THE FINANCIAL MANAGEMENT OF THE SMALL AND MEDIUM SIZED COMPANIES IN ROMANIA

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Abstract: The objective of the paper is to identify the possibilities and promotion limits of the financial management in the small and medium sized companies in Romania starting from the concepts expressed in the literature and expressed in the concrete situations in the Romanian economy practice. We have also presented the role of the financial management in small and medium sized companies and the risk management objective of financial management considering that the risk is a fundamental component of a strategic and tactical decision. At the end of the paper we have presented the conclusions stemming from the study, the basic one being that there is a beginning in the promotion and applicability of theoretical elements of financial management in small and medium sized companies in Romania together with the European integration.

Key words: small and medium sized companies, financial management, investment, risk, economic profitability

1. INTRODUCTION

The essential objective of financial management must be maximizing the company's value.

The role of financial management is to follow and give response to the following:

· The assets and projects in which the company has to invest
· The best forms of financing such investments
· The distribution or reinvestment of the profits obtained.

Also the financial management is to provide methods and techniques by which they can evaluate and classify investments for finally the most profitable to be chosen, and on the other hand it means the connection with financial market, i.e. how to get funding we need.

The financial management's role is to help us find the optimal structure of capital, not only in terms of the costs involved, but also of their chargeability, it also helps to effectively manage the obtained profit. The company is required to know at any time the ratio of the effect produced on the one hand and the effort made, on the other hand, to appreciate and provide a vision for the future to assure a comfortable position in facing competitive market. It is therefore a suitable financial instrument allowing the company to carry out a proper financial analysis and formulate a competitive strategy. This financial instrument is actually made of all financial indicators.

In relation to the company's solvency, there is the question of its indebtness calculated with the help of the indebtness indicators: total debt ratio and net debt ratio.

Dg = (Dl + Dm + Ds) / Atot and

Dn = (Dl + Dm + Ds) / Cs

where:

Dg - indicator of overall debt

Dn - the net debt ratio

Dl – the long-term debt

Dm - the medium-term debt

Ds - short-term debt

Atot - total assets

Cs – the social capital of the company.

Rates of profitability are the rates of results and are presented in several forms, namely:

· Rates of commercial profitability;

· Rates of economic profitability;

· Rates of financial profitability.

A) The commercial profitability appreciates the sales performance assessed at different stages of business formation activity result, being determined as the ratio between the accumulation and turnover margins or the value added. From the category of these rates we mention:

a) the commercial rate margin (RMC) is used primarily by companies with trading activity and it is determined by the report between the reference margin (CM) and the turnover without VAT (CA):

$$R_{mc} = \frac{MC}{CA} 100$$

RMC reveals the commercial strategy of the company, which may be interpreted as: the increase of RMC, accompanied by a decrease in sales (CA), means that the company is trying to maintain the margins by promoting a policy of high prices. The declining trade margin rate, accompanied by a strong increase in sales (CA), points out that the company prefers to reduce the selling prices in order to conquer a new market segment. The increase of RMC, accompanied by an increase in CA, shows a favourable situation for the company, that the sale of products with superior performance or filling the new position on the competitive market.

b) The rate of the gross operating margin (R_{mb}) measures the gross operating surplus (EBE), independent of the financial policy, the investment policy, the incidence of taxation and other exceptional items:

$$R_{mb} = \frac{EBE}{CA} 100$$

R_{mb} reflects the ability of the activity to relieve the operating profit, its increased value inducing its financial business opportunity of the rapid renewal of the production equipment. The improvement of R_{mb} also expresses a productivity growth since R_{mb} is not a simple consequence of RMC increase, and its decrease in its relation to a stable RMC proves a burden on the operating costs.

c) The rate of the operating income margin (Rme) measures the relative level of income, regardless of the financial policy, the tax incidence and the incidence of exceptional items, but given the company's investment policy. It is determined by comparing the operation result (RE) to the turnover without VAT (CA):

$$R_{me} = \frac{RE}{CA}100$$

B) The economic profitability concerns, in essence, the effectiveness of the economic capital allocated to the productive work and takes the form:

The economic profitability rate (Rre) is calculated as a ratio between the operating result (RE) and the total assets (TA) or a part of total assets (Ai) and measures the profitability of the entire invested capital of the company or parts thereof:

$$R_{re} = \frac{RE}{TA}100;\ R'_{re} = \frac{RE}{A_i}100$$

C) The financial profitability is the firm's ability to achieve the net income from the capital employed in its work. It reflects the ultimate goal of the shareholders in a company, expressed by the rate of the remuneration of the capital investment made by them in buying the shares or of the total (partial) reinvestment of the rightful profits. The financial profitability is expressed by means of several categories of rates, depending on the items considered, namely:

a) The rates of net income (Rm) or the profit rate highlights the return on the turnover of 100 um and is determined by:

$$R_{rn} = \frac{RN}{CA}100$$

Rrn indicates the difficulties in equity investing for a low value, and the high value reflects the relative ease in attracting funds from the financial market.

b) The net profitability of the own capital (Rn), which is determined by reporting the net result of the exercise (RN) to the own capitals (Cpr):

$$R_{n} = \frac{RN}{C_{pr}}100$$

c) The profitability of the permanent capital (RCP) is calculated by reporting the net result of the exercise (RN) plus the interest related to loans (D0), to the own capitals (Cpr) plus the medium and long term loans (Dtml):

$$R_{cp} = \frac{RN + D_0}{C_{pr} + D_{tml}}100$$

A high value of RCP indicates an efficient use of the permanent capital and the low value of the report shows that the investments made by the company, financed by the medium and long-term loans, have not had the expected effectiveness.

The financial profitability of the permanent capitals shows the payment of the own capitals by providing dividends and the payment of the loans through the interests. For the listed companies, the financial profitability is determined by using rates determined on the basis of accounting and stock sizes. In this case, instead of the own capitals we are dealing with stock exchange value.

One key objective of the financial management refers to the risk **management in the activity of a small and medium sized company.**

Each entrepreneur has to quantify the risk which his/her commitment to a particular business involves together with the resource assessment.

At the same time we consider that after the completion of an investment, managers should continuously monitor the rate at which the investment is recovered in regular income in order to prevent potential risks that may jeopardize the future business activity.

The risk means the probability of an undesirable event occurrence.

The risk of an asset, various managerial finance professionals think, is defined by the probable variability of the future profitability of the asset. The risk equals the vulnerability of the company that can occur in all the sectors (commercial, technical, human, financial, etc.) so that its analysis involves numerous researches, which highlights the weaknesses of the economic and financial activity.

In general, the risk is defined as the possibility that future revenues are different from those expected to achieve. In other words, the risk is the variability of the revenues under the influence of the environment, involving the event of an adverse event.

The International Accounting Standards considers that the risk describes the variety of the results. The risk adjustment may involve increasing the value on which duty is assessed. In evaluating the results and contingent expenses of uncertainty, the precautionary principle must be applied not to overstate assets and not to undervalue the liabilities. However, the elements of uncertainty do not justify the creation of excessive provisions or underestimation of the obligations.

The risk in the business activity must be seen as a possible variability of the recovery of amounts invested in that business. Under these circumstances, the management decisions can be divided according to the conditions of their adoption, in three categories: decisions under conditions of certainty (safety), decisions under risk and decisions under conditions of uncertainty (uncertainty). The difference between risk and uncertainty is that risk means those situations where the likelihood of event is known. In the case of uncertainty, however, these probabilities cannot be known.

Regarding the business risk typology, from the multitude of risk classification criteria, we consider particularly those aimed at the policies relating to the business activity, within a competitive economy.

Thus, according to the number of options considered in the adoption of a strategy we identify:

· the unique risk specific to a single alternative, with one single probability to be achieved;

· the substantial risk for several variants, differentiated in value, with different probabilities of achievement;

Depending on the manner of the anticipation of events that will occur following the adoption of a strategy, risk can take two forms, namely:

· Potential risk, which means anticipating an event that would occur in the future or anticipate the effect of an event in progress, and

· Real risk, which means the transformation of a potential risk into an undesirable event.

Depending on the risk area, risk can be:

· Political, which mainly concerns the political instability. The political risk refers to the political climate and conditions of that country. The political risk is the lack of security of an investment because of the political regime in a country.

· Social, characterized primarily by the social demands, and

· Economic, characterized by the general state of economic structures. The economic risk is an uncertain event or process that can cause a loss, a loss in an activity, an operation or an economic action. Unlike uncertainty, the economic risk can be characterized by the possibility of the description of a probability law (rules) for the expected results, as well as for the knowledge of this law by those interested.

The economic risk can take, in turn, two forms namely:

– objective risk, which is characterized by the variation of the possible results, and it is a variable independent of the individual.

- subjective risk, which is the estimation of an objective and depends on the individual, on his/her information, on the temperament and the attitude.

According to the degree of aggregation, the risk can be identified on three levels:

· Regional risk, which concerns a geographical area;

· Country risk (macroeconomic) characterizing the overall condition of a country, and

· Microeconomic risk, identified at the level of the economic agents.

The risk at the microeconomic level is classified according to the location of its generating causes, with such external risks and internal risks of the company. The external risk occurs because of the action of factors outside the company. This category includes:

- Political risk (the country);
- Currency risk;
- Risks of natural character;
- Interest rate risk;
- Market risk (beta or systematic).

The internal risk has its origins in the particularities of each company and is closely related to the management, the organization and the enrolment of the business activities, namely the quality management actions (production, commercial, financial, marketing and personnel) and the execution.

We know that within the small and medium sized companies in Romania the specific criteria required by the financial management are not applied consistently and at the right level, but there is a beginning in that the banks, the guarantee funds and the government agencies that administer the structural funds have specific instruments, methods and techniques to assess the creditworthiness of a small or medium sized company requesting financial resources. In this context the specific business risk is well monitored.

The efficient management of businesses requires the ongoing monitoring of risks in a dynamic business system consisting of the following components:

· Setting strategic targets of the business administration;

· Profit management;

· Choosing the best business funding strategy.

We agree that the strategic goals of the business of a company can not ignore:

- business development portfolio;
- market research;
- assessment of production costs;
- assessment of the profitability threshold.

Profit management involves the best financial decisions of the profit-sharing for:

- the remuneration of the social capital;
- the remuneration of the foreign capital (interest);
- strengthening the capacity of self-financing of the enterprise.

The financing strategies of the current businesses consist on one hand in providing the resources and on the other hand in their use in accordance with the financial, short-term policy of the company, and which can be implemented through self-financing decision and / or short-term debt decision.

The investment strategy requires the adoption of appropriate financial policies, which permanently take intro account the manner of strengthening the infrastructure by self-financing or by increasing long-term indebtedness.

The online payment of taxes and the fees for setting up companies, and also the internet transmission of reports required by the authorities are the objectives of a project recently launched by the Ministry of Economy, with the deadline for implementation in **April 2011.**

The purpose of the pilot project is to simplify the administrative procedures for small companies to reduce the number of forms and to streamline the delivery of public services to small and medium sized companies through the establishment of unique offices. Specifically, the plan includes two components, which will coexist: one IT platform (e-government) and a physical office where small businesses can address directly to experts. Regarding the portal, it will include all the necessary information, being explained step by step. Forms can be downloaded, which then, after they are filled in, can be submitted online to those institutions. The hope is, through this, payments could be made to pay the taxes, even the ones type CAS, as well as the fees for setting up the company. Also, there will be a separate section covering legislative news and funding opportunities from national and Community budget, according to Capital magazine. The virtual environment will store the data which firms are required to report, so that the competent institutions could download directly from the site. Initially, the portal will be only in Romanian.

To achieve the objectives, the Ministry of Small and Medium Sized Companies will collaborate with other public authorities, the support of other institutions being necessary for elements such as, for example, the secure electronic signature, which is not yet widely used in Romania. But the portal will be developed in stages, the small companies can benefit from these facilities in time.

Thus, the cancellation or the transfer of the business of the small or medium sized companies will also take place in cyberspace. The portal will address a part of the administrative issues from the setting up stage of the business, continuing with the fiscal and non-fiscal obligations and ending with the closing of the company or its transfer to third parties.

The project, called The simplification of the administrative procedures for the small and medium sized through the introduction of unique offices **"One Stop Shop",** has obtained the European funding of around 4.4 million RON, through the European Social Fund. The total project is 5.175 million lei, of which the contribution of the Ministry of Economy is 15%. Of the total amount, approximately 40% is dedicated to creating and implementing the IT solutions.

Originally, for the business representatives a site will be created where they will be able to express their views on how the two components, the IT version and the office, of the program should work. The consultancy is provided by two companies: Infogroup Consulting in Greece and Leader AT in Romania, their selection process lasted about 6 months.

The project also seeks to identify, from among similar models existing in the EU, the one who fits the situation from Romania. All the versions meet three main roles: to inform, to centralize data on companies (so that entrepreneurs are not required to provide the same documents to several institutions) and administrative procedures (so that the contractor is not required to go to those institutions) and to advise and assist the development of the businesses. At the moment, the existing options are assessed. One of the models given as examples of best practices by the European Commission is the **Dutch model.** It succeeded in a first stage to reduce bureaucratic procedures by 10%. After about 7 years since it was launched, the Dutch model has come to "cut" with 60% the bureaucracy for small businesses. Another example is the Belgian one, consisting of a single database and one stop shops, so that the companies do not have to communicate that information repeatedly to various public institutions.

As a first step, the opening of a physical office in Bucharest is planned, where the most small and medium sized companies are and where it can be managed more easily.

The development of the small and medium sized companies in Romania is a key point along with the European Union integration. The special importance granted to the small and medium sized companies in most developed countries has as foundation the solid economic and social considerations.

The small and medium sized companies are more responsive to what the market needs, and are more adaptable to change and more innovative in their ability to respond to the consumer’s demand, making a significant contribution to improving the competitive environment specific to any market economy.

The financial management must address the crucial issue of planning, allocation and utilization of the financial resources in small and medium enterprises.

We also consider that risk is an essential component of a strategic and tactical decision. And this aspect should be taken into account otherwise the company can have serious problems in the future regarding its evolution on the market competition.

2. CONCLUSIONS

From the facts presented, several conclusions may be drawn:

Firstly, we consider that risk is an essential component of a strategic and tactical decision. Without considering this parameter, the company may have serious problems in the future evolution of the market competition.

Secondly, a business risk assessment should be based on specific management methods and specific managerial, mathematical, statistical and banking procedures, to highlight where the company has had financial difficulties, and the decisions adopted to eliminate them.

Thirdly, we believe that in an investment decision, on the one hand, the capital invested and on the other hand the gain that can be obtained if the business has a high degree of risk should be taken into account, so that for the risky investments, the profit obtained should be to its extent.

Finally, we consider that failure to take account of the risk parameters in a strategic financial and tactic decision, can lead to the state of liquidity, and on long-term (on a horizon of 3 to 5 years), to a state of insolvency and bankruptcy.

As a general conclusion we can say that in Romania, there have been created the prospects for the development of the small and medium sized companies sector, the financial management is the key to achieving these goals.

Together with the simplification of administrative procedures for the small and medium sized companies through the introduction of the **"One Stop Shops",** 3 administrative procedures, which now belong to different institutions, will be simplified and will be taken by a single "shop".

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