation in fairs and exhibitions, collaboration with local agents, the use of special catalogues, etc.).

Finally, the main obstacles to export activities of SMEs refer to: fiscality (84% of the interviewed firms), high costs of production (67%), export formalities (55%), low quality of products (48%), inadequate technologies (46%), lack of demand (36%), lack of qualified personnel (14).

The analysis of the information provided by these surveys has indirectly revealed that the SME territorial networking phenomenon has already appeared in Romania, although it is still in an incipient stage.

The geographical distribution of supply and delivery markets and other additional facts suggest the creation of the framework for networking not only at regional (county) level, but also at interregional and international level. Within these networks SMEs interact mainly with other firms of the same sector and size but, in various cases, with big state firms as well. Empirical observations demonstrate that SMEs have focused on those products/services able to create a competitive advantage but so far there is not enough information to measure the scope, the extension of the process of parallel outsourcing of functions that could be better performed by specialised suppliers within indirect vertical integration through the creation of networks of local subcontractors, nor the creation of spin-offs and new firms in related sectors. These still remain subjects for further studies in this field.

Although industry represents a major factor able to mobilize local economies, constructions, commerce and services play an active role as well, according to the

special features of transition and new developments in local production systems. For example production services such as wholesale trade, logistic activities, banking and insurance, etc. have been more and more integrated in territorial networks.

Encouraging signs of networking have also appeared between firms and universities, modern consulting services, training centres, sectoral associations of producers, local public administration, chambers of commerce, following endogenous development models. Counties with longstanding industrial traditions, where higher education institutions are also located are particularly active in innovation process and promotion of new entrepreneurial skills. Unfortunately innovation support has lower priority in public policy. Not only in Romania, but in all former socialist countries “there is a strong danger that the old R&D infrastructure, much of which could still provide a basis on which to build, is being weakened by funding cuts which took place after the transformation to a market system began” (Funk and Kowalski, 1997). That is why universities are more involved in promoting R&D at local level than the old research establishments belonging to the national academy of science or ministries.

On the other hand privatisation of state enterprises and the establishment of a quite large number of SMEs is gradually transforming the economic behaviour of economic actors. These private firms are well financed and compete against each other, being motivated to create new products, introduce new technologies, produce more cheaply, sell more efficiently.

As the analysis has demonstrated the participation of foreign capital in Romanian SMEs also influences the innovation mechanisms and innovative behaviour. Foreign partners do not contribute only to the diffusion of new technologies but also bring about new ways of behaviour, new business routines, new mentalities which are essential for the success of transition to the market economy.

From networking perspective SMEs can perform a role in an international framework when they are closely integrated with other firms in foreign countries. One of the characteristic phenomena from this viewpoint in Eastern Europe, including Romania, is subcontracting agreements between foreign SMEs and domestic ones within a process of outsourcing some parts of production by the former.

Another interesting phenomenon presented in studies devoted to the internalization process of SMEs is the increased activity in the same foreign countries of many small entrepreneurs originating from the same region (Cappellin, 1998). A relevant example is the activity of textile entrepreneurs of the Veneto region in

Romania. Italian entrepreneurs are mostly interested in South-West and Western regions of Romania due to the advantages in terms of infrastructure (especially transportation infrastructure: airports with direct flights to/from Italy, good rail and road networks) and traditional relationships in some industries (textile, leather, wood, furniture).

There are also numerous projects of SME development included in the transborder co-operation programmes (e.g. those financed by Phare). Various examples of microintegration can be found not only in traditional industries like leather, clothing, metalworking, furniture, chemistry, car industry, electric appliances but also in advanced ones such as computer peripherals, software, electronic goods. The better the economic situation in a country, the more numerous the firms of the latter category (Török, 2001).

In general terms the measures aimed at encouraging a healthy business environment and overall economic development can contribute to supporting the expansion of SME sector, with all entailed advantages for the local and regional dynamism. Of course, specific measures are also required and should be integrated in active regional policies promoting SME development and networking within the endogenous development model.

#### **4. SMEs and regional policy**

Integrated in the process of reform required by the transition to the market economy, Romanian regional policy suffers a series of influences induced by the hardships of this period, the clear tendency to decentralisation, the increasing territorial competition. Under these circumstances one of the major options focuses on turning to good account the natural advantages of local economies, in accordance with endogenous development objectives. The modern outlook of this model is centred on local production systems which are not seen just as a territorial concentration of specific firms working in the same sector or in closely related sectors but also as a specific form of organisation of the close relationships among all local actors. It seems that the NEC type of local production systems, based on intense SME networking can serve as a model for the regional policies aimed at supporting SME development in the countries in transition, Romania inclusively.

In general terms the importance of SME sector to regional policy derives from their ability to innovate, their contribution to the performance of less developed regions and their role in the revitalization of certain industrial regions. In the case of countries in

transition this sector has a specific relevance and a series of particular advantages such as (Dragusin, 1998):

- as a source of intensifying competitiveness, SMEs act as an engine of structural changes and economic revitalization, following decentralization;
- SMEs can absorb a part of the unemployment resulted from a radical restructuring of industrial giants;
- SME sector can facilitate the transfer of economic resources from declining sectors to the prosperous ones;
- SME development can substantially contribute to the increase in the number of entrepreneurs and, thus, to creating a new social category, very important to setting the social basis of transition;
- SMEs diminish the regional consequences of privatization and/or restructuring for regional development;
- SME activity can contribute to reestablishing the macroeconomic equilibrium and moving towards a relative stability state, with a certain price of transition.

These potential advantages have determined a special concern with SME development in Romanian regional development plans. Without neglecting the importance of large firms for restructuring the production systems, the SME sector has been particularly focused by programmes aiming at reconstructing the regional economies in accordance with the specific problems of various areas (e.g. disadvantaged areas, growth potential areas, border areas, etc.).

Though, as already presented, the basic requirement for making SMEs a true factor of local dynamism is the integration in territorialized networks. Up to present this objective has not been offered the adequate importance so that this paper proposes some reflections that could be considered by the Romanian regional policy in the forthcoming years.

To meet the condition of creating and enhancing territorial networks regional policy has several complementary solutions that have to be applied considering the stage of development of SME sector and the perspectives after the completion of transition.

First, an appropriate, comprehensive institutional and legal framework must be established, as pre-condition for the success of any policy measure. The reform of public administration should have in view the replacement of the so-called 'prescriptive approach', based on dirigisme or top-down planning and characteristic to the centrally-

planned economy, by a 'transactional approach' where both national and local government define general norms ('rules of the game') and "aims to remove the obstacles to a greater and more flexible integration among various economic actors through the provision of 'public goods', such as information, infrastructure, services, and strategic initiatives based on public-private cooperation" (Cappellin, 1998). Within this framework the policies of territorial organisation can be combined with the traditional instruments of local development policies, such as financial incentives and provision of specialised producer services.

Taking into account the situation existent before 1990, a special emphasis must be put on enhancing the idea of entrepreneurship, SMEs being able to bring about an important contribution. It is often stated that a region can regain its dynamism if it regains its entrepreneurs (Coffey and Polèse, 1985). Of course, in the case of Romania the problem is not to regain, but to create a generation of true entrepreneurs, characterised by qualities of responsibility, spontaneity, imagination, capacity to predict and to adapt to change by detecting new opportunities, development strategies, identifying new resources, and relational know-how with people and the environment.

In order to stimulate the spirit of enterprise regional policies have to consider the particularities of each region from structural (nature of industries, size of firms), socio-cultural (occupational profile of the local population), economic (local availability of factors of production, such as premises or capital, and demand for new firm product from particular geographical markets) viewpoint (Maillat, 1990).

Another aspect that has not been paid the attention deserved is strengthening SME research and innovation. It has been argued (Funck and Kowalski, 1997) that even with limited financial resources – that is a very tough constraint to the countries in transition – the formulation and implementation of this policy is possible and necessary. The elements of such policies should encompass: promotion of development of small technology-oriented companies; assistance in the restructuring of applied research institutes; promotion of interaction between SMEs and technology organisations; provision of training in activities related to the innovation process; creation of national and regional transfer channels and policy.

The integration of SME activity in a complex networking – at regional, interregional, international level – requires intense efforts for implementing large-scale infrastructure projects. So far infrastructure is in the worst situation in Romania and this is perceived as a serious bottleneck in economic development.

Without being exhaustive the exposure of some priorities of regional/local policies centred on SME sector development stresses an important idea: the local dynamism does not result from the action of separate firms but from their overall behaviour. This phenomenon is illustrated by the notion of milieu or local environment-based approach that is concerned with understanding the firm in its local and regional context. As described by Aydalot and Keeble (1988, quoted by Maillat, 1990), “the firm, and the innovating firm, are not viewed as pre-existing in or separate from the local environment, but as being a product of it. Local milieus are regarded the nurseries, the incubators of innovation and innovative firms... The historical evolution and characteristics of particular areas, their economic and social organization, their collective behaviour, the degree of consensus or conflict which characterizes local society and economy, these are major components of innovative behaviour... This approach implies that innovative behaviour is as much dependent on variables defined at the local and regional level as on national scale influences. Access to technological know-how, the availability of local industrial linkages and inputs, the impact of close market proximity, the existence of a pool of qualified labour – these are the innovation factors which will determine areas of greater or lesser innovative activity within the national space”.

The milieu is composed of material and non-material elements, connected with hard/soft location factors acting within a given territory (Kowalski and Rottengather, 1998). The material elements are organised around the territorial production system, the local labour market and the territorial scientific system, closely interrelated. The non-material elements refer especially to the technical culture, but other aspects like the creative climate, the identification of local citizens with their location – city or region – based on historical and cultural motivation and future aspirations (Funck and Kowalski, 1996) should also be considered.

In conclusion, the policy measures meant to improve the frame conditions for SMEs and overall regional development should constitute a coherent ‘package’ including economic, legal, infrastructure, cultural and socio-political elements. “The aim of the package must be the definition of a ‘regional profile’, stressing and taking advantage of specific feature of each local area” (Funck and Kowalski, 1997). Of course, in an increasing regional competition there will be always winners and losers, but “it is important to recognise the difference between absolute and relative winners

(and losers)” (Nijkamp, 1997). This is what gives the main sense to bringing the SME question as a corner stone in the debates about current regional policies.

## **5. Conclusion**

SME sector represent an important source of local and regional dynamism. Even though the big firms remain a key factor of restructuring the productive system, from regional viewpoint the SME activity appears as a strategic one for each region’s economic reconstruction, provided SMEs be included in a well-structured environment, in a coherent territorial network, involving links, relations, exchanges between them and other economic agents (like banks, higher education institutes, training centers, consulting firms, chambers of commerce, local public administration).

In order to turn to good account the development potential of the Romanian SMEs, a stronger support should be offer to this sector within the overall economic policy, concentrating on three aggregate objectives: the removal of any administrative, financial, legal, etc. barriers that still hinder the SME starting-up and development; the provision of assistance and information to SMEs; encouraging cooperation and partnership between firms.

The analysis undertaken in this paper revealed that the framework for networking not only at regional level but also at interregional and international level has been created but so far there is not enough information to measure the scope of this phenomenon. The extension of the process of parallel outsourcing of functions that could be better performed by specialised suppliers within indirect vertical integration through the creation of networks of local subcontractors, the creation of spin-offs and new firms in related sectors still remain subjects for further studies in this field.

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