

## PERFORMANCE THROUGH INTERNATIONALIZATION AS A STRATEGIC OPTION FOR SMES

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**Abstract:** *Internationalization is often considered a strategic option for SMEs, but a large part of small firms' contribution to internationalization is not reflected in statistics, as many of them participate indirectly in the global economy as suppliers of exporting firms. The export-oriented model of SMEs seems to follow the general strategic choices, most SMEs do not export at all, and most exporting SMEs are regular companies. The literature mentions a number of characteristics that distinguish companies that are likely to export such as group membership, consistent expertise, size, rapid growth and innovation orientation, production experience or collaborations in production and distribution. At the European Union level, the recognition of the role of internationalization in increasing the performance of SMEs and the performance of the economy as a whole is complemented by extensive support measures, which prove both their direct role (volume of exports and imports, degree of international cooperation, profitability, turnover, competitiveness) but also their indirect role, to train young companies, dynamic in the world economic circuit.*

**Keywords:** SMEs, European Union, internationalization, performance, strategy.

**JEL classification:** L26, M16, F15.

### 1. Introduction

The internationalization of entrepreneurial firms is often presented as a feature of modern, dynamic and knowledge-intensive times, a profitable, complex and risky option at the same time. However, the internationalization of entrepreneurial businesses is not a recent phenomenon, and one in which the complexity and risks are associated only with the specifics of the contemporary period. According to Etemad (2018), entrepreneurs of past historical periods have faced greater risks, complex political, economic and social situations, with personal difficulties almost unimaginable nowadays. Documented historical information on entrepreneurship in international trade dates back to ancient times, with the famous Silk Road, a network of roads that connected major cities in Asia and Europe for almost 1600 years, referred to, in fact, much later, as "roads of silk". The very long missions, the risks, the losses and the lack of information and security suggest the enormous uncertainty and complexity of these activities. They required great adaptability, flexibility and other

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Cite as:

Cenan (Ciucos), M., and Badulescu, A., 2022. Performance through Internationalization as a Strategic Option for SMEs. *Oradea Journal of Business and Economics*, 7(1), pp. 86-97, <http://doi.org/10.47535/1991ojbe140>

outstanding entrepreneurial traits, active relationships with partners, buyers, suppliers, inventing and developing a multitude of support services for concluding transactions. Later, European traders faced similar uncertainties, taking great risks in their continental or intercontinental travel, expressing those attributes we now call "entrepreneurial" orientation, capacity, commitment and motivation, adaptability, interaction management, risk-taking and complexity management.

## **2. Literature on the relationship between internationalization and entrepreneurial performance**

Located at the crossroad of entrepreneurship and international business, contemporary international entrepreneurship focuses on a strategy that combines innovative, proactive, and opportunity-seeking behaviour across national borders to create value in organizations (McDougall & Oviatt, 1996), (Oviatt & McDougall, 2005). Such a strategy allows firms to actively pursue opportunities for growth and innovation in foreign markets, enhancing firms' performance (Zahra, 2005). However, entrepreneurial internationalization also exposes firms to uncertainties and risks that require adapting internal routines and processes to new external environments - a resource-consuming challenge that can affect firms' performance. Considering these divergent arguments, it is not surprising that empirical findings from different studies and contexts are largely inconclusive, and it still remains unclear to what extent entrepreneurial firms should pursue an internationalization strategy to succeed in various limited conditions.

The main argument is that valuable resources allow firms to pursue (internationalization) strategies more efficiently, and according to the knowledge-based vision (Schwens, et al., 2018), knowledge is the most important strategic resource of a company, allowing the company to gain competitive advantages and maintain these advantages as long as the company's knowledge retains its value (Amit, et al., 1993). Internationalization is an effective means for entrepreneurial firms to exploit and explore valuable knowledge abroad, as long as the dispersion of knowledge can be prevented (Oviatt & McDougall, 2005). An entrepreneurial firm depends on the inherent knowledge in its activities and previous results and this knowledge is a valuable resource, a source of competitive advantage, ensuring performance in the case of the internationalization option.

Although the internationalization and performance of firms is a multidimensional phenomenon (Zahra & George, 2002), we must distinguish between the dimensions of internationalization (i.e. the degree, scope and speed of internationalization) and the performance of that firm (i.e. growth and profitability). The initial emphasis of the relationship between entrepreneurship - performance - internationalization, starts from the motivations of companies that internationalize fast and proactively shortly after their start-up (McDougall & Oviatt, 1996), (Oviatt & McDougall, 2005). Another perspective is to analyze the cross-border expansion of entrepreneurial firms, regardless of their size and age (Zahra, 2005), a considerable part of the relevant literature investigating young and small firms crossing national borders, (such as *born global*, or young firms attracted to the opportunities offered by new international projects). Another area of theory focuses on the cross-border entrepreneurial expansion of larger and more established firms.

In general, entrepreneurial firms are characterized by the specificity of their activities, by the involvement of innovation and risk-taking as they expand (or reduce) their international operations (Zahra & George, 2002, p. 260). While early research assumed a positive linear relationship between internationalization and business performance, a broader view considers both the benefits and costs of an internationalization strategy, as innovation is by nature proactive and risky (Schwens, et al., 2018), and therefore may have potentially negative implications for performance (McDougall & Oviatt, 1996).

Zahra & George (2002) identify three key dimensions of an entrepreneurial internationalization strategy: (1) the degree of internationalization refers to the percentage of an abroad (foreign) sales in total sales and expresses the extent to which the firm is exposed to foreign markets, (2) the scope of internationalization covering the number of countries or regions in which the entrepreneurial firm is active, thus indicating the diversity of the company's international activities, and (3) the speed of internationalization describing the period of time between the setting-up of the firm and its first foreign sales indicating the "precocity" of a firm's exposure to foreign market environments (Khavul, et al., 2010), (Zahra & George, 2002). Thus, the degree, scope and speed of internationalization are relevant dimensions to understand the various aspects of the internationalization of an entrepreneurial firm (Khavul, et al., 2010).

Company's performance is considered a major outcome variable in international business and strategy (Rauch, et al., 2009). Firms can achieve an increase at the expense of short-term profitability, for example an international increase through aggressive price reduction strategies, leads to an increase in market share, but to a declining profitability (Schwens, et al., 2018).

The existing literature that studies the relationship between internationalization and performance among entrepreneurial firms provides largely mixed results. For example, some research reports simultaneous sales growth and profitability, while others show that while sales growth is considered a significant positive effect of internationalization, international diversity and return on investment can have positive, negative, or insignificant influences (Zahra, 2005), (Schwens, et al., 2018). Moreover, McDougall and Oviatt (1996) do not find any significant direct relationship between the share of international sales in total turnover and the return on investment of new technology-based enterprises. In contrast, other research reveals that the extent of internationalization is significant (though marginal) and positively related to profitability, but not to sales growth. Finally, there are analyses that find even a negative and significant effect between internationalization in terms of export intensity, and the performance of small firms.

The "entrepreneurial" behaviour of internationalized firms seems to contribute to their success abroad to a greater extent than broader variables, such as firm size or age (McDougall & Oviatt, 1996). On the other hand, the intensity of knowledge can negatively influence the relationship between internationalization and performance, highlighting the risks for knowledge-intensive companies, technology, etc., which enter various foreign markets and the efforts required to integrate diverse foreign knowledge. The intensity of knowledge positively mediates the relationship between the speed of internationalization and performance. Many theories argue that less pre-existing knowledge allows early internationalized firms to enjoy the learning benefits because firms have less "baggage" that prevents them from seeking new knowledge abroad (Autio & Acs, 2007), (Gustafsson & Autio, 2011). In contrast, other theories claim that more pre-existing knowledge helps firms that internationalize early to absorb new foreign knowledge more efficiently.

### **3. Development and internationalization of entrepreneurial companies in the European and global context**

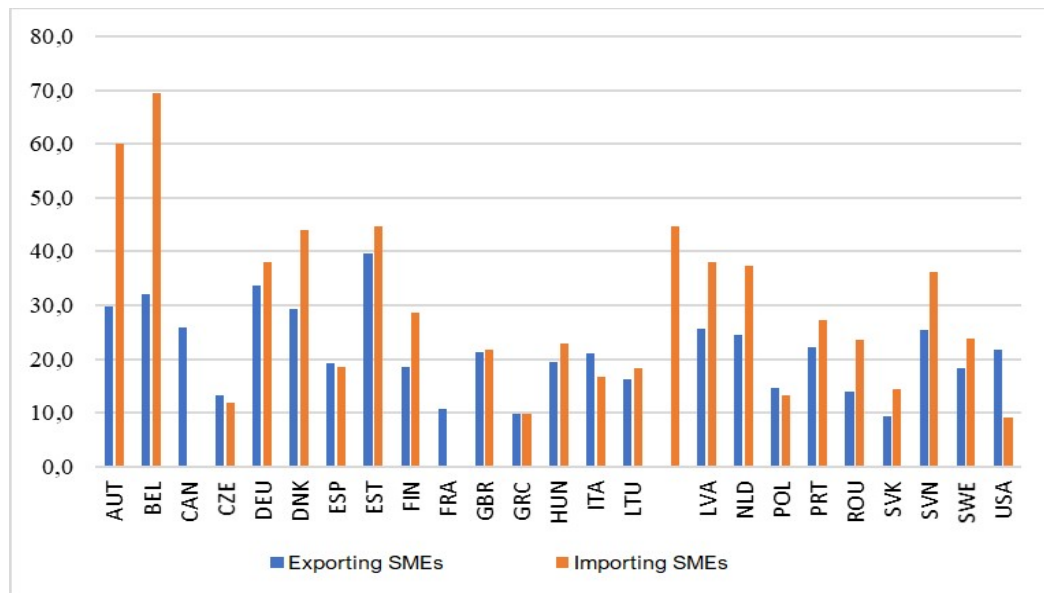
The internationalization of entrepreneurial firms is a specific topic, often presented in a favourable light as inherent in the development of this type of business. Growth is a crucial part of their strategies and direction, as evidenced by the fact that almost 90% of young European firms say they intend to internationalize, or increase their degree of internationalization in the next twelve months (Steigertahl & Mauer, 2018) (Bormans, et al., 2020).

Successful capitalization of foreign markets has proven to be a major driver of the recent growth of many EU' SMEs. There are several ways in which SMEs can expand internationally - by exporting or importing goods and services, by making foreign direct investment abroad, or by attracting foreign investors to their business, becoming part of a national value chain which also has an international component, through involvement in cross-border research and development and collaboration in innovation, or by licensing or franchising certain products or services.

Most European start-ups usually start expanding to neighbouring (EU) countries and then try to move to larger international markets. According to surveys, 77% of these firms have plans to internationalize in the EU in the next 12 months, and about 36% want to do so (and) outside the EU (in North America and then in Asia), 26% in the EU and outside the EU, and 11% have no such intention (European Commission, 2015).

### 3.1. The situation of the internationalization of SMEs in the European Union, and the OECD

According to OECD statistics, “the share of enterprises participating in international trade varies significantly from country to country, ranging from 10% to 40% for exports and from 10% to 70% for imports” (OECD, 2017). Small countries tend to have higher levels of involvement in import-export operations, reflecting the limited size of their internal market, although there are substantial variances from one country to another. In almost all economies and in all size classes, the number of importing enterprises is usually higher than the number of exporters, and the United States is a notable exception (OECD, 2017), see Figure 1.



**Figure 1.** Share of exporting and importing SMEs, in total firms involved in exports, respectively imports, OECD countries, 2017 (in %) Source: (OECD, 2021a)

There are significant differences between SMEs of different sizes in terms of participation in international trade. On average, 15% of micro-enterprises in OECD countries are involved in international trade, while for small enterprises the share reaches 60% and for medium-

sized enterprises up to almost 80%. Finally, the export sector is relatively concentrated, the top 100 exporting companies in each country have a significant share of that country's exports, and this percentage can range from about 25% in Italy to over 90% in Luxembourg (OECD, 2017). Data that reflect only direct export (and import) channels may underestimate the true scale of integration into global value chains, especially by size classes of firms. For example, upstream SMEs may participate in global value chains by providing goods and services to larger exporting firms, but their importance is often underestimated, and this in most cases refers to small size, usually micro-enterprises.

If we analyse the internationalization of firms, depending on the size class, we find that, although between 25 and 70% of exporting firms are micro-enterprises, they represent only a limited part of the total value of exports. Micro-enterprises active in wholesale and/or retail commerce have play a significant role in stimulating import-export activities. They include about three-quarters of all companies in the sector engaged in international trade and approximately 15-50% of total imports and exports in the sector. In general, compared to large firms, small firms are more likely to export to markets relatively close to their country of origin, which is explained by the impact of fixed costs, which tend to be relatively higher for smaller firms. Barriers to importing SMEs seem less expensive than those to export activity. Another result of this analysis is that the value of exports (imports) relative to the firm's turnover is generally higher as the firm is larger and the economy is smaller (OECD, 2017), see also Table 1 below. These include countries such as Ireland and the Netherlands, which host many foreign multinationals with a high use of intellectual property, and which have the highest export rates in OECD turnover.

**Table 1:** Ratio of export value to turnover, by size classes (SMEs and large firms), OECD countries, in 2017\*

	Export		Import	
	SMEs	Large firms	SMEs	Large firms
Austria	31.33	51.94	21.48	31.04
Belgium	40.06	43.77	27.15	35.12
Czech Republic	25.47	45.88	18.23	29.14
Germany	17.73	34.43	10.80	17.58
Denmark	31.26	41.69	15.49	16.73
Spain	23.32	28.75	14.45	30.77
Estonia	51.78	62.50	30.57	43.04
Finland	20.93	35.79	11.31	22.62
France	16.49	27.73	13.15	22.19
UK	17.03	24.93	14.20	21.18
Greece	24.66	38.38	22.60	55.45
Hungary	31.18	53.05	27.09	43.98
Ireland	69.79	62.25	16.59	17.46
Italy	23.48	32.75	11.50	19.12
Lithuania	46.12	65.67	33.55	62.19
Latvia	47.09	33.25	24.79	23.46
Netherlands	37.14	39.99	24.25	33.37
Poland	24.03	35.60	15.76	28.51
Portugal	25.43	46.58	18.64	41.51
Romania	30.05	50.66	26.88	38.54
Slovakia	34.43	61.38	26.36	46.18
Slovenia	32.23	71.05	23.78	38.10
Sweden	23.86	44.82	14.15	21.92

	Export		Import	
	SMEs	Large firms	SMEs	Large firms
Turkey	11.56	18.51	14.22	32.51
United States	9.39	12.51	8.97	14.76

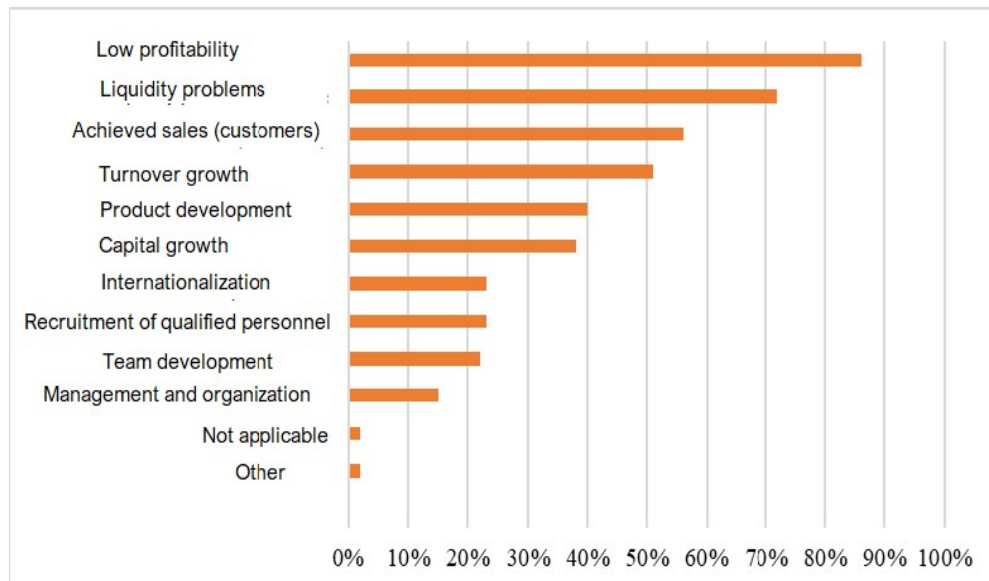
Note: \* or the most recent year available  
 Source: (OECD, 2021a)

Differences in participation in international trade between size classes and by country may highlight important barriers to participation in international trade, especially for smaller firms (OECD, 2021a), (OECD, 2017).

### 3.2. Internationalization and competitiveness as strategic options for SMEs

Entering new foreign markets is not an easy task and it is important to find those factors that can best help SMEs to internationalize. As a rule, SMEs refrain from entering new markets because they do not understand or have the ability to control the risks associated with operating abroad. This is why when asked to specify their needs in this sector, most mention "providing information on external markets, their legal and regulatory environment", "connecting with new partners", "guidance and training needs", and "providing financial support" (European Commission, 2015).

Thus, entrepreneurs face many challenges such as: lack of stable external relations (55%), adequate financial support (43%) and insufficient knowledge of differences in legislation (38%), or difficulty in adapting production and products (23.3 %), language barriers (20.7%) and cultural differences (32.4%) (Steigertahl & Mauer, 2018), (Bormans, et al., 2020). Ensuring acceptable profitability (86.2%) and cash flow (72.3%) (Figure 2) are considered by most start-ups to be the biggest challenges of internationalization. Expanding into new markets is done to gain access to more potential customers, higher sales and possibly more financing.



**Figure 2:** Difficulties and tasks facing start-ups in business development and internationalization

Source: (Bormans, et al., 2020), (Steigertahl & Mauer, 2018)

Encouraging SMEs to become more innovative and export-based is based on consistent policies and arguments – about two-thirds of European SMEs currently operate in sectors with either low knowledge and technological intensity or are poorly visible on export, with a very high concentration of micro-enterprises and small enterprises with less than 50 employees (European Commission, 2018). Similarly, about 90% of SMEs are active in sectors with low and very low export intensity (see Table 2).

**Table 2:** Distribution of EU SMEs in value added generation, employment and number of enterprises between sectors with different export intensities

Intensity of export sectors	Micro	Small	Medium	Micro	Small	Medium	Micro	Small	Medium
	Number			Added value			Employment		
Very high (over 40%)	0,9%	0,2%	0,1%	0,6%	1,9%	4,3%	0,6%	1,4%	2,8%
High (20-40%)	3,2%	0,5%	0,1%	1,4%	2,8%	3,7%	1,8%	2,6%	3,0%
Medium (10-20%)	4,8%	0,6%	0,1%	1,6%	2,6%	3,7%	2,8%	3,2%	3,5%
Low (5-10%)	28,0%	1,0%	0,2%	10,9%	7,4%	7,7%	10,7%	5,3%	5,4%
Very low (0-5%)	56,3%	3,5%	0,5%	20,8%	16,3%	14,3%	27,4%	17,5%	11,9%

Note: Export intensity – the share of exports in total sales, calculated for each industry  
Source: (European Commission, 2018)

According to the latest data, SMEs are more active in the Single Market, which is somewhat to be expected. The small size and limited human and financial resources of SMEs (Badulescu & Badulescu, 2010), (Badulescu & Petria, 2011), typically prevent these firms from expanding globally outside the EU, with nearly 25% of SMEs importing from other EU Member States and half of the number of SMEs imports from outside the EU (European Economic and Social Committee, 2017). An even smaller share of SMEs (7%) dare to export their production globally.

### 3.2. Improving the performance of companies through internationalization and the role of public support

Various research and surveys conducted by the European Commission over the last decade (EIA (Pantheon), 2010), (European Commission, 2010), (European Union Open Data Portal, 2015) have shown a strong correlation between internationally active SMEs and business performance, better than average. Although part of this effect may be due to "self-selection", in the sense that better performing SMEs are more likely to be active internationally, it is very likely that there will be a direct, positive effect on business performance. Which become active internationally. This will also have an effect on the performance of the national and European economy and, in addition, there may be indirect effects, for example, on learning and innovation. Surveys cited by these studies have shown that SMEs active in export-import operations have much higher employment increases than other SMEs: nearly 7-8% in the case of import-export operations compared to SMEs operating only on national markets, and by more than 15% in the case of SMEs involved in foreign direct investment, compared to SMEs that do not benefit from this investment.

Whether we are referring to SMEs active in international activities, or to SMEs with concrete plans to become active internationally, we can assert that they report an increase in employment of 7%, compared to only 1% for SMEs without plans or effective involvement in

international activities. Secondly, the evolution of the turnover in a few successive years shows a positive correlation between the active firms at international level and the faster growth of the turnover. The effect is particularly high for SMEs that invest abroad, SMEs that are subcontractors of a foreign company and SMEs that have foreign subcontractors, respectively, about 20% of them reported that the turnover increased "quite enough" in the last three years, while for ordinary SMEs the average is only 12%. Moreover, SMEs firms that have invested abroad and those that have been involved in external technological cooperation have increased by more than 50%, compared to an average of 33% (EIM (Panteia), 2010).

Thirdly, surveys confirm the strong correlation between internationalization and innovation, with over 25% of internationally active SMEs introducing new products or services for their sector in their country, while for non-internationalized SMEs this percentage is only 8%.

Internationalized SMEs perform above average, i.e. they are more competitive than non-internationalized SMEs, in the long-term, because internationalization and innovation complement and stimulate each other.

They already indicate the need to combine internationalization and innovation when designing government support for this type of enterprise. Public support can indeed play a role in promoting greater internationalization of firms, and especially SMEs, with some firms acknowledging that they would not have internationalized without this support (European Union Open Data Portal, 2015). More than half of domestically active SMEs mention that they have identified growth opportunities at the international level as well, clarified or encouraged by the existence of support measures for internationalization. Public support can also make a valuable contribution by addressing those issues that are perceived as the main obstacle to internationalization: access to information and access to financial support. However, it is important to note that not all public support is equally effective, it needs to set clear quantitative targets and objectives, tools for monitoring and evaluating results, to ensure that support reaches the intended recipients and avoids wasting resources (EIM (Panteia), 2010), (European Union Open Data Portal, 2015), (Yu et al, 2020).

### **3.3. Internationalization of Romanian SMEs**

Regarding the access to the Single Market, the reports of the Small Business Act (SBA) show that Romania performs below the EU average in this respect. In 2017, Romania had the lowest percentage of SMEs with intra-EU online imports and exports. The ease of market access in 2015 for new and growth-oriented firms is among the lowest in the EU, the same low level being valid for the percentage of public contracts provided by SMEs abroad in 2017 (European Commission, 2019).

Regarding the field of internationalization of SMEs, based on the latest available data "Romania performs in accordance with the EU average in this regard. Although Romania has one of the lowest scores in the EU for SMEs exporting online outside the EU and for SMEs with exports of goods outside the EU, Romania performs substantially above the EU average in terms of procedures and formalities prior to import-export operations" (European Commission, 2019). Moreover, the "World Bank's Doing Business Romania 2020 Report shows that Romania has, out of all 10 chapters, the maximum performance (100) and rank 1 in Trading across Borders" (Herte & Badulescu, 2020).

In recent years, "Romania has made limited progress in policies and economic measures to support SMEs in this area, only a few programs implemented providing financial and information support to SMEs that help them internationalize~ (Herte & Badulescu, 2020), i.e. to do business abroad. Single access points have been set up for information on rules and regulations on foreign markets (Ministry of Business Environment, Trade and Entrepreneurship, 2019) (Ministry of Economy, Trade and Business Environment, 2019).



According to the European Start-up Monitor (Bormans, et al., 2020), (European Commission, 2019) Romanian SMEs have a low degree of internationalization, most of these businesses address their products or services to the local market, more exactly the population of the locality where it operates (36%). Approximately 34% of new firms trade products and services for the national market and only 30% from them went abroad, more precisely 10% are focused on regional markets and around 20% are active on international markets (European Commission, 2019).

In the future plans to expand into new markets, internal or external, start-ups entrepreneurs intend to enter with their business in new geographic markets (external) in a proportion of nearly 50%. The preferred area of expansion is the regional one, Europe, targeted by nearly 51% of those who plan to enter new markets. “A significant number of start-ups intend to enter the US market (17%) and a relatively small proportion of such firms (10%) are thinking of expanding nationwide” (Ernst & Young Global Limited, 2019), see Table 3.

**Table 3:** The main new markets (domestic or international), targeted by a possible expansion of the Romanian SME business

<b>Internal</b>	Cities in Romania (10%)		
<b>External</b>	Europe (51%), <i>of which</i>	Germany	7%
		Bulgaria	3%
		Hungary	1%
	Asia (5%), <i>of which</i>	China	2%
	North America (18%), <i>of which</i>	Canada	1%
		USA	17%
	Africa (1%)		
Globally (3%)			

Source: (Ernst & Young Global Limited, 2019)

The most important difficulties and obstacles mentioned by young business entrepreneurs are the lack of capital for investment (45%), limited resources for promotion (38%), the lack of qualified staff (35%) and the lack of clients (34%).

Sources of financing, for growth and expansion, international or not, “are often different, not so much in their variety but in frequency of use, compared to already established or young firms, but not necessarily innovative” (Herte & Badulescu, 2020). Traditional ways of financing (such as the founders' personal savings - 78% of cases, or support from family and friends - 30.2%) are the most frequently invoked, but they are followed by Business angels (29%), venture capital (26%) or various equity investors (21%), government grants/funding (20%), crowdfunding (18%). Compared to “ordinary” SMEs that add bank loans to personal resources, and family and friends; start-ups are more opened to unconventional (crowdfunding) or risky (capital investors) financing. Working with other businesses can be a way to overcome challenges and access new markets and opportunities. The survey conducted by Bormans, et al. in 2020 shows that about 29% of new firms work together with large companies, and the majority of them seem to be international trade with goods and services, but also high-tech cooperation, followed by cooperation with traditional SMEs (41%), universities (11%), other start-ups (9%), governmental agencies and institutions or NGOs (11%) (Bormans, et al., 2020). The reasons are diverse, but we can notice - 84% for access to new markets and customers or 42% for improving image, reputation and commercial know-how transfer.

#### 4. Conclusions

In this article we have analysed the link between the performance of small and medium enterprises, in relation to the exit on new foreign markets. It is a fact that the internationalization of European SMEs has significantly contributed to economic growth in recent years, exports of SME goods from the EU-28 have increased by 20% in the last 5 years, and the Single Market is proving its importance and special character for EU' SMEs. However, SMEs are internationalizing on the basis of strategic choices, in which political support can play a decisive role in influencing this choice. Finally, there are high expectations that policy measures aimed at stimulating currently non-exporting SMEs to relocate to foreign markets to give results in the future and that many SMEs currently operate in sectors that are characterized by a low level of knowledge, technological intensities or openness to export. Internationalization can support economic growth and well-being and improve the performance of firms, also generating indirect effects on learning and innovation, by opening up to newness, cooperation in various fields, dissemination of knowledge and production techniques.

Given the importance of the internationalization of SMEs in the European economy, both in terms of turnover and added value growth, but especially in employment, technological dynamism and innovation, the role of public support for internationalization is becoming essential. Some of the SMEs that use public support measures have acknowledged that they would not have internationalized without this support, many of them have identified growth opportunities at the international level as well, clarified or encouraged by the existence of support measures for internationalization.

Measures are required to make this support more effective, to set clear quantitative targets and objectives, tools for monitoring and evaluating results, to ensure that support reaches targeted recipients and maximizes resources in tangible results, encouraging firms to real internationalize, in the medium and long term

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