

The Impact of COVID-19 on Romanian SMEs

Elena Rusu (Cigu)

Anca Elena Afloarei Nucu

“Alexandru Ioan Cuza” University of Iași,

Faculty of Economics and Business Administration, Romania

elena.chelaru@uaic.ro

anca.afloarei.nucu@uaic.ro

Abstract

In the context of the COVID-19 pandemic, all countries are facing a sharp economic recession. Small and medium sized enterprises (SMEs) are severely affected and thus the involvement of the state in the economy is inevitable. The purpose of the paper is to analyze the impact of coronavirus outbreak on Romanian SMEs. The research explores the literature regarding economic strategies and model in recession times. Also, based on descriptive analysis methodology, the status of SMEs in the 42 counties of Romania corresponding to NUTS 2. The paper can be considered a useful viewpoint in understanding the impact of COVID-19 on Romanian SMEs.

Key words: Coronavirus crisis, SMEs

J.E.L. classification: G32, O52

1. Introduction

The “lockdown” effect, with partial or total closure of some economic activities and the distancing or isolation of people has been generated high economic and financial costs. The reorientation of the activity of some enterprises (towards goods needed in the context of the pandemic), telework and the intervention of public authorities with supporting funds for SMEs are measures to attenuate the negative impact of COVID-19 pandemic, but the economic activity is dominated by a certain fragility and a considerable level of uncertainty.

The novelty of the paper is given by the fact that this paper analyzes the status of Romanian small and medium enterprises (SMEs) and explores the impact of COVID-19 on Romanian SMEs creating an initial viewpoint based on descriptive analysis methodology.

The paper is structured as follows: Section 1 briefly describes the literature review regarding the impact of coronavirus crisis on businesses. Section 2 presents the status of Romanian SMEs in terms of legislation, Section 3 provides information about the registration and deregistration of SMEs in Romanian counties, while the last section brings the main conclusions and the implications for development policy.

2. Literature review

In the light of coronavirus outbreak, the firms are facing new challenges in terms of financial constraints and have to adopt new business models. This line of research is new, but we can identify several pioneering papers analyzing the business environment under the impact of COVID-19. Wenzel et al. (2020) highlight that the competitive landscape of SMEs was negatively affected by coronavirus crisis. The firms are facing a decline in the demand of goods and need to adopt new costly processes (Amankwah-Amoah and Syllias, 2020). The pandemic has generated a demand and supply shock, many businesses looking for government support (subsidies, tax relief) and other financial and non-financial support (Cook & Barrett, 2020).

In Romania, the main challenge that non-financial companies faces is represented by the management of the effects produced by COVID-19 pandemic. In the context of the COVID-19 pandemic, almost a quarter of the companies were affected by reduced sales. Unlike SMEs, which have been affected to the greatest extent by declining sales by more than 75 percent, most corporations (61 percent) have registered a decrease of sales reductions by less than 25 percent. At the sectoral level, the turnover of companies from agriculture, construction and real estate was less affected, while at the opposite pole are the companies from services and utilities sectors. At the level of trading companies, exporters have suffered more from the pandemic, since half of them registered a decrease of sales higher than 50%, during the emergency period. Of the companies that import goods, 40 percent had registered more than 50% decrease of sales during the peak restrictions (NBR, 2020). The declining exports and imports took place mainly as a result of the decrease in demand for products from two groups: machinery and transport equipment, groups that have an important share in the structure of both trade flows.

The most common measures taken by companies to overcome the negative effects of the pandemic on their business, at the aggregate level, are: the reduction of the activity, the suspension of the activity or the technical unemployment of employees. On the other hand, the least popular measures are: the application of the insolvency procedure or judicial reorganization procedure, suspension of the bank payments or dismissal of the employees. It is recognized that corporations were more proactive, compared to SMEs, in taking measures to reduce the negative effects of the pandemic. Therefore, corporations have resorted to the telework regime for some or all employees, while in the case of SMEs, only a small percent had the infrastructure needed to use this solution.

3. Legal overview

The legal framework in Romania for SMEs is complex and started to be developed of the beginning of '90s based on harmonization with the European Union and international legislation. Law no. 31/1990 on companies (republished) gives the main legal framework on Romanian companies, establishing Agricultural Cooperatives (AC), European Economic Interest Group (EEIG), Economic Interest Group (EIG), Family-Owner Business (FOB), Individual Enterprise (IE), Authorized Natural Person (ANP), Autonomous Administration (AA), Joint Stock Company (JSC), Cooperative Society (CS), Limited Partnership (LP), and Limited Liability Company (LLP). The legal framework is supplemented by a multitude of other normative acts such as: (i) Law no. 346/2004 on stimulating the establishment and development of small and medium enterprises, amendment and completion by the Law no. 346/2004; (ii) Law no. 1/2005 regarding the organization and functioning of the cooperation; (iii) Decision no. 1065/2010 for the approval of the Framework Agreement between the Government of Romania and the Swiss Federal Council on the implementation of the Swiss-Romanian Cooperation Program aimed at reducing economic and social disparities within the enlarged European Union, signed in Bern on September 7, 2010; (iv) Commission Regulation (EC) No 1407/2013 of 18 December 2013 on the application of Articles 107 and 108 of the Treaty on the Functioning of the European Union to de minimis aid; (v) Emergency Ordinance no. 10/2017 to stimulate the establishment of new small and medium enterprises; and (vi) Law no. 112/2017 regarding the approval of the Government Emergency Ordinance no. 10/2017 to stimulate the establishment of new small and medium enterprises.

The normative framework in the conditions of COVID-19 was completed with a series of normative acts, respectively 39 normative acts of primary level, 12 normative acts of secondary level, and 75 tertiary level normative acts.

The main legislative measures that have had an impact on the way in which public authorities, institutions and entities with special responsibilities have used the public funds allocated for this purpose can be grouped into the following categories: 1) Legislative measures adopted in the field of public procurement; 2) Legislative measures adopted in the field of health; 3) Legislative measures adopted in the field of labor and social protection; 4) Legislative measures adopted in order to ensure the support of the economy; 5) Legislative measures aimed at general actions to limit and control the spread of the pandemic with COVID-19.

The legislative frameworks with significant impact on SMEs are the following (Coalition for the Development of Romania, 2020):

- Emergency Ordinance no. 29/2020, subsequently amended and supplemented by Emergency Ordinance no. 42/2020, considered to prevent the spread of COVID-19 virus and limit its negative effects through a series of measures that targeted the public health sector, as well as measures to limit the negative effects caused by the limitation or interruption of socio-economic activities.
- Emergency Ordinance no. 30/2020 clarified some aspects regarding some days off to the parents for the supervision of the children, in the situation of the temporary closure of the educational units. For staff that cannot benefit from days off, financial incentives are provided. At the same time, new social and salary benefits are introduced for the emergency period.
- Emergency Ordinance no. 33/2020 aimed at stimulating the payment of due tax obligations, taking into account the needs of financing budget expenditures, by granting payment bonuses for taxpayers who have the financial capacity to pay corporate income tax / income tax to micro-enterprises. At the same time, in view of the need for medicines, protective equipment, other devices or medical equipment and sanitary materials that can be used in the prevention, limitation, treatment and control of COVID-19, a postponement of the customs payment of VAT has been made to support economic operators who import such goods.
- Emergency Ordinance no. 37/2020 created facilities for the payment of installments and interest due for loans to debtors, individuals, Family-Owner Business, Individual Enterprise, Authorized Natural Person, Autonomous Administration, small and medium-sized enterprises and NFIs.
- Government Decision no. 268/2020 regarding the amendment of Government Decision no. 807/2014 for the establishment of state aid schemes aimed at stimulating investments with major impact on the economy.
- Government Emergency Ordinance no. 48/2020 on some financial-fiscal measures considered the extension of the income tax deduction of micro-enterprises and sponsorships made according to law, to public institutions and authorities, including specialized bodies of public administration, to ensure the necessary resources to finance public institutions, in mainly in the social and medical field.

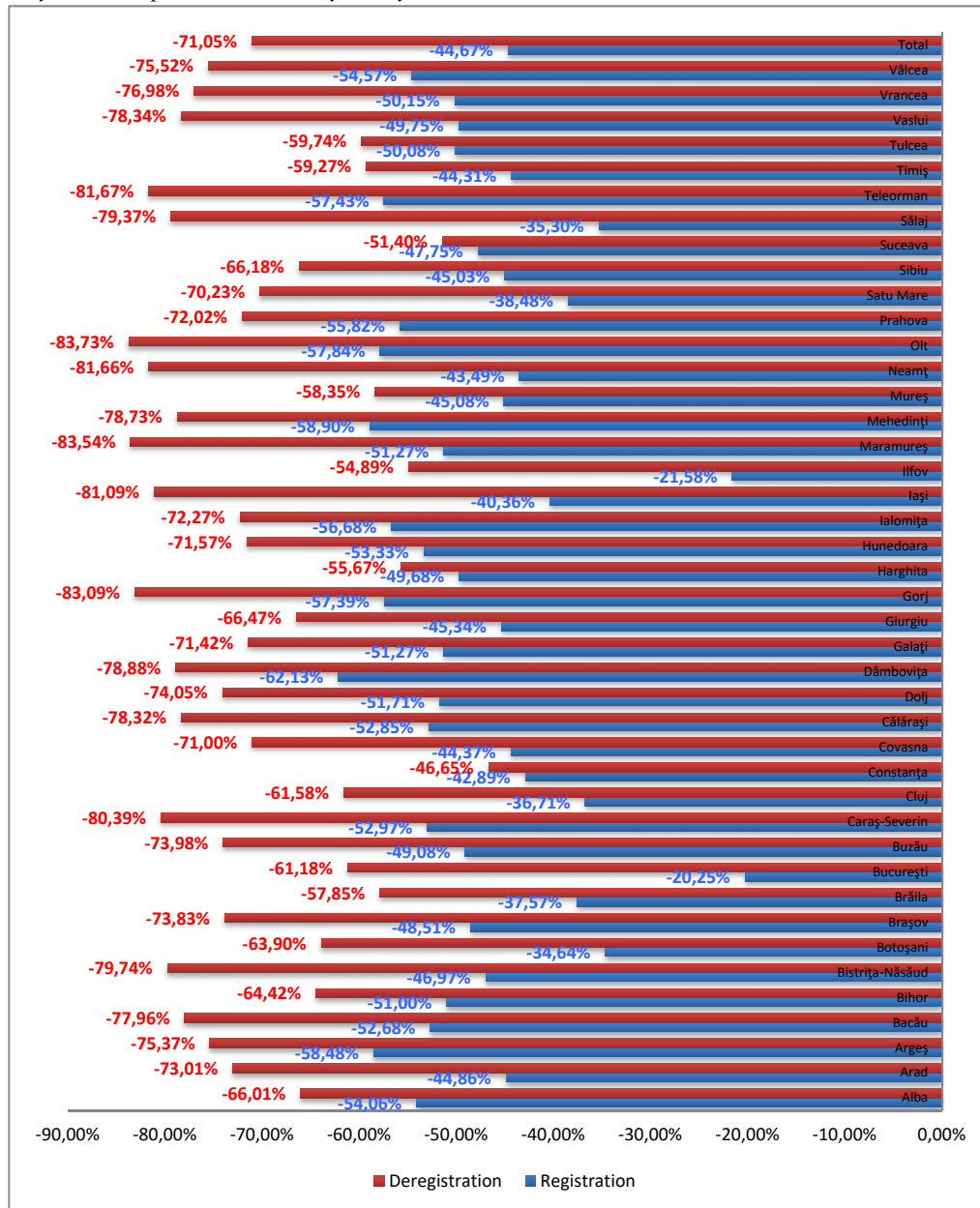
4. Empirical evidences of SMEs in Romanian counties

Analysts assess the current state of the economy as given the limited capacity of the Romanian supply to cover the surplus of domestic demand, imports maintained a robust growth rate, their unfavorable footprint on the trade balance being doubled by the modest course of exports, affected by the prolongation of international tensions. This pattern of economic growth has been accompanied by a deepening of the budget deficit and the external one, thus accentuating the question marks regarding its sustainability.

However, the challenges to the economy intensified with the onset of the COVID-19 pandemic in the first months of 2020. The supply shock caused by the measures of isolation and social distancing intended to flatten the epidemic curve materialized in the appearance of syncope in supply-production chains, affected the activity in multiple fields (NBR, 2020). From a demand perspective, beyond the emotional amplification, for a short period of time, of the purchase of essential goods, the shock wave associated with the rapid spread of the epidemic has the potential to cause longer-term changes in the behavior of all actors in the economy (NBR, 2020). Thus, at the level of internal absorption, the adjustment of wage incomes (as a result of the decision taken by many companies to send their employees into technical unemployment or to close the business) eroded consumer demand and fueled the sharp deterioration of public confidence, with possible consequences and at the level of investment inclination. At the same time, the turmoil in the activity of the corporate sector and the inherent uncertainty on the future evolution of the business climate are likely to discourage capital accumulations among companies. The mobilization of important budgetary resources to cover the social needs and support of the affected companies is done at the cost of a slowdown in public investment. At the same time, external trade in goods and services has lost intensity both on the export side (as a result of the restriction of the activity of the main trading partners, with a direct effect on the local manufacturing sector and on freight transport services) and on imports with the adjustment of the internal absorption, but also of the demand of inputs for the manufacture of the

products with external destination.

Figure no. 1. Dynamics in Registrations and Deregistration of SMEs over the period of time January – May 2020 compared with January – May 2019 in Romanian counties



Source: computed by authors using database of National Office of the Trade Register (2020)

Figure 1 presents the Dynamics in Registrations and Deregistration of SMEs over the period of time January – May 2020 compared with January – May 2019 in Romanian counties.

According to Figure 1, there was a decrease of approximately 45% of registered companies in National Office of the Trade Register and main reason for such a decrease is just COVID-19 pandemic. Over the period of March 16 and May 14, 2020, all activities in Romania were lockdown. Of the 42 counties, including Bucharest, 20 of Romania's counties show a decrease of over 50% in the number of companies registered in the comparative period, these being Vâlcea, Vrancea, Tulcea,

Teleorman, Prahova, Olt, Mehedinți, Maramureș, Ialomița, Hunedoara, Gorj, Galați, Dâmbovița, Dolj, Călărași, Caraș-Severin, Bihor, Bacău, Argeș and Alba. The smallest decreases are registered in Bucharest, with respectively 20.25%, and in Ilfov, with respectively 20.25%. These two counties are also those that form one of the eight development regions of Romania, corresponding to NUTS 2, respectively the Bucharest-Ilfov Region, which is also the most developed in the country.

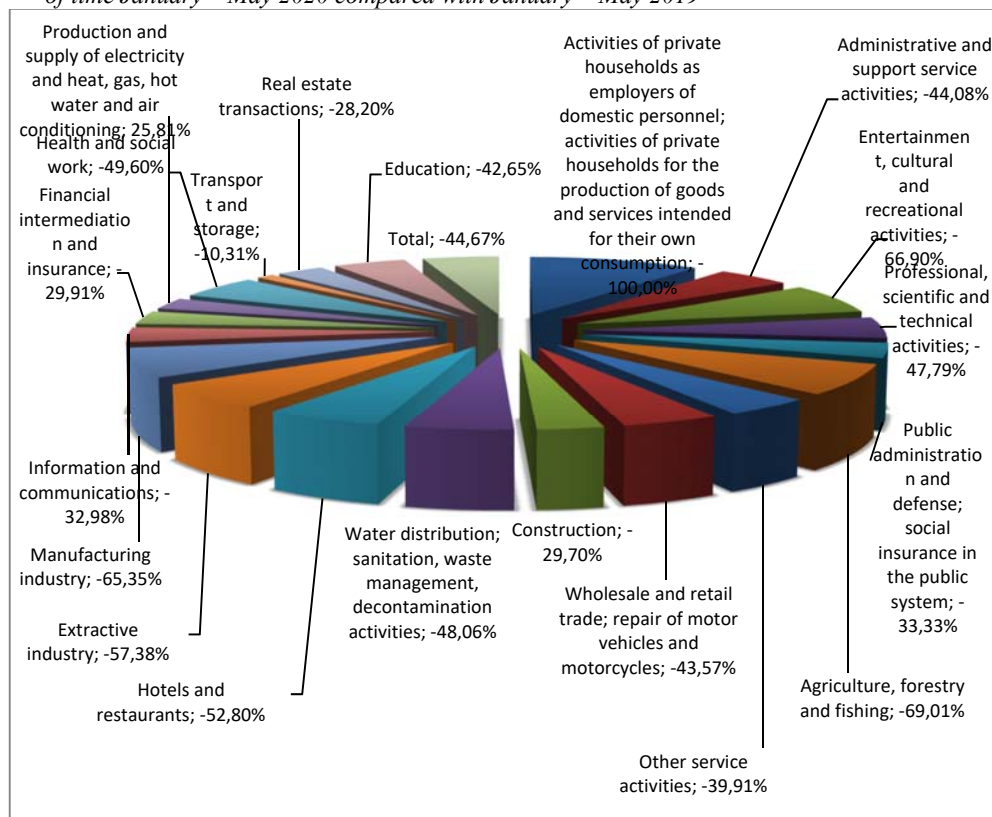
Regarding deregistration of SMEs was significantly lower compared to the same period of the previous year, respectively a decrease of approximately of 71%. The low rate of deregistration is justified by state intervention with financial support of companies in difficulty due to the COVID-19 pandemic. The best-positioned counties with a percentage of over 80% are Teleorman, Prahova, Olt, Neamț, Maramureș, Iași, Gorj, and Caraș-Severin.

The highest gap between registered and deregistered companies is in Buchares, Iași, and Sălaj. This gap must be interpreted as the best positioning in the management of small and medium enterprises.

The evolution of small and medium enterprises by classification of activities in the national economy can be seen in Figure 2.

According to Figure 2, based on classification of activities in the national economy, the highest gap is registered for activities of private households as employers of domestic personnel; activities of private households for the production of goods and services intended for their own consumption, where there is a decrease of 100%. Entertainment, cultural and recreational activities registered a decrease of approximately 67%, manufacturing industry of 65.35%, Agriculture, forestry and fishing of 69.01%. The best positioned is transport and storage, which determined a decrease compared to the same period of the previous year of only 10.31%. The most companies were registered in the field of Wholesale and retail trade, repair of motor vehicles and motorcycles (8667), but nevertheless there was a decrease in this field compared to the same period of 2019 of 43.57%.

Figure no. 2. Registrations of SMEs by classification of activities in the national economy over the period of time January – May 2020 compared with January – May 2019



Source: computed by authors using database of National Office of the Trade Register (2020)

A large number of companies registered between January-May 2020 are in the field of Construction with 5155 companies and a decrease of 29.70% compared to the previous year. Investments in construction objectives increased by more than 25%, in the context in which, in addition to prolonging demand pressures, this sector benefited from incentives in terms of labor market regulations (setting a consistent minimum wage threshold, granting scaling facilities and relaxation of employment conditions outside the Community). Thus, the construction of buildings has expanded by almost 40%. The constructions with industrial-logistical destination were maintained on a robust trajectory, although the new delivered surfaces did not accumulate the record level from the previous year. However, the evolution of this segment - which has a high potential, given the low stock of modern spaces available to Romania compared to other countries in the region - continues to be hampered by the insufficient development of transport infrastructure.

The most affected sectors by COVID-19 pandemic were HoReCa (76%), Transport and Logistics (69%), Production (64%) and Services (63%).

The SME INVEST ROMANIA program, approved by Emergency Ordinance no. 29/2020, establishes that the Romanian state guarantees 80% or 90% of investment loans and credit lines related to working capital contracted by micro, small and medium enterprises and will benefit from grants for the payment of interest and commissions up to 800,000 of euros each.

The budget of the state aid scheme is 781 million lei (161 million euros), and the maximum guarantee is 15 billion lei (3.1 billion euros), with the maximum duration of financing of 6 years in the case of investment loans and 3 years in the case of working capital loans. Loans / lines of credit for working capital can be extended for a maximum of 3 years. The maximum value of loans / credit lines for working capital financing is 5 million lei, and for investment loans, the maximum value of financing is 10 million lei. Also, the cumulated loans granted to a company will be within the total limit of 10 million lei.

Ensuring the continuity of the activity of SMEs, companies and companies in the private sector was achieved through measures on technical unemployment, respectively:

- Regulating the conditions for achieving technical unemployment during the state of emergency and ensuring the necessary funds to support it from the unemployment insurance budget;
- Regulation of tax measures and benefits for employees whose individual employment contracts have been suspended during the state of emergency, at the initiative of the employer, as a result of the effects produced by COVID-19, such as: (i) the calculation by the employer of the calculation, withholding and payment of income tax, of the state social insurance contribution and of the social health insurance contribution related to the indemnities from which they benefited; (ii) taking into account the period of suspension of employment during the state of emergency established by law, when establishing the contribution period of at least 12 months in the last 24 months prior to the date of registration of the application for unemployment benefits; and (iii) recognition of the period of emergency, in which the individual employment contracts were suspended and for which the employers did not owe the insurance contribution for work, as an internship assimilated in the unemployment insurance system.

Romanian Court of Accounts (2020) states that at the end of the state of emergency (May 13th, 2020), out of the total number of 54,498 SMEs that applied for financing under the SME Invest Romania Program, a number of 11 applications were approved by banks, for which the National Guarantee Fund Loans for Small and Medium Enterprises (NGFLSME) concluded 3 guarantee contracts, related to the application of 2 SMEs. Out of the total of 64,282 SMEs that have applications/requests registered at the National Credit Guarantee Fund for Small and Medium Enterprises on June 25th, 2020, a number of 5,488 applications were approved by banks, representing a percentage of 8.5%. At the same time, out of the number of applications approved by banks, NGFLSME issued 1,451 guarantee contracts, representing a percentage of 26.4% of the applications approved by the bank, for a number of 1,418 SMEs. Until June 25th, 2020, guarantee contracts amounting to 588,379 thousand lei were issued, representing a percentage of 3.9% of the ceiling of 15 billion lei. The largest share of SMEs that applied for financing was registered until May 13th, 2020, the date of completion of the state of emergency. Between May 13th and June 25th, 2020, the number of SMEs that applied for financing increased by 18%, while the number of guarantee contracts issued by NGFLSME increased from 3 to 1,451 guarantees. Although NGFLSME concluded agreements with 22 credit institutions participating in the State Aid Scheme through the

SME Invest Romania Program, only 2 complied with their obligation to submit information on loans guaranteed under the SME Invest Romania program until May 31st, 2020.

5. Conclusions

The COVID-19 context has led to important changes in the evolution and financial performance of SMEs, so that the economic recovery requires a concerted effort by national and international authorities. In the case of Romania, it is necessary to introduce the Institution of the credit mediator for SMEs to identify problems, regarding legal, economic or bureaucratic issues, that provide solutions to SMEs for obtaining financing from banks and to notify the Government in case of major problems related to business lending. Given the limited fiscal space existing before the pandemic, the financial resources provided by the EU is a remarkable opportunity, whose values involve the identification of viable projects that can contribute to a sustainable economic recovery.

At the national level, there is a necessary program for quick access to cash (e.g., 10,000 - 15,000 euros) for SMEs that can be used only for an SME urgently needs (to not close the company), such as salaries, rents, utilities, health expenses in work or adaptation to telework. The loan under consideration should be reimbursed the entire amount without any interest.

6. Acknowledgement

This work was supported by a grant of the "Alexandru Ioan Cuza" University of Iasi, within the Research Grants program, Grant UAIC, code GI-UAIC-2018-06“.

7. References

- Amankwah-Amoah, J., Syllias, J., 2020. Can adopting ambitious environmental sustainability initiatives lead to business failures? An analytical framework. *Business Strategy and the Environment*, 29 (1), pp. 240-249.
- Coalition for the Development of Romania, 2020. *COVID-19 medical crisis and the Romanian economy*. [online] Available at: <https://fic.ro/Documents/view/CDR-TF-Macroeconomic-The-COVID-Medical-Crisis-and-Romania-s-Economy> [Accessed 03 October 2020].
- Cook, L., Barrett, C., 2020. *How Covid-19 is escalating problem debt*. [online] Available at: <https://www.ft.com/content/4062105a-afaf-4b28-bde6-ba71d5767ec0> [Accessed 02 November 2020].
- National Bank of Romania, 2020. Annual Report 2019. [online] Available at: <https://www.bnr.ro/Publicatii-periodice-204.aspx> [Accessed 24 October 2020].
- National Office of the Trade Register, 2020. Statistics. [online] Available at: <https://www.onrc.ro/index.php/ro/statistici> [Accessed 13 October 2020].
- Romanian Court of Accounts, 2020. *Management of public resources during the period state of emergency - Special report made at the request of the Romanian Parliament*. [online] Available at: http://www.curteadeconturi.ro/Publicatii/Raport_stare_urgenta_11082020.pdf [Accessed 28 October 2020].
- Wenzel, M., Stanske, S., Lieberman, M.B., 2020. Strategic responses to crisis. *Strategic Management Journal*, 41, pp. V7-V18.