

THE EFFECTS OF RURAL SMES' INVESTMENT ON ECONOMIC DEVELOPMENT

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Small and medium enterprises (SMEs) are generally thought to play a crucial role in driving economic growth in both developing and developed countries. They have the ability to answer in a flexible way to the competitive markets and to adapt to the structural and cyclical changes of the global economy. In the same time, the small businesses should be considered the force capable to lead to a better allocation of resources, introduction of new ideas and innovative products, new business methods, to generate more new jobs than large firms and they can push economic reform and the modernization of economies. Therefore is necessary to be done a research in order to find out what impact these enterprises have on growth and poverty or how such impact occurs. The analysis was based on a study regarding the rural SMEs, encouraging insights on the potential of these firms as a vehicle for growth and poverty reduction and some policy guidelines for the design of interventions to maximize this potential. The economic impact of investment in SMEs is significant, all the analyzed firms have achieved a significant positive economic rate of return. Also, new jobs were created and the enterprises provide substantial non-salary benefits. Many of these enterprises invest in training their workers during employment and this creates a substantial asset for employees, as it permits wage increases and a skill premium. As well, employees benefit from the stability of employment. Through investment, the rural SMEs introduce new business methods, products, and services which can lead to the restructuring of the agricultural sector. The rural SMEs help spread the benefits of economic growth by engaging low-income groups in national development. As well, they form dynamic supply-chain linkages between small-scale producers and lucrative urban, national, or export markets. In the reverse direction, they link large urban businesses with mass consumer markets. All these results suggest that it is well worthwhile for the development community and for the investors to put more effort into SME financing.

Keywords: rural SMEs, investment, economic development, financing.

The economic situation in Romania has improved over the last years and starting in 2001 the growth rate averaged more than 5 percent per year. Also the development of the financial sector has gathered pace and the domestic and foreign direct investments register a rapidly increase in the context of our country's accession to the EU. These favorable trends, however, are far from being evenly distributed over the territory: Bucharest and a few other big towns in more

favorable regions account for the bulk of the growth, while a large part of the country's economic potential, representing small cities and rural communities, is not fully utilized.

The Romanian rural area is confronted with many problems, as follows:

- the fragmentation of the agriculture farms; 94.4 million household have about 8.4 million hectares, which represent half of the arable area of our country;
- the agriculture population is too numerous (36.4% from the active population in Romania in comparison with 4.7% in EU);
- the poverty, the lack of the entrepreneurship and the low training level of the rural population;
- the weak performance of the agriculture farms.

Romania joined the European Union in 2007 with a lot of disparities in the rural field and has to recuperate the big gaps regarding the development level and also regarding the implication of population in the efficient administration of the small and medium business. These aspects are reflected in the recognition of its financial and technical needs, thus Romania would beneficiate by financing on all axes established by European Union, which could improve the correlation between SMEs sector investment and the rural development. In order to face the competition on the European market, the solutions consist in improving the access to information, services and financing.

Accordingly with the National Development Plan (NDP) 2007-2013, the rural development is one of the 6 national development priorities and will get an amount of 15.3 billion Euro, representing 26% from total financing allocation in the period 2007-2013 and the financing sources are the followings: EU funds - 43%; national public sources - 48%; private sources - 9%.

MATERIAL AND METHOD

For presenting the statistical data for Romania, there were used the official information, several reports and analysis regarding the rural development in the context of European integration. Among these studies are the followings: "Study regarding the situation and needs of the SMES in 2004", organized by the National Agency for SMEs and Cooperatives and the Yearly Report of the MIMMCTPL (Ministry of SMEs, Trade, Tourism and Liberal Professions).

As statistic methods there were used investigation methods.

RESULTS AND DISCUSSIONS

The impact of the SME sector has to be considered a complex one, involving economical, financial, social, cultural aspects. For the Eastern and Central European countries, small businesses have to be considered a force capable to lead to a better allocation of resources and to generate new jobs for those who lost them as a consequence of the restructuring process. The development of the SMEs sector should be the starting point because at this level, every individual is involved in the innovation activity, increase the responsibility and competitiveness, and this is the beginning for registering progresses at the level of communities, regions or states.

From the total Romanian SMEs, 20,3% are in the rural areas, most of them being micro enterprises (more than 90%). The structure of the number of SMEs employees by activity sectors, in 2004, indicate the following structure: 3,3% in agriculture, silviculture and fishery, 34% in industry and energy;10,7% in constructions and 52% in services.

The analysis of the rural SMEs reflects their relatively reduced capacity to meet the requirements regarding availability of jobs for the rural population, both due to the small number and to the structure by number of employees.

The most rural SMEs were created in the trade activities (48.6%), followed by the manufacturing (19.6%), agriculture (9.8%), tourism (7.2%), transports (5.9%), constructions (3.3%), services (5.3%) and extractive industry (0.2%) (figure 1).

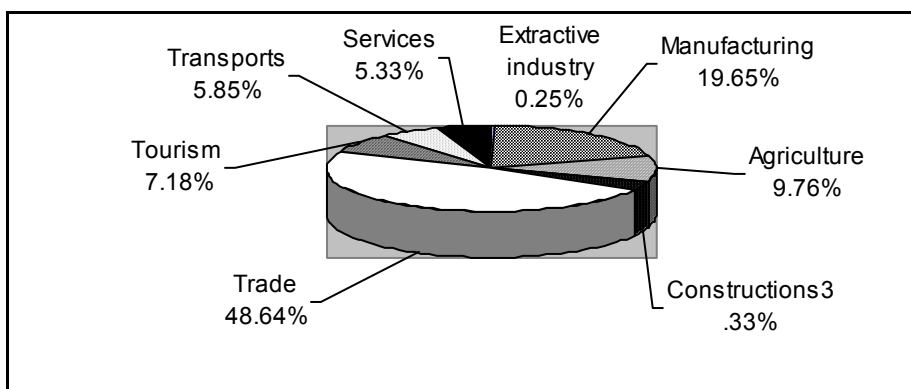


Figure 1. **The situation of rural SMEs – by activity sectors**
 Source: *Yearly Report of Romanian SMEs, 2005, MIMMCTPL*

The initiatives for creation new SMEs are oriented towards the trade sector because this involves reduced funds, shorter periods for covering the investment, and reduced experience in management.

The SMEs in the rural areas operating in the non-agricultural sectors represent 16% of the total non agricultural SMEs and are mainly operating in handicraft production, rural tourism, agro tourism, agricultural raw materials processing, transport etc. These businesses have a positive impact on the rural communities and contribute to the growth of these areas. However, the rural non-agricultural activities remain low and most of the businesses are micro enterprises.

The analysis of SMEs in the rural areas showed a relatively low capacity of SMEs to provide additional employment for the local village populations, due to their inability to grow and the available skills. In that sense, an important role is played by the persons who come back from urban areas to the rural ones. In general, they have a higher education level and are qualified in many industrial jobs but which can be adapted to the needed jobs for the rural communities.

As alternatives to occupation in agriculture, besides raw materials processing, there are opportunities in tourism, agro-tourism and handicraft, all having high development potential that can be further developed.

The unsolved issues of the rural area, coming from the impossibility of satisfaction the basic needs, including the poor development of basic infrastructure and basic services have impacts on the overall growth of the areas, their contribution to development and the improvement of living standard for the population.

In 2004, from the total rural SMEs, 48.1% did not do any investment, while 32.8% did small investment and 19.1% did major investments. The percentages are close to the investment situation registered by the total Romanian SMEs.

Table 1

SMEs investment on activity sectors

Activity sector	% IMM from total		
	no investment	minor investment	major investment
Agriculture, sylviculture, fishery	48,1	32,8	19,1
Industry and energy	33,4	49,7	15,4
Constructions	28,2	56,3	14,9
Trade	39,6	46,0	13,5
Hotels and restaurants	1,4	73,3	25,3
Transport and communications	46,8	41,8	7,3
Other services	43,3	38,0	14,1
Total SMEs	37,9	41,1	14,3

Source: *The Yearly Report of Romanian SMEs, MIMMCTPL 2005*

The framework that is used for assessing development impact is summarized by the groups which can be, directly or indirectly, affected through SME investment. The followings describe how each of the groups can be potentially impacted through SME investment:

- SME financiers should receive a private return, as measured in the traditional financial rate of return.

- Employees may receive higher wages than they might have received elsewhere (that is, higher than their opportunity cost) and they may receive training (which improves their human capital and thus raises their value in the labor market).

- Customers may receive a new good or service, not previously available, with a value to them that is greater than the price they pay; or they may receive a better quality product at the same price as before; or they may pay a lower price than they did before due to the increased supply on the market (resulting in an increase in their consumer surplus).

- Producers of complementary goods or services may see an increased demand for their own products, and hence higher sales and profits.

- Suppliers may see an increased demand for their goods, and hence increased sales and profits. A network of new suppliers may come into being, and the company may extend assistance to the suppliers (both new and old).

- Competitors may see a reduction in the demand for their product, but this is not a loss from the viewpoint of society as a whole but rather a shift in surplus to consumers. Competitors may gain the reputation of products sold by the company as well as from network gains resulting from the bigger market or improved suppliers.

- New entrants to the activity sector may develop as a consequence of the network effect.

- Local communities may be impacted in several ways. There may be environmental gains (or losses), new physical infrastructure may become available or become more congested, and a new social infrastructure may develop.

- Local governments may benefit from the value of profit or value-added tax revenues generated by the SME.

- Financial institutions such as local banks, pension funds, and insurance companies may benefit from SME investment.

Also, increased wages for managers and employees may result in higher savings placed in banks and/or pension funds (in turn, the banks/pension funds can then generate additional sources of financing for further development). Higher wages and better practices may also result.

CONCLUSIONS

Growth and modernization in the SME sector are often associated with successful economic development, particularly in lower income countries. In turn, such growth and modernization are associated with general poverty reduction.

SMEs have a large positive impact on their communities. The multiple paths by which these SMEs have affected their communities are the followings:

- The economic impact of investment in SMEs is significant. On average every dollar invested generates an additional ten dollars in the local economy. Also, the firms can achieve a significant positive economic rate of return, even before the investment is brought to term.

- Of the quantifiable results among stakeholders, the greatest share of benefits from the investments goes to employees, followed by governments.

- Two-thirds of total employment in the firms goes to low-skilled workers, confirming the hypothesis that SMEs generate new jobs that are suitable for the poor.

- Employees' annual real wage increase can be high: up to 28 percent for low-skilled workers and 34 percent for high-skilled workers.

- The enterprises provide substantial non-salary benefits, which are valuable to low-skilled workers who would not receive them were they self-employed.

- Many of the enterprises invest heavily in training their workers during employment. Being forced to hire people with relatively low skills, they tend to invest disproportionately in training their employees.

- The training creates a substantial asset for employees, as it permits wage increases and a skill mobility premium.

- Employee's benefit from the stability of employment. Along with the payment of health and social security benefits, this helps them to accumulate tangible assets and savings, hedging them against poverty.

- SMEs can provide access to formal markets for informal sector and rural producers; they form linkages between small-scale producers and lucrative national and export markets.

SME development is often seen as a critical component of growth strategies:

- SMEs generate many of the new jobs in the economy. Since many of these jobs are suitable for semi-skilled or unskilled workers, the poor can take them up.

- SMEs introduce business methods, products, and services that help restructure weak agricultural sectors or other uncompetitive transition economies, thereby absorbing labor that would otherwise drop into the ranks of the poor.

- SMEs help spread the benefits of economic growth by engaging low-income groups in national development. They form dynamic supply-chain linkages between small-scale producers and lucrative urban, national, or export markets. In the reverse direction, they link large urban businesses with mass consumer markets in remote areas.

All of these effects prove that the SMEs are an integral part of the communities in which they operate and contribute actively to community development.

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