Win-Win Growth and Small Giant suppliers' Growth Determinants

-Case Study of Samsung Electronics Corporation's Small Giant suppliers-

April 30, 2015

Rhee, Chong Ook (Professor, Department of Economics, Seoul Women's University, Seoul, Republic of Korea), Email: cgrh@swu.ac.kr; Phone: +82-2-970-5521

Keyword: win-win, small giant supplier, financial characteristics, firm growth, Samsung Electronics Corp.

<Track>

Creating Shared Value (CSV) (First Choice)

Small Business and Small & Medium Enterprises (Second Choice)

<Abstract>

1. Aim of the Paper

German economy has been grown in the recession followed by American 2007 financial crisis. Several papers published in Korea report that the stable German economic growth has been supported by globally competitive hidden champions. The firm size of German hidden champions is the small and medium firms which have both innovation and growth. They also play the main role in the German local economy to create employment and economic growth. German hidden champion depends on export and creates employment. .

Korean economy faces the low economic growth without employment creation which follows the polarization between small and medium firms (SMEs) and big firms. Korea's export-oriented growth does not push employment creation.

To overcome low growth and employment in the industrial sector of Korean economy, Korean government has had strong desire to learn methods to incubate German hidden champions. Hence it proposed the big plan to make the economic environment to create and incubate Korean style of hidden champions, so called small giant, on 2014. It expects good employment opportunities and growth sources to be created through these industrial policies.

Simon's books and lectures provide good materials on conditions for hidden champions and on their business plans. But they don't give any information on the hidden champions' financial variables in the financial statements and on their special financial characteristics.

This paper investigates the structural transformation of financial variables of small giant suppliers selected by Samsung Electronics Corporation annually from 2012, and shows how different their growth stages are from the comparison group.

2. Background Literature

The previous literature published in Korea(H. Simon, 2008, 2012; C.O. Rhee, 2010; IBK Economic Institute. Korea Small Business Institute, 2012) has no comment on how the hidden champion in the Germany has grown and transformed, what the entrepreneurship and firm succession to create, incubate and grow the hidden champion is, what the political, legal, cultural, and educational infrastructure to support the hidden champion is, how and why the town people love the hidden champion, what the relationship between hidden champion and local economy, culture, education and politics is, etc.

But Korea policy authorities have emphasized the important role of hidden champions which support the German economy in spite of the global recession incurred by the global contagion of

2007 USA financial crisis, and hence pushed various policies to promote Korean small giants compared to German hidden champion.

To succeed in the development and incubation of Korean small giants, we need some information in structural adjustment of future hidden champions' financial variables on how the growth stage of hidden champion has been developed, how the structure of hidden champion's financial statement has been transformed, etc.

Coincidently, Samsung Electronics Corporation has announced small giant suppliers around March annually from 2012 up to now which are selected among small suppliers promoted by win-win programs,. Since the selection criteria have not been opened, the selected suppliers can be evaluated by applying Simon's three criteria to select German hidden champion: ① 1 – 3 rank in the world market share or the first rank in the continent in which the firm is located, ② less than 5 billion euro sales, ③ low recognition in the public.

The important financial variables in this paper to evaluate the financial structure of small giant suppliers chosen by Samsung Electronics Corporation are capital, sales and operating profit, to reflect the three criteria used in the selection of Simon's German hidden champion. First, since the hidden champions occupy the 1st – 3rd in the world market share or the first in the continent in which the hidden champion is located, the size of capital is getting important. Second, since sales are less than 5 billion euro, the size of sales and the growth of sales are critical. Third, the low recognition for the public is the same for the supplier of the big company. .

3. Methodology

1) Analysis Data

The small giant suppliers' data used in this study are the corporate financial statement data provided by Korea Financial Supervision Service. The data of Samsung Electronics Corporation's business unit financial statement are provided by the Win-Win Division of Samsung Electronics Corporation. The small firms' data compared with small giant supplier is collected from ***Financial Statement Analysis*** annually published by Bank of Korea.

The panel data are constructed as follows: the total number of firms announced from 2012 to 2014 is 24 firms and the time-series range of analysis target was set to 2003 ~ 2013. Since firms' data are not collected in some periods, the unbalanced panel data are used in the empirical analysis.

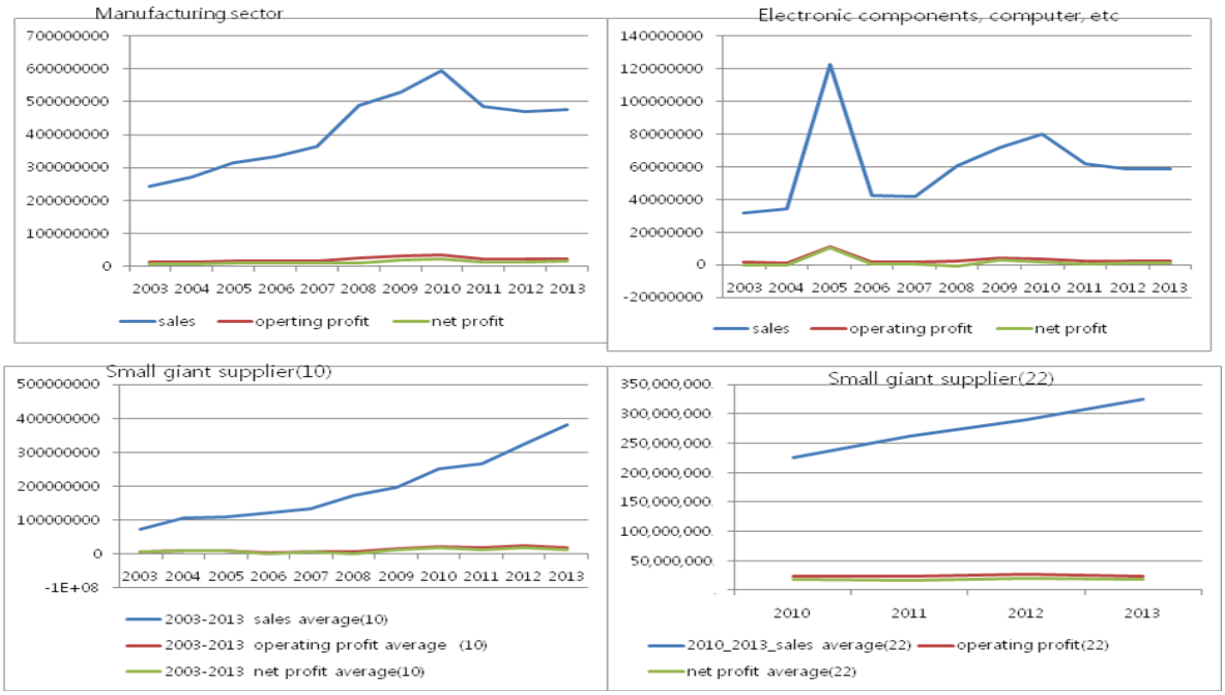
2) Analysis Model

(1) Graphical Comparison

This paper focuses on variables corresponding to the definition of German hidden champions to

show how different small giant suppliers selected by Samsung Electronics Corporation are from comparison groups. Two comparison groups, i.e., SMEs' sector of manufacturing and sector of electronic components, computer, radio, television and communication equipment and apparatuses, are chosen from *Financial Statement Analysis*.

The next graphical comparison shows us clear differences among groups. The trend of sales by small giant suppliers is different from those of both manufacturing sector and electronics sector.



(2) Pooled Data Estimation Model

Graphical analysis points to a fact that sales of small giants are getting faster than two comparison groups. This finding is directly and indirectly related to facts 8 to 10 among 10 stylized facts (Klette and Kortum, 2004). First, the stylized fact 8 is that smaller firms have a lower probability of survival, but those that survive tend to grow faster than larger firms. Also among larger firms, growth rates are unrelated to past growth or to firm size. Second, the stylized fact 9 is that the variance of growth rates is higher for smaller firms. Thirdly, the stylized fact 10 is that younger firms have a higher probability of exiting, but those that survive tend to grow faster than older firms. The market share of an entering cohort of firms generally declines as it ages.

As listed in stylized facts on firm size distribution and firm dynamics, we can infer from Figure 1 that the firms which survive and are selected as small giants tend to grow

faster than the average growth rate of both manufacturing and electronics industries.

Hence the regression analysis to use pooled data has been developed to find the determinants of salient characteristics found in the small giants' sales trend compared with two categories of both manufacturing and electronics industries.

The pooled model in this study is estimated by the least squares method to investigate determinants of sales growth. Generally the regression model to use pooling data as in (1) can be used.

$$y = \beta_0 + \beta_1 \Delta X' + \beta_2 \Delta Z + \varepsilon \qquad (1)$$

Where y is sales; X' the vector consisting of intangible assets, tangible assets, and capital ; Z time-series explanatory variable vector (sales of manufacturing sector, sales of electronics sector, Samsung sales, etc.)

4. Results and Implications

This paper shows that the growth trend of small giant suppliers' sales and capital from the graphical analysis is distinguished from those trends in both manufacturing and electronics industries. Although severe downturns of the business cycle during 2003 to 2013 occur, the small giant suppliers selected by Samsung Electronics Corporation show the monotone increasing function of both sales and capital in the graphical analysis and confirm one of stylized factors that firms conditional on survival grow faster than the average grow rate in the industry.

From the empirical analysis using pooling data to investigate small giant suppliers' sales determinant, we find the capital is critical and positive, and intangible assets are positive and more important than tangible assets which are negative. The competitive development of small giant suppliers is at the stage of innovation-driven growth. Rising importance of intangible assets in suppliers' growth is the same as that in German hidden champions.