

# Study on Establishing Growth Strategy System for Pre World Class Companies

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## Abstract

**Background/Objectives:** The local small giant support project for cultivating Korean hidden champions is formal rather than bringing practical effect. This study aims to help companies practically by suggesting customized growth strategies for local small giants. **Methods/Statistical Analysis:** A growth strategy system for local small giants was presented and the effectiveness of the growth strategy presented was verified. Also, an interview for satisfaction research was conducted with 5 consultants and 14 company managers, who specialize in planning growth strategies for local small giants, using standardized questionnaires. The questionnaire consists of questions about satisfaction, work concentration and strategy compliance. **Findings:** The growth strategy system maintains the growth strategy systems of the world-class 300 enterprises and reinforces the key technology securing strategies for developing future growth engines, from the perspective of BSC (Balanced Score Card). According to the survey on the effectiveness of these customized growth strategies for local small giants, 94.7% of the subjects were satisfied with the growth strategy system suggested. 55.6% of them replied that it could provide practical help and 38. % of them replied that it lightened the burden of paperwork. All the consultants answered that they got time to concentrate on the companies and it would provide practical help by enabling them to present in-depth data. **Application/ Improvements:** Further researches for empirical studies to examine whether the growth strategy is connected to practical business performance and meet national competitiveness, is required.

**Keywords:** Growth Strategies, Hidden Champion, Local Small but Strong Businesses, Small and Medium-sized Businesses, World Class 300

## 1. Introduction

### 1.1 Global Economic Crisis and Advancement in Germany

America's financial markets took a hit due to subprime mortgages crisis in 2008, and in this process, super massive mortgage loan companies (Lehman Brothers, Merrill Lynch, Bear Stearns) went bankrupt in a row and credit crunch occurred. This resulted in international financial crisis in 2009. Many countries suffered from difficulties in these economic recession but Germany positively affected economic recovery with enormous current account surplus to the amount of GDP 6.5 % 2010 up to 2012. During this period, Germany's real GDP

recorded a 2.6 percent average annual growth rate and the unemployment rate displayed 6.2% so that they achieved the lowest level since German reunification in 1990. In other words, Germany was supported by strong exports since the economic crisis and showed high growth and low unemployment as much as major industrialized nations would envy, and in this way Germany has emerged as the best country in the global economy since the global economic crisis and received the attention of the whole world for the factors of the success. Schröder government implemented the active labor market reform policy of Germany and produced agreement between labor and management to curb labor costs. In addition to that, it reduced the unemployment rate due to factors such as the

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launch of the Eurozone and contributed to heightening export competitiveness of companies.

In this regard, the role of Mittelstand referring to 3.6 million strong small and medium-sized enterprises which are sustaining the economy of Germany, has been received attention and positive researches on Mittelstand have proceeded.

## 1.2 Mittelstand

In the southern part of the 19th century Germany, land allotment inheritance system which distributes property of the head of household such as land equally for all children, has been implemented and in northern Germany, exclusive inheritance laws which allow only one among children to be inherited, became effective. In accordance with this, in southern Germany farmland of individual farmers were changed into small scale<sup>1</sup> and as a means to which farmers preserve income, employment at a cottage industry or special handicraft workshops was activated. However, the farmers who had any patch of land because of Stratum consciousness that corresponding in themselves at middle class, hesitated to become a full-time factory worker. In a political respect, right to vote or political rights in Germany were recognized only to property owners. There were factory businesses in the form of modern capitalism at that time but because of a manpower shortage problem in the rural areas, an outside order given to workers in a cottage industry or special handicraft workers rather than internalizing the production process of business, has been developed. Handicraftsmen or artisans were able to establish a business of Mittelstand and maintain their status of middle-class, not being degenerated into migrant workers in the process of industrialization.

On the contrary in Britain, the cradle of Industrial Revolution in which technology using the steam engine has been commercialized and manufacturing productivity such as textile and metal has greatly increased, export sharply has increased with mass production and the competitiveness of shipping industry based on the world's largest merchant ship cooperation. At this time, in order to avoid competition with British products, Mittelstands in Germany concentrated on expensive bespoke production rather than mass production on the basis of specialized technology and targeted a niche market in the way of shortening the cycle of products. With respect to this, cook's knives from the district of Solingen and silk

hats and dishwasher for business use from the district of Barmen became representative industry and in this way, they chose an 'Extreme focus' strategy<sup>2</sup> concentrating the corporate capabilities on specialized product production such as Premium consumer goods, Machine tools and parts materials. Therefore, at the end of the 19th century, Britain having gone into the automotive industry used the components of most of Germany to make completed vehicles. In this regard, German Mittelstand distinguished themselves in parts and material industry.

Germany was divided into 27 independent small countries, then and each had to exercise their rights as economic policy until the establishment of the second Reich in 1871. Customs union was formed as internally tariff-free and externally customs between nations composing Germany in 1834 and competition for economic development between the nations began in earnest. Local governments in southern Germany in which Mittelstand centered industrial system has been established, set up saving banks, supported vocational trainings and carried out technology transfer, and thus, they implemented policies that reflected their competitive edge and ultimately German equipped with export competitiveness of industry, which played a role of the driving force for the rapid economic advance even in economic crisis<sup>3</sup> emphasized that the German secret of success in a position of the largest exporter in the world was no. 1 to 3 in of the global market and hidden champions more than 1,000 as companies of less than \$ 4 billion by sales revenue, not well known to the public. By the way US, UK and France call smaller businesses Small and Medium-sized Enterprises (SMEs).

There are a variety of studies on hidden champions worldwide<sup>4</sup> argued that for reviving national economy, there should be over 95% of effort into small companies<sup>5</sup> published a research on innovation of Russian hidden champion enterprises, human capital and internationalization. These researches shows that this is worth studying.

## 1.3 Mittelstand and Hidden Champion Co.

Prof. Hermann Simon argues that "contrary to a common idea that a country's export is determined by few large companies, it depends on many medium-sized enterprises excellent at export, what are called hidden champions." Among 2,734 hidden champions across the world in 2012, 1,307 were from German Mittelstand. At

present, Mittelstand refers to SMEs constituting German economy's waist. It has been shown that it was in charge of 60.8% of total employment and created 51.8% of GDP<sup>6</sup>.

**Table 1.** World manufacturing's hourly pay<sup>7</sup>  
(unit: Constant dollars, 2011)

| Brazil | UK   | USA  | France | Germany |
|--------|------|------|--------|---------|
| 11.7   | 30.8 | 35.5 | 42.1   | 47.4    |

As shown in the Table 1. above, however, since Germany's manufacturing labor cost still implies a high level over the world, not only cost-cutting efforts but Mittelstand based excellent quality and technological competitiveness were the driving force which made Germany a global manufacturing power. Germany is sorting out a common problem such as technical standards through the cluster industry-university-research. Standard regional industry clusters have been formed and traced 327 in all over Germany in 2013 and a mutual collaboration and open innovation system have been established. 7 to 8 percent of the total sales for Mittelstand R&D investment is higher than that of large firms with 5%. In this way, R&D investment has built up virtuous cycle with improvement of product quality and strengthening of technical competitive.

**Table 2.** A comparison for hidden champions between Germany and Korea<sup>8</sup>

| Division                                        | Germany | Korea <sup>9</sup> |
|-------------------------------------------------|---------|--------------------|
| Enterprise number (unit)                        | 1,000   | 114                |
| The average business achievement (year)         | 61      | 30                 |
| The average sales (hundred million won)         | 4,700   | 4,654              |
| The average export (hundred million won)        | 2,930   | 2,757              |
| The average export cost                         | 62%     | 69%                |
| The average business profit rate                | 11%     | 7%                 |
| The average employees (person)                  | 2,037   | 468                |
| The average number of overseas companies (unit) | 27      | 4.4                |

Furthermore, German hidden champion enterprises pay wages of 80~90 % compared to big companies and Culture that respects highly skilled engineers, called 'Meister' is also a key factor. As shown in the Table 2. The average work period is 37 years and job change rate is 2.7% in these companies and thus, it shows a big difference from 10.8 years and 15.1% of Korea. In regard to this, Prof. Hermann Simon pointed out that "South Korea's SMEs' potential for growth is enough, but the problem is that they are not good at cultivating a global market"<sup>10</sup>.

In addition, German government devised 'Mittelstand innovation program' and supports SMEs investing in R&D and further, regional governments also supports with small business streets. Moreover, not only did they revise tax law in 2007 and exempt from Inheritance tax for SMEs having maintained a job volume over 10 years but also financial institutes supported SMEs' over markets with SMEs task force. As a result, only 35 % of high school graduates went to college and the rest were trained with professional education at 'Meister' for 3 years and grew as an engineer with competitiveness. If they will have received the certification of Meister through qualification test later, they will become leaders in the industry and a high income will be guaranteed so that it has been identified that 1.5 million German youth receive professional education<sup>11</sup>.

In this effect, there are many cases grown into large businesses based on the success story in global market. An apprentice trained skilled feature at a technical institution for three years, started out a small workshop with two employees in Stuttgart in 1886. They developed their major part, a magneto ignition system just in one year after foundation and magneto ignition devices for vehicles in 1887, and opened a dealer shop in U.K. in 1889. Bosch, a German auto parts company that invented a high tension magneto ignition device in 1902 and built up an overseas factory in the United States in 1909, and has grown into a huge multinational enterprise with the current 300,000 employees, is the most prominent example<sup>12</sup>.

#### 1.4 Mittelstand's Success Factors

Firstly, they aimed at export from the initial stage and endeavored to realize economy of scale through positive globalization. Mittelstands concentrated on niche markets instead of mass production and domestic demand was immediately saturated and thus, they pursue overseas markets since the first time. Bosch or Daimler having grown up into large enterprises based on this kind of success in the global market, shows typical examples from foundation of apprentices through success in overseas markets up to growth into a big company. Furthermore, in case of Sennheiser, a manufacturer of high quality of mikes and headphones, in order to prevent leaks of the core of the acoustic transducer technology, they produced direct products at domestic factories and in the overseas cooperation's of Ireland and USA instead of outsourcing.

Thus, preference of FDI (Foreign Direct Investment) over outsourcing for protection of technology was one of Mittelstand's success factors.

Secondly, as securing a competitive advantage in the market of high quality and high price based upon global technology, they sought to differentiate themselves from the countries offering low-cost products based on low wages and focused the performance of company on specialized products. 2008 to 2011, German Mittelstand's the average business profit rate was 4.79% and higher than that of SMEs in France (4.18%) or Italia (3.31%)<sup>13</sup>. This is all because they produced high quality and high value-added products centered on skilled craft workers in the brand name of Meister and realized high profit margin in the market and further, realized differentiation from products of lower price of emerging countries based on low wages. Moreover, Mittelstand's high profits were reinvested in research and development to develop its technology. Mittelstand's the total R&D investment spending in 2010 was 8.7 billion euro which not only was higher than that of Spain (7.5 billion euro)<sup>14</sup> but it has been identified as which exceeded the number of total patent applications of Some European countries<sup>15</sup>, given that the number of patent applied by G&D, a Germany's printing paper money business in a year of 2010 was 161. As Harvard Business Review expressed the business strategy of Mittelstand as 'extreme concentration' that targets a niche market attempting by the product specialization<sup>16</sup>, focusing the performance of corporate in product production in specialized field such as premium consumer goods, machine tools, parts and materials, results in their competitive power for quality. *Henckels* who established a business in 1731 and has adhered to the manufacturing of high-end kitchen knives with alloys and heat treatment technology, and *Winter halter* who established a business in 1947 and has stuck to dishwasher for business use like hotels or restaurants, are representative examples.

Thirdly, they formed clusters by region and sorted out the problem of technology standardization, cultivating skilled craft workers in the complementary relationship with other companies. As shown in the Figure 1. Germany alone, in 2013, 327 units of industrial cluster exists, and according to current cluster statistics of the European Union at the end of April 2015, it has been extended to 2,009 of clusters across Europe as well as Germany. German companies have solved out jointly the difficult issues to be solved by force of individual companies such as training

of skilled craft workers or technology standardization, and it might be not only because mobile workforce is low due to similar wage levels but because local dealer became supervisor and managed the vocational training system in a duality with theory classes of vocational schools and on-site training in business.



Figure 1. EU cluster Map<sup>17</sup>.

The activation of this cluster is equipped with a function autonomously redefining industry standards in line with change of regulation environment and advances in technology, participating groups by industry machinery or automobiles of each enterprise.

### 1.5 Implications

With the world attention to the German Mittelstand, historical background and analysis on how Mittelstand was able to prosper, have been actively conducted. Developed countries such as USA, UK and France endeavor to learn from them saying that "We need to learn lessons from the model of Mittelstand<sup>18</sup>," while promoting the manufacturing revival to create good jobs with export growth. As for an alternative to solve out the problems of jobs and polarization, Korea also is showing an increased interested in Mittelstand<sup>19</sup>. In relation to the success of Mittelstand, we can draw out a couple of implications and in general, it can be categorized into two: growth into global small but strong business through 'one well sinking', and their business strategy combining specialization of production by high-level technology and active advance.

The most owners of Mittelstand are skilled workers and their class consciousness as middle-class was firm. Ludwig Erhard, former minister of economy who outlined the economic revival of West Germany after the second world war, also emphasized that Mittelstand

is “the expression of special spirit and attitude”<sup>20</sup>. It reflects on which Mittelstand is the core value of stratum consciousness and work ethic formed by the background of an independent farming centered society. Based on this stratum consciousness, Germany’s skilled technicians have managed global small but strong businesses with pride of their job and prosperous start-up will. Moreover, in specialized industries, the generational business succession tradition has been established and a vocation sense of Mittelstand was formed. Selection and concentration on products based on a vocation sense made it available in achieving up the highest market share in the world, and fund, manpower and knowhow became the base for easy branch out to other products. It was also significant to specialize finding a niche in the global market through Germany vocational training system of Meister and the activation of industry clusters, and to cultivate the global marketing capabilities with overseas markets and efforts to focus resources on innovation required.

South Korea also needs a social atmosphere that skilled technicians and SMEs businessmen can have pride as middle class and of occupation and also support of the policy for constant specialization through the family business succession.

## 2. South Korea’s Policy for Upbringing Hidden Champions

### 2.1 Survey of Korean Type Hidden Champion Enterprises

Korea Industrial Technology Agency, on Oct. 2014, conducted a survey of success knowhow and bottleneck problem for 44 enterprises which could be categorized as domestic hidden champions. Responded 33 of 44 (2/3) enterprises were identified as SMEs and 27 (61.4%) were located in metropolitan area. In relation to Business achievement, 27 of 44 businesses indicated less than 20 years and 40 (90.9%) of 44 companies were found as making B2B.

As shown in the Figure 2. The factors of the success of these enterprises were explained as superiority of technicality and the value of scarcity (30 companies, 68.2%) over competitiveness with a low price (9 companies, 20.5%). As shown in the Figure 3. While most firms showed high satisfaction for R&D and government

assistance funding, new market opening and human resources were expressed as low satisfaction. In addition, the biggest problem for SMEs in growing into hidden champions was identified as the difficulty in new market opening Including exports (21 companies, 7.7%) and the difficulty in obtaining professional workforces (17 companies, 38.6%). As shown in the Figure 4.

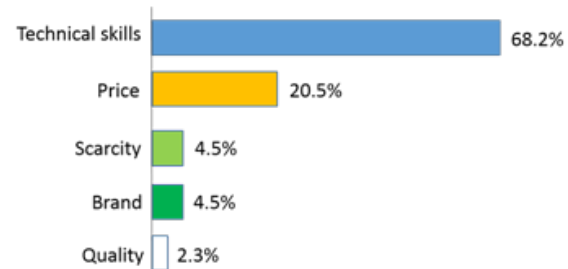


Figure 2. The biggest competitiveness.

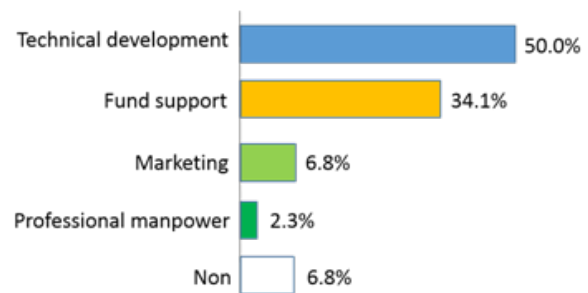


Figure 3. Helpful government support.

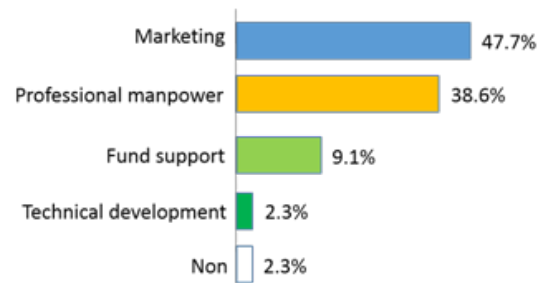


Figure 4. Bottleneck problem while growing up.

### 2.2 The Government’s Relevant Policy

With a program of World Class 300 company upbringing presented by the Ministry of Knowledge Economy on 2011, the full-scale development policy of hidden champions began with interests to SMEs. 2011 World Class 300 by the Ministry of Knowledge Economy as a project for concentrated supporting of 300 SMEs and upbringing them into global companies until 2017, has

been suggested in the form of comprehensive package support by varieties of institutions, including financing for research and development of 1.5 billion won per every year for five years. Companies that wanted to receive support should have met the basic requirements<sup>21</sup> and established a mid - and long-term growth strategy (global marketing, technology innovation, investment innovation and management innovation) with in-depth face-to-face assessment and the field survey and then, the final selection was determined. 100 enterprises have been selected so far through 30 companies including *Jusung Engineering Co., Ltd.* in 2011, 37 companies including *Kyeongdong Navien Co.* in 2012 and 33 companies including *Kaonmedia Co., Ltd.* in 2013, and they were able to launch the world class corporation's association in 2014. With changes in related policy in 2014, in which the project was transferred from Ministry of Trade, Industry and Energy to the Small and Medium Business Administration, the latter supplemented more 56 companies including *Gigalane Co. Ltd.* in 2014 and 30 companies in 2015 and further, 50 companies will be added in 2016.

After the transfer of the project to the Small and Medium Business Administration, Korean type hidden champions was redefined and a master plan for this was announced in Oct. 2014. As integration into the long-term enterprise support program is announced, 'regional small but strong enterprises competitiveness project' and 'global small but strong enterprises upbringing project' are combined into global take-off stage support, and also the existing 'world class 300' and 'global specialized companies' projects were combined into global growth stage support.

In accordance with this, comprehensive Roadmap by which SMEs can grow up into Korean type hidden champions through global take-off stage support and global growth stage support, was constituted. Following Pre World Class demo business in 2014, it is executing as being divided into global take-off stage enterprises and global growth stage enterprises by public notification of integration in 2015.

### 2.3 Support Policy for Global Take-off Stage Enterprises

To build the ladder of company growth can contribute not only to solving out the problem of polarized economy and creating good jobs but also to building up a healthy

corporate ecosystem and guaranteeing the continuation of Korea's economic growth. On this account, professional and sensitive policy to foster SMEs is needed<sup>22</sup>. However, domestic SMEs lack the capacity to establish medium and long term strategy and fail to adapt to rapid structural changes in the industry and environmental change. For SMEs' continuous growth, it is important to ensure the strategic planning functions, which will establish a plan for the base of all business activities.

In this regard, this study will examine the problems of application of SMEs within SMEs growth strategy system currently required by the government questions system small and medium-sized enterprises applied strategies, and present a strategy framework applicable to SMEs in the point of view of growth ladder. Through this, it is expected that not only does it enable SMEs to grow into enterprises of middle standing and further, big companies and global enterprises, but balanced development will be accelerated and their competitiveness will be enhanced.

## 3. Research Model

Management strategy is recognized as major determinant of corporate performance, and the securing of competitive advantage and maintenance are selected as the core concept<sup>23</sup>. Management strategy is categorized into varieties of types according to analytic levels considering characteristics of business, strategic approaches and organizational system<sup>24</sup>. As shown in the Figure 5. The present research's scope ranges from BSC (finance, customer, internal process, and learning and growth) currently applied to global take-off stage businesses and global growth stage businesses up to enterprise of growth strategy to which the securing strategy of key technology for securing future growth engines is added.

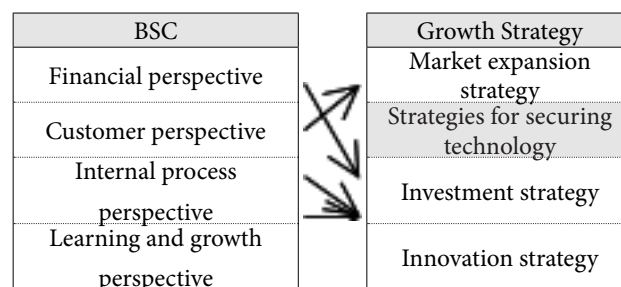


Figure 5. BSC & growth strategy structure.

**Table 3.** Proposed Model.

| Item                                  | Details                                                                                                                                                                                               |
|---------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| environment analysis on target market | Market definition, growth potential and main Customer characteristics<br>The status of their competitors and major activities                                                                         |
| Evaluation on internal ability        | Level of market competition and performance for three years<br>Enterprise, product and Brand awareness<br>Status of internal organization                                                             |
| establishment of target               | Directions of expanding market                                                                                                                                                                        |
| Market expansion strategy details     | Strategy for expanding market by target market<br>Market expansion Risk Management                                                                                                                    |
| Technology trends                     | Trend of technology, motive of change and technology necessary to secure<br>Trend challenges at home and abroad                                                                                       |
| Internal capacity                     | Status of research organization and research personnel<br>research equipment, facility, equipment, network<br>Challenges application and registration application performance in the last three years |
| A strategic target                    | Secure technology direction and final goal                                                                                                                                                            |
| Detailed strategy                     | technology development goal and development content<br>Risk Management                                                                                                                                |
| Investment environment                | Future investment items and analysis of conditions<br>Yearly investment roadmap                                                                                                                       |
| Plans to secure investment funds      |                                                                                                                                                                                                       |
| CEO leadership                        | CEO Management philosophy and core values                                                                                                                                                             |
| Human Resource Management             | Management Plan for the present situation of human resources and key personnel<br>The cause of a manpower shortage and the effort to improve<br>Education and Training System, and Improvement        |
| Organization management               | Organizational structure and Improvement<br>achievement management system and Improvement                                                                                                             |

## 4. Proposed Method

As shown in the Table 3 and Figure 6. Mega Process set growth strategy is (1) environment analysis, (2) capacity evaluation, (3) establishment of target, (4) detailed strategic planning system and thus, this system should be maintained but as to details and sub-details, this research Gave the change to focus on implementation rather than strate-

gic planning just for the strategic planning. Since the goal is growth into medium businesses, this study presented an applicable system while simplifying growth strategy.

## 5. Experimental Results

To identify the validity of growth strategy system presented in the present research, the interview of satisfaction levels

**Figure 6.** Growth strategy model.

by 5 consultants of growth strategy planning and each company in charge of 14 was conducted and as a result, 94.7% showed a satisfaction. With respect to major factors contributing to this content, a response that it might be more practical help accounted for the highest percentage (55.6%) and another response that the burden of paperwork has been reduced was shown as 38.9%. The whole consultants commented that it will be practical help in that the time to focus on businesses was secured and the information in depth were presented.

## 6. Conclusion

The result of the present study indicates a suggestion of SMEs customized growth strategy system at a level to speed up national competitiveness. Further researches for empirical studies to examine whether the growth strategy is connected to practical business performance and meet national competitiveness, is required.

## 7. Acknowledgements

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