

ANALYSING THE POTENTIAL OF RURAL SMEs IN THE CONTEXT OF SUSTAINABLE ECONOMIC GROWTH

RAȚIU Patricia¹, MORTAN Maria²

Babeş -Bolyai University, Cluj-Napoca, Romania

Abstract

In the present paper we have chosen to make an analysis of the performance of the SME sector during the period 2008-2013, under the impact of economic crisis and taking into consideration three core indicators: number of SME, number of persons employed and gross added value.

Due to the fact that rural sustainable development become at present a strategic priority for European Union, the research aims to bring into attention the divers potential of SMEs sector in the rural area of Romania, in order to identify solutions that contribute to economic recovery for the next period in concordance with the Europe 2020 strategy.

We conclude that the future for developing rural enterprises and diversifying the rural economy will depend very much on integrating both agricultural and non-agricultural activities by attracting government and community funds.

Keywords: rural development, SME sector, non-agricultural activities, Europe 2020 strategy, sustainability

JEL classification: Q01, Q12, M13

1. Introduction

It is widely recognized that the role of small and medium enterprises (SMEs) in the national and regional economy is very important because they

¹ Teaching Assistant Ph.D, Faculty of Economics and Business Administration, Management Department, e-mail: patricia.ratiu@econ.ubbcluj.ro

² Associate Professor, Faculty of Economics and Business Administration, Management Department, e-mail: maria.mortan@econ.ubbcluj.ro

contributes in a large proportion to the achievement of the country's GDP (gross domestic product) and provides jobs for a large number of people. Therefore the economic recovery largely depends on the improvement of SMEs' performance.

At European scale, the financial and economic crisis has further accentuated the need for far-reaching and comprehensive policy measures in favour of SMEs, as a key for future employment and prosperity in the European Union (EU). In order to mitigating the effects of the crisis, European Commission launched in June 2008 an ambitious new policy initiative, a Small Business Act for Europe (SBA), to put SMEs at the forefront of decision-making, to strengthen their potential, to create jobs in the EU and to promote their competitiveness in the global markets (EC, 2009). Also the European charter of Small and Medium Enterprises imposed the EU member states to support and encourage the sector of small businesses. According to Annual Report on European SMEs (2013, p. 8) in 2010-2012 only, the EU's Member States implemented a total of almost 2.400 policy measures to support SMEs, an average of 800 measures per year, and almost 90 measures per country.

We consider that correcting the problems of the past and putting the Europe on a more sustainable development path for the future is a shared responsibility of the Member States and the EU Institutions. The Europe 2020 Strategy responded to this by setting out the foundations for future growth and competitiveness that will be smart, sustainable and inclusive, and which would address our principal societal challenges.

Moreover the European Union's rural development policy 2014-2020 becomes a major component of the Common Agricultural Policy (CAP) and addresses the challenges faced by rural areas as a whole and contributes to their sustainable development. Recognizing the challenges the rural areas are facing, the European Commission and OECD agree with the fact that the term "rural" is not synonymous with decline (Dachin, Sercin, 2012).

In this context, the topic of debate chosen for this article is of great interest for Romania because highlight the importance of creating and developing of small and medium sized enterprises in the rural area, as a factor of sustainable economic growth. Some authors (Giurca, Popa, 2007, p. 1) consider that for Romania, the SMEs sector should be the key of a triple sustainable rural development: economic, social, environment. The manner how to design and apply the funding of programs for rural development in

Romania could represent a chance for our country economy to perform on the EU market. We consider that a new concept of rural development should be defined and the needs to establish priorities should be more focused, taking into account the potential of our country, where rural areas cover 87,1% of the national territory comprising 47,2% of population (around 8,98 millions inhabitants) and rural employment rate is 58,5% (INS, 2011).

2. Material and method

The methodology during this study consisted in the analysis of the dynamics of SMEs, using statistical data. In the absence of an integrated database on small and medium enterprises, first challenge of the analysis was to identify potential sources of relevant data on the activity and performance of SMEs.

Because we have found differences between data from different sources for presenting the statistical data for Romania and EU-27 there were used the official information from INS, EUROSTAT, DIWecon, London Economic, several reports in order to capture the evolution of SMEs in the analyzed period. The main methodological steps used in this article were the analysis on: the number evolution of SMEs, the number of employees working for them, contribution to gross value added and the distribution into categories such as size and fields of activity.

Also a synthesis review was deemed appropriate because it integrates isolated information into a more comprehensive and internally consistent whole. It thus facilitates the integration of separate studies with different focuses and uses a variety of information to provide a comprehensive account of the subject being reviewed. Bibliographic documentation was performed by using secondary information sources to review current situation, problems and potential solutions about SMEs sector in the European Union and Romania. The sources include scientific literature (from national and international databases), European strategy on Rural Development, several reports of the European Commission and National Rural Development Programme of Romania 2014-2020.

3. Analysis the evolution of SMEs sector in Romania, in the context of economic crisis

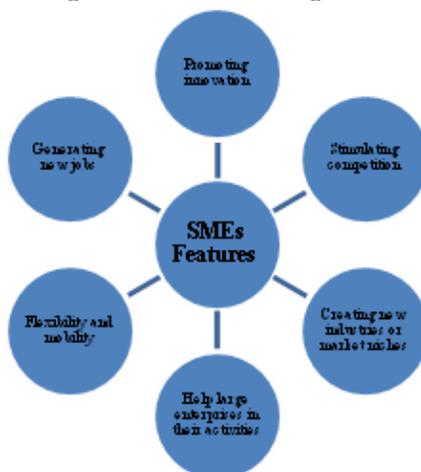
Delimitation of SMEs in the economic landscape has been, over time, a difficult and controversial topic. According to Definition of European

Commission Recommendation no. 361/2003/CE: “micro, small and medium enterprises category (SME) is formed up by enterprises that employ less than 250 persons and have a net annual turnover up to 50 million euros and /or have total assets up to 43 million euros ". We can notice that SMEs are defined in terms of the number of employees and either in terms of turnover or total balance sheet. The definition was also taken on in the Romanian legislation through Law no. 364/2004, and the classification of SMEs is made according to this law, as:

- micro-enterprises: up to 9 employees and net turnover/total assets up to 2 million euro;
- small enterprises: between 10 and 49 employees and net turnover up/total assets up 10 million euro;
- medium enterprises: between 50 and 249 employees and net turnover up to 50 million or total assets up 43 million euro.

SMEs feature a series of defining attributes, which define their role and place in economy (figure 1), such as being a factor of macro- and micro-economic balance, a source of generating jobs, creating new industries and meet the needs of a small group of consumers, promoting technical innovation, stimulating competition, facilitate functioning of large enterprises and have a high degree of flexibility and mobility.

Figure 1: SMEs defining attributes



Source: authors' conception based on literature review

SMEs play a key role in guiding the European economy towards more sustainable patterns of production and consumption. Through the high degree of mobility and flexibility they are the most adaptable segment regarding the adjustment of supply to the volume and the specific demand. (Pîslaru, et al., 2012, p. 37). Also SMEs have been considered one of the “driving forces” of modern economies due to their contributions in terms of technological upgrading, product and process innovations, in the presence of key assets such as human resources, finance, infrastructures and services (Miles, 2009). We consider that the ability of SMEs to innovate is important because it improves not only their own competitiveness, but also through linkages and knowledge spill-overs with other firms the entire industry and macro economy is influenced in a positive way.

The impact of the SME sector has to be considered a complex one, involving economical, financial, social, cultural aspects. First of all, for the developed countries from Europe and for the Eastern and Central European countries, small businesses have to be considered a force capable to lead to a better allocation of the resources and to generate new jobs for those who lost them as a consequence of the restructuring. (Giurca, Popa, 2007, p. 2). Never economic recovery and development fate, both in Romania and Europe, did not depend so much as now, on evolution and economic performance of SMEs sector. This is because, in the present context, SMEs are the most dynamic factor in economic development and social inclusion, by their competitiveness, innovation and the ability to create and maintain jobs in society, show the Report on the SME sector in Romania (2013).

In this context, the analysis of the dynamics of SMEs offers information on the way they reacted to economic crisis and legislative measures. Also after this analysis we propose some solutions that contribute to the recovery of this sector in Romania and sustainable economic growth.

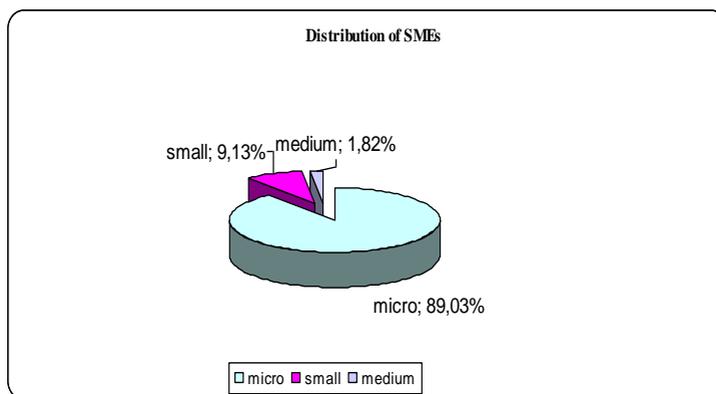
In the last years the evolution of SMEs sector in Romania was similar to that of European Union, in terms of the number and structure. In 2012, the share of active SMEs in total national firms was 99,65%, very close to the share of SMEs in total enterprises in the EU-27 which was 99,78%. (Eurostat, DIWecon, DIW, London Economic, 2013). As we can notice in the figure 2 and figure 3, both at national and European level there is a high asymmetrical distribution of the SMEs, a majority of them being micro-enterprises that have less than 10 employees according to the European definition.

We notice that there are slight differences in the structure of the sector by size in the sense that the share of micro Romanian enterprises is 89.03%, which is below the EU average of 92,27 percent. Small firms accumulate 9.13% of all SMEs, more than the share registered in EU of this size class (6.63%). This volatile area of companies is responsible in part for the low contribution to the growth of the entire sector.

High percentage of micro-enterprises is not likely conjectural. The explanation for the existence of the same very high percentage in the structure of the SME sector, over a long period of time may be related to several factors of influence:

- this is the first step in developing any business done by most of the entrepreneurs;
- low level of own funds;
- vulnerability and inability to survive in the economic environment;
- legislative factors;
- policy and fiscal measures that encouraged rather multiplication, the number of new legal entities than strengthen and develop of those already registered.

Figure 2: Distribution of Romanian's SMEs by size, 2012 (%)

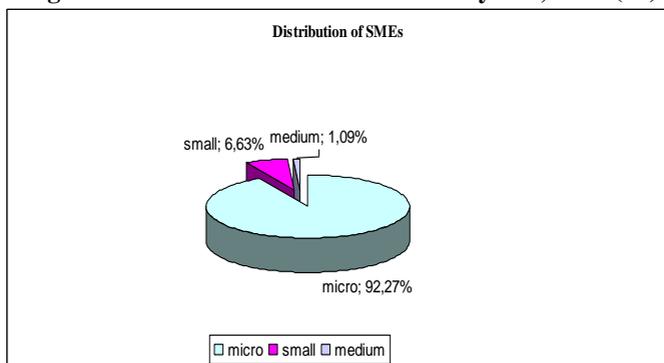


Source: data processing by authors, based on Eurostat databases 2013

To create the picture of the SME sector in Romania, we further analyze the performance of SMEs, using the following indicators: number of enterprises, number of person employment and gross value added.

Dynamic data analysis presented in the table below reveals two intervals of differentiated evolution in the number of active SMEs in 2008-2013. The first period was characterized by constant growth in the number of firms, so that the peak year 2008, reached a maximum of 504.581 SMEs respectively about 50% more compared to 2003. (Pîslaru, et al., 2012, p. 39).

Figure 3: Distribution of EU-27 SMEs by size, 2012 (%)



Source: data processing by authors, based on Eurostat databases 2013

Table 1: Enterprises, Employment and Gross Value Added of Romanian SMEs (all sectors)

Indicators/ Years	2008	2009	2010	2011	2012	2013
Total SME	504.581	489.646	442.241	435.788	437.126	474.416
Persons employed	2.904.965	2.626.121	2.443.818	2.519.954	2.522.128	2.623.448
Gross Value Added (mil Euro)	30.947	23.618	23.108	24.963	24.849	26.792

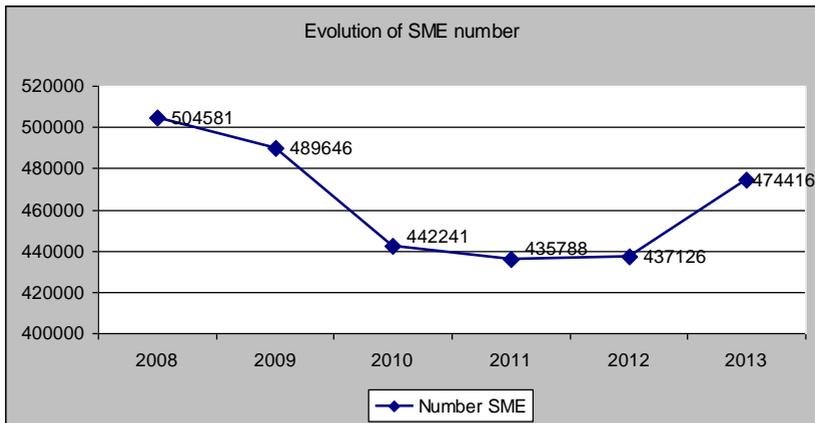
Table 2: Enterprises, Employment and Gross Value Added of EU-27 SMEs (all sectors)

Indicators/ Years	2008	2009	2010	2011	2012	2013
Total SME	20.255.804	19.966.234	20.912.116	20.720.451	20.355.838	20.614.113
Persons employed	88.323.609	87.646.250	87.528.611	87.426.846	86.814.717	87.092.299
Gross Value Added (mil Euro)	3.565.257	3.234.099	3.374.418	3.439.607	3.395.383	3.429.985

Source: Eurostat, DIWecon, DIW, London Economic, 2013

We can notice in the figure 4 that the positive trend of the number of SMEs at national level was stopped by financial and economic crisis which occurred since 2009. For the first time after a relatively long period of uninterrupted growth, the number of active SMEs fell by about 3% from the previous year. Decreasing trend was accentuated in 2010 when the number of active SMEs fell by another 9 percent from the previous year, reaching at 442.241 firms. This loss is basically a return to the level recorded in 2006 (Pislaru, et al., 2012, p. 39).

Figure 4: Evolution of Romanian SMEs number, 2008-2013



According to data, in 2012 a number of 437.126 SMEs were active, which represents a minor increase only 0.3% from the previous year. It can be concluded that approximately 67,000 active SMEs Romanian disappeared from the economic landscape during the crisis (2008-2012). *About 1 of 6 jobs lost* in SMEs in the European Union as a whole, during the crisis, were from Romania. (Pislaru, et al., 2012, p. 124). As we can notice in the figure 4 the trend is an upward one, and estimates show that the number of SMEs will get close to that recorded in 2008, showing that they still represent the main provider of jobs and overcoming the current crisis and renewed growth depends on them.

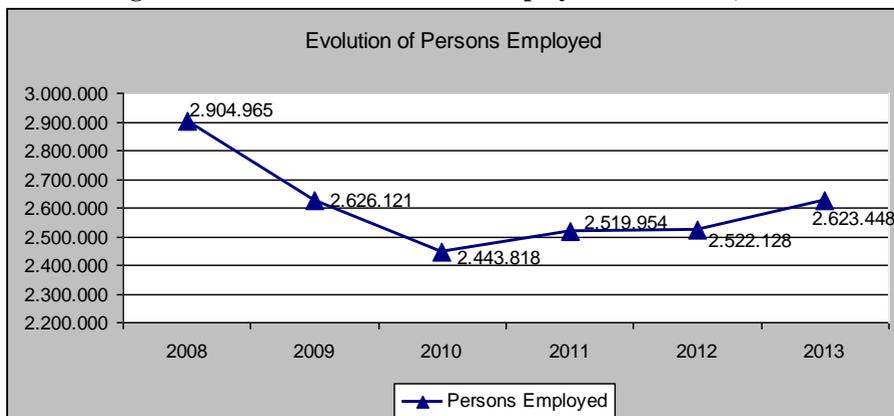
In Romania SMEs have consistently maintained a significant share of the number of employees in total employment in the non-financial business sector, with a value situated around 65% annually, comparable to that in the

EU-27 (66,9%), which means that 2/3 the total employed persons working in SMEs.

Thus, in the peak year 2008 SMEs engaged the largest number of employees (2.904.965), representing more than 65% of all employees in the non-financial business. It is worth to notice that the highest level of this percentage, almost 66.44% was achieved in 2009, the year marked by profound restructuring of staff in big companies.

Regarding the dynamics of employees' number data indicate that the average number of employees in SMEs decreased in 2010 by 7%, and since 2011 is increasing every year, with an average annual rate of 2.51%.

Figure 5: Evolution of Romanian employment in SMEs, 2008-2013



Source: data processing by authors, based on Eurostat databases 2013

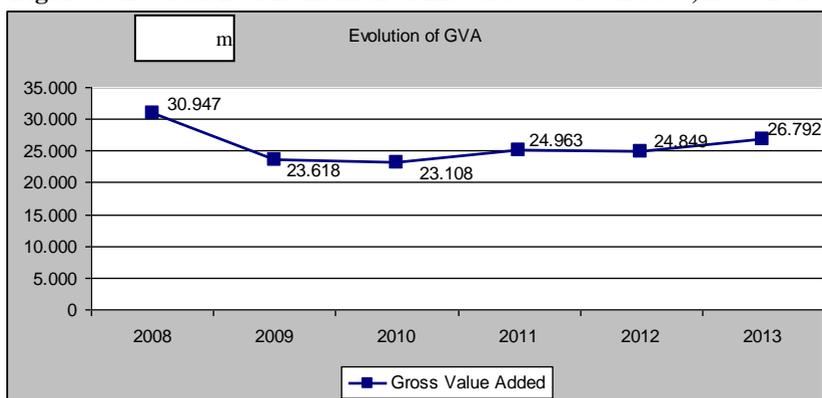
However, the SME sector in Romania has certain features that distinguish it in the negative sense of the EU-27 average. Although in the terms of employment domestic SMEs are in line with European average (about two-thirds of the total), differences arise when it comes to SME contribution to gross value added. The indicator is defined as the difference between the difference between output and intermediate consumption and is the main measure of economic growth (GDP is affected by changes in taxes).

In 2012 the sector's contribution to the creation of GVA was 50.89%, while the EU27 average was 58%. This situation is the consequence of lower average productivity in Romania (77.6% compared to the EU average of 86.7%), which negatively affects the competitiveness of SMEs but also

because many of them are classified in micro class or are not active and thus fail to contribute through their results to the growth of this indicator. In 2011, SMEs in Romania registered a positive growth of added value (+7.53% compared to 2009) without fully recover job losses caused by the economic crisis.

We believe that sustainable growth of SMEs is feasible especially in the manufacturing and services, both in urban and in rural areas, where the gross value added has greater effect of auto-generation and multiplication

Figure 6: Evolution of Romanian SMEs Gross Value Added, 2008-2013



Source: data processing by authors, based on Eurostat databases 2013

Following the trends (figure 1, figure 2, figure 3) it is found that the economic crisis has affected all three indicators from 2009 until 2012. The main problems which have faced SMEs between 2009-2012 were lower domestic demand, excessive taxation, bureaucracy, high costs of business financing, sever lack of liquidity, corruption, poor infrastructure, difficult access to credit, lower export demand.

Romania is one of the European countries most affected by the recession. Eurostat placed Romania on the last position among Member States regarding the evolution of performance indicators in particular the number of employees and gross value added. (www.postprivatizare.ro). Unfavorable situation can be explained by the fact that the pre-crisis economic expansion was based mainly on direct foreign investment, which who were severely restricted when the global economic crisis have been felt by foreign investors.

Being more dependent on domestic consumption market, SMEs have been affected by the severe decline of the national economy. The complex difficulties occurred could not be compensated by European funds available for SMEs, utilization of these funds being very low. This is a consequence of poor administrative management, and the lack of experience and knowledge of small entrepreneurship in implementing European projects from the requirements of the procedure.

Figure 7: Real value added and employment in the SME sector in 2011, EU 27 Member States



Source: Annual report on small and medium-sized enterprises in the EU, 2011/2012

In figure 7, Eurostat data for 2011 show that compared to 2008, only three countries have managed to improve both the real value added and employment of SMEs sector: Germany, Austria and Malta. In European Union countries economic activity has improved since the second quarter of 2013 and it is expected to gain strength later in 2013 and into 2014; therefore, projections for SME performance in 2013 and 2014 are mildly positive. The forecasts for the next two years indicate that SMEs in the services sector will continue to grow in terms of employment and value added and it is important the same trend to be recorded in the evolution of Romanian SMEs.

As we have seen in previous analyzes, SME sector in Romania keeps major vulnerabilities and they it is still far from the mature markets of Europe; therefore our country faces an important challenge in the next period to

remove these drawbacks and to become competitive through different measures and solutions. Therefore we propose further to discuss about the potential development of rural SMEs in Romania, as a solution to diversification of rural economy and to sustainable growth.

7. Opportunities and challenges for SMEs development in rural areas. Diversification of the rural economy

Importance of expanding SMEs in rural areas starts from the need of faster economic recovery from the crisis and diversification of the rural economy, in relation with the realities and specificities of our country. The rural economy is more developed and dynamic, as has a more diverse structure and the share of non-agricultural economy is higher.

In our opinion the development of a viable network of small and medium in rural area (agro-food or industrial enterprises, processing of local products, handicraft, mining and wood processing, agro-tourist houses the public and private services) has, in addition to important economic function, a remarkable social component. The last one refers to “stabilization” of rural population (primarily of the young), eliminates commuting and even migration phenomenon. Starting from the principle that the movement of labor is more expensive (economic and social) compared with the movement of materials and products, most European countries have changed location policy for SMEs, in the sense that they have moved business to labor force and not vice versa. Labor movement requires massive investments and complex social phenomena. In contrast, the location SMEs in rural areas means diversifying the economy, employment and stabilizes the rural workforce, increasing the economic strength of rural communities and contributes to the overall development of the economy.

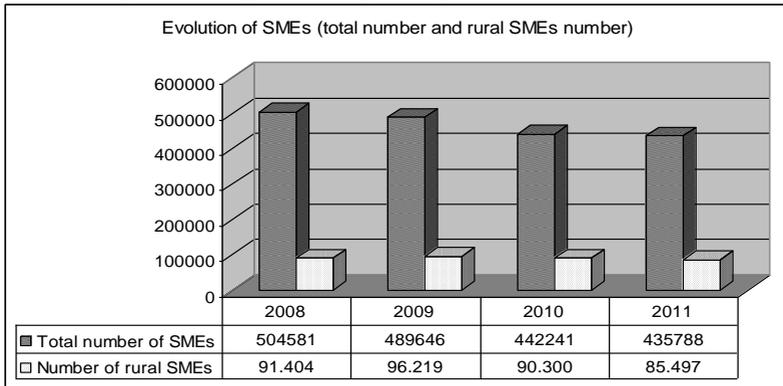
Rural development in Central and Eastern Europe (CEE) was frequently associated with agricultural development. Recently, opinion has begun to move away from this position. Attention is now focusing on the role of the non-farm sector in the context of rural development because of this sector’s potential for absorbing excess labor from agriculture, alleviating problems caused by urban-rural migration, contributing to income growth, and promoting a more equitable distribution of income (Junior, Pearce, 2001, p. 1).

In Romania, only about a quarter of villages have non-agricultural economic activities, organized as SMEs in the mining and quarrying, manufacturing, handicraft and agro-tourist activities. (C.N.S.R., 2014-2020-

2030, p. 37). We propose for development of non-agricol rural economy, performance by local authorities, mayors and councils of industrial micro-areas that contain all the necessary equipment, as we meet in most of the European countries.

Statistics on rural economy and rural SMEs shows that only 5.7% of Romanian rural economy is represented by the industrial activities (mining and manufacturing non-agricultural) versus 9.3% in the EU and Romanian rural services have accounted for, only 9.9% (compared to 42.2% in the EU) demonstrates unused potential of our country resources. (C.N.S.R, 2014-2020-2030, p. 38). Overall, non-agricultural rural economy has 21% share in total rural economy, compared with its share of 59.7% in the EU (C.N.S.R., 2014-2020-2030, p. 38), demonstrating once again predominantly agrarian character of the rural economy with consequences effects on the economic status and quality of rural life.

Figure 8. Disparities regarding the number of rural SMEs



Source: data processing by authors, based on Eurostat databases 2013 and MADR, 2013

In 2011, in rural area were approximately 85.497 small and medium enterprises out of 435.788 total SMEs in the country, mean a percent of 19,6%. An important indicator of the development of the SMEs sector is the number of SMEs per 1000 inhabitants, which reflects the density of SMEs. This indicator cannot be calculated accurately because in Romania there was a strong process of population migration both within national borders (from rural to urban areas and a less developed region to more developed regions)

and abroad (population migration to more economically developed countries). (Drob, Zichil, 2013, p. 9).

At the national level, there are still strong disparities between urban and rural areas with regard to the number of SMEs per 1,000 inhabitants. Thus, if in 2011 cities have approximately 23 SMEs/1,000 inhabitants, the rural areas have only 9,64 SMEs/1,000 inhabitants, resulting a national average of 16,5 SMEs/1,000 inhabitants, three time less then the European average, 52 SMEs/1.000 inhabitants. (MADR, 2013, www.madr.ro).

As a result, rural SMEs fail to contribute significantly to sustainable economic development of the rural area as long as there is not a sufficient number of companies and a favorable framework for their establishment and growth.

We believe that solving the problems faced by SMEs in our country and explore ways of development in rural areas should start from rural economic development strategy proposed by the EU for the 2014-2020 period and increase productivity in the agricultural sector. Agriculture and the presence of farmers in rural areas are essential components of rural dynamics and this is why rural development policy falls under the Common Agricultural Policy (CAP). (Chambon, et al., 2011). Furthermore, agriculture plays an important role in rural areas by generating additional economic activities, especially through close ties with processing, tourism and trade.

We have to consider that the development of the rural area is based on the concept of sustainable rural development and the expansion and diversification of the rural economy involves the integration of both agricultural and non agricultural activities. The development of non-agricultural activities and hence of services to rural areas is closely connected to the activity of family households practicing agriculture and rural development of small and medium enterprises. As the above data indicate, Romania is experiencing low levels of labor force employed in non-agricultural activities (www.madr.ro, MADR, 2013, p. 53).

The main challenges (obstacles) in opening and developing micro-enterprises in non-agricultural areas and especially in the rural services are due to lower level of education among population, lack of entrepreneurial culture, also lack of capital needed to start a new business, migration phenomenon and not least poor rural infrastructure.

Being educated is a fundamental component of the quality of life of an individual (Frank, et al., 2010). Moreover, education and training provision

play a role in determining levels of human capital, which, in turn, have an impact on rates of economic growth of the area. This is the reason because the development of the education and training for the population from the rural area is very important. Thus, the increasing of the life standards in the rural areas will determine the population to be less dependent on agriculture and to need new job's qualifications. These will attract the employees from the agriculture activities and therefore the SMEs would be ideal for offering such types of services.

On the other hand to strengthen the SME sector, the entrepreneurship must be encouraged, to support sustainable economic development (based on diversity using local resources) and to improve the employment of labor (especially in non-agricultural activities). In Small Business Act for Europe (2011), European Commission stressed that the main challenge is the need for a larger number of entrepreneurs, entrepreneurship culture being a powerful factor of economic growth and job creation. Entrepreneurial culture or entrepreneurial orientation refers to the proactive behaviour towards risk-taking ventures and innovation of the entrepreneurs.

Decisions makers and specialists should consider entrepreneurship as a priority and a solution to the economic crisis and mitigate the risk of slipping into poverty. Romanian rural area, are important reservoir of labor force (around 45% of total population), largely unused or partially used (according to INS, 2011, employment rate is 58,8% and registered a peak growth of 5.4% in 2009). Given that, encourage creating and developing of SMEs enterprises must become a strategic priority, through initiate special training programs and promoting entrepreneurship.

Regarding the leading to non-agricultural activities and services have identified a number of problems related to high interest rates charged by commercial banks to grant and system of fees and charges for various services provided by the bank (the opening of accounts, grant loans) (www.madr.ro, MADR, 2013, p. 53). In this context, a major role is played by the investment which can support the firms in acquiring the competitiveness in order to face the competition from the European market.

Concretization of entrepreneurship initiative by opening new businesses in the agricultural and non-agricultural rural area is justified by the natural potential of Romania, but also as a result of economic development policies, supported by public and european funds.

6. Conclusions.

Analysis of the overall situation of Romania SMEs, after joining the European Union and under the impact of global crisis, reveals a number of inabilities and vulnerabilities of small and medium enterprises which appear poorly prepared to compete successfully in the domestic market of the European Union.

With a share of 99.6% in total active companies, SMEs should represent the backbone of the Romanian economy as the basis for capitalizing entrepreneurship and development emerging private sector. But after analyzing the indicators, it turns out that the performance of this sector, under the impact of the economic crisis had been the most affected of all EU countries. If you approach from the perspective of employment value-added relationship, the results lead to the conclusion that this sector is less efficient in terms of resource capitalization.

It can be said that demographic evolution of Romania SMEs has been influenced by worsening market conditions caused by the economic crisis and the pace and magnitude of changes in the tax regime introduced by the Government, as measures to counter the effects of the crisis. These measures were perceived burdensome by the business and therefore many companies have ceased or suspended their activities.

In this framework, creating and developing rural SMEs is:

- a solution to diversify rural economy
- a factor of sustainable economic growth
- a way of employment and stabilization of rural population
- a key determinant in assuring a prompt and sustainable recovery from the economic crisis.

Given the specific and particularities of rural areas and national realities we can say that the future of SMEs in Romania will depend very much on attracting and using government and community funds to develop this sector, especially in the rural area where the potential for developing agricultural and non-agricultural activities can help reduce the gap between rural and urban, between Romania and other developed countries from EU. Also structural and financial policies combined with an innovation-friendly environment and entrepreneurial culture can provide greater opportunities.

The solutions for the rural Romanian enterprises in order to face the competition from the European market and for the sustainable rural development consist on the improving the access to the information,

financing, promoting entrepreneurship, developing of the infrastructure through attracting and proper use of structural European funds.

We consider that applying a model of multifunctional agriculture and rural development means to promote the development of the agricultural functions of the rural areas together with the promotion of non-agricultural functions of these areas. This model is compatible with the economic and social policy of the European Union, whose main objective is to reduce the development disparities between the EU regions and hence in reducing of the development gap between rural and urban areas.

We believe that urban-rural economic balance can be done through a permanent policy, adapted to the realities and specificities of our country and through economic and financial support by providing significant tax incentives. Otherwise rural SMEs still remain a “bird in the bush” for Romanian economic recovery.

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