Hidden Champions in CEE and Dynamically Changing Environments: Who are they, where they come from, how different are they?

Summary of research results
Agenda

1. Research overview
2. Success stories
3. Market position
4. Competitive strategy & leadership
5. Marketing strategy & innovations
6. Summary
Disclaimer

- All analysis and findings outlined in this presentation are preliminary

- Full research results and country chapters will be published in the upcoming book:
  - Title (TBD): “Hidden Champions from Central and Eastern Europe”
  - Editors: Hermann Simon, Danica Purg, Melita Rant, Marek Dietl
  - Expected publisher: Emerald
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Geographic scope

Our research covered 18 countries with population over 400 million but we identified around 300 HCs, and study in a greater detail 165 HCs.

Simon’s HC research

<table>
<thead>
<tr>
<th>Macroeconomic indicators:</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>German-speaking countries (A, DE, CH)</td>
<td></td>
</tr>
<tr>
<td>Total population (2009): 98 million</td>
<td></td>
</tr>
<tr>
<td>Total GDP (2009, current $): 4.2 trillion</td>
<td></td>
</tr>
<tr>
<td>Range of av. GDP growth ('99-'09): 0.9%-1.9%</td>
<td></td>
</tr>
<tr>
<td>Avg. GDP/cap. (2009, current $): 50 thousand</td>
<td></td>
</tr>
<tr>
<td>Total export (2009, current $): 1.8 trillion</td>
<td></td>
</tr>
<tr>
<td>Export as % of GDP (2009): 43%</td>
<td></td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>Hidden Champions:</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of HCs: 1316</td>
<td></td>
</tr>
<tr>
<td>HCs per 1000 inhabitants: 0.0134</td>
<td></td>
</tr>
</tbody>
</table>

CEE HC research

<table>
<thead>
<tr>
<th>Macroeconomic indicators:</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>18 countries (C/SE Europe, Turkey, Kazakhstan)</td>
<td></td>
</tr>
<tr>
<td>Total population (2009): 400 million</td>
<td></td>
</tr>
<tr>
<td>Total GDP (2009, current $): 3.7 trillion</td>
<td></td>
</tr>
<tr>
<td>Range of av. GDP growth ('99-'09): 2.5%-8.0%</td>
<td></td>
</tr>
<tr>
<td>Total export (2009, current $): 1.3 trillion</td>
<td></td>
</tr>
<tr>
<td>Export as % of GDP (2009): 34%</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Hidden Champions:</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of HCs: 300</td>
<td></td>
</tr>
<tr>
<td>HCs per 1000 inhabitants: 0.0007</td>
<td></td>
</tr>
</tbody>
</table>

* Albania, Belarus, Bosnia and Herzegovina, Croatia, Czech Republic, Estonia, Hungary, Kazakhstan, Latvia, Macedonia, Poland, Romania, Russian Federation, Serbia, Slovak Republic, Slovenia, Turkey, Ukraine.
Research methodology: Dilemma „Rigor vs. Relevance“?

Unreliable maps, ambiguity, substantial institutional and cultural differences, lack of resources. The only true resource: Committed researchers.

<table>
<thead>
<tr>
<th>Year</th>
<th>Activities</th>
<th>Challenge</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008</td>
<td>Pilot study: Poland. Original Simon’s questionnaire.</td>
<td>Quantitative approach works well on big samples. Semi-structured interviews work better. Max 90 min.</td>
</tr>
<tr>
<td>Oct 2010-Jan 2011</td>
<td>Interviews with companies. Writing detailed analytical cases and questionnaires.</td>
<td>Not many Simon’s type of HCs. Adjustment of selection criteria.</td>
</tr>
</tbody>
</table>
### Hidden Champions in DACH and CEE

Simon’s HCs reached outstanding global position. Our HCs are on the way there.

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Simon’s HCs</th>
<th>HCs from CEE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market position</td>
<td>No. 1 in Europe or World's top 3</td>
<td>Global / Europe / CEE / Regional leaders</td>
</tr>
<tr>
<td>Average revenues (p.a.)</td>
<td>€ 326 millions</td>
<td>€ 141 millions*</td>
</tr>
<tr>
<td>Revenue growth (10 years in EUR)</td>
<td>8.8% p.a.</td>
<td>10.4% p.a.</td>
</tr>
<tr>
<td>Export (% of revenues)</td>
<td>61.5% (51.1% 10 years ago)</td>
<td>62.1% (58.2% 10 years ago)**</td>
</tr>
<tr>
<td>Productivity (revenues per employee)</td>
<td>€ 160,039</td>
<td>€ 99,240</td>
</tr>
<tr>
<td>Median age of the company (years)</td>
<td>61</td>
<td>19</td>
</tr>
<tr>
<td>R&amp;D expenses (% of revenues)</td>
<td>6%</td>
<td>16.4%</td>
</tr>
<tr>
<td>Patents per 1000 employees</td>
<td>30.6</td>
<td>41.98</td>
</tr>
<tr>
<td>ROCE/ROI (%)</td>
<td>13.6%</td>
<td>32%</td>
</tr>
<tr>
<td>Equity ratio (%)</td>
<td>41.9%</td>
<td>56%</td>
</tr>
</tbody>
</table>

* Data for Poland 2008, Turkey not included. ** Some companies did not exist 10 years ago.
Industry structure: Substantial diversity

1. Information and telecommunication technologies and other nano technologies (35.7%)
2. Manufacturing of machinery and equipment (18.4%)
3. Electrical industry, electronics (11.2%)
Segmentation of CEE HCs*

Majority of CEE HCs were established after transition to market economy. Despite short presence in the market some of them have become global players.

* Turkey & Greece are excluded from the segmentation due to different historic background.
** Czech Republic & Slovakia was excluded because late arrival of the data.
*** Data on both age and market position is available for 140 out of 157 researched companies.
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Success story # 1: Hidria (Group 1)

Real Hidden Champion!
- Third in the world in diesel cold start systems for internal combustion engines.
- First in the world in range extenders for hybrid electric vehicles.
- Second in Europe in ALU die castings for automotive steering systems.

Growth & globalization
- Growth rates (2000-2010): revenues x2.4; growth both organic and through M&A.
- 25 sales subsidiaries and 9 production plants in 15 countries; however sales in 80 countries.
- Clients all major OEMs: Renault, Peugeot, Volkswagen, Audi, BMW, Citroen, MAN.

Competitive advantages
- Building strategic partnership to manager ambiguity over the prevailing standards for EV technology: R&D departments at strategic clients: BMW, Audi, PSA, Technology platforms: ERTRAC, ESTTP, STTP, SGTP....
- Backward integration – even machines are designed in-house.

Leadership
- Ownership consolidation early on; employees co-owners - unified interest.
- Top management cosmopolitan, well-educated in both technical and managerial background.
- Top decision-makers Slovenes; building their global mindset through education and own development.
Success story # 2: Morpol (Group 2)

- **Real Hidden Champion!**
  - World leader in manufacturing of smoked salmon.
  - Not know to general public however listed on the Oslo Stock Exchange.

- **Growth & globalization**
  - Growth rates (2005-2010): revenues x4; EBITDA x5 (2009); employees x5.
  - Polish company listed in Oslo with operations in 8 countries and market presence in 20+ countries.
  - Organic growths + successful cross-border M&As (including German Laschinger Group).

- **Competitive advantages**
  - Focus on: global mentality, quality, efficiency.
  - Backward integration – even machines are designed in-house.
  - Covering whole value chain: from farming to end customer.

- **Leadership**
  - Mr. Jerzy Malek – founder & CEO – real entrepreneur.
  - CFO and COO from UK.
  - Supervisory board: two Norwegians, two Poles and one Dutchman.
Group 2 is growing extremely fast through internationalization.

Note: Poland not included in the calculation.

✓ Statically significant differences between groups (sign. < 0,05).
Group 2 is more satisfied with performance and competitiveness

Survival ranked the highest – profit ranked the lowest by both groups!
However, the grades are still very high!

<table>
<thead>
<tr>
<th></th>
<th>Group 2</th>
<th>Group 1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Satisfaction with company survival capability</td>
<td>6.10</td>
<td></td>
</tr>
<tr>
<td>Satisfaction with growth</td>
<td>5.98</td>
<td></td>
</tr>
<tr>
<td>Going over the recession better than competitors</td>
<td>5.79</td>
<td></td>
</tr>
<tr>
<td>Satisfaction with capacity utilization</td>
<td>5.76</td>
<td></td>
</tr>
<tr>
<td>Satisfaction with competitive position</td>
<td>5.74</td>
<td></td>
</tr>
<tr>
<td>Satisfaction with the overall performance</td>
<td>5.71</td>
<td></td>
</tr>
<tr>
<td>Employee satisfaction</td>
<td>5.58</td>
<td></td>
</tr>
<tr>
<td>Satisfaction with profit</td>
<td>5.23</td>
<td></td>
</tr>
</tbody>
</table>

Note: Poland not included in the calculation.

✓ Statically significant differences between groups (sign. < 0.05).
Why is growth important?

Revenues reinvested in R&D in %

- Group 1: 5.58%
- Group 2: 11.14%

Length of a product usage

- Group 1: 7.98
- Group 2: 6.08

Note: Poland not included in the calculation.

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Group 2 is in new technologies where the demand is growing.

**Group 1:**
1. Mature stage
2. Machinery, industrial equipment (36%)
3. Transportation, automotive industry (21%)
4. Inconspicuous products for B2B segment within one industrial branch

**Group 2:**
1. Growth stage
2. ICT, Nano technologies (37%)
3. Electrical industry, electronics (29%)
4. Multi-purpose technologies for numerous industrial branches

Note: Poland not included in the calculation.
Structural attractiveness of industries is better for Group 1.

Competition:
Number of relevant competitors
Group 1: 20
Group 2: 22

Competitive rivalry exists.
Slightly stronger in Group 2.

Customers:
Revenues from Top 3 customers
Group 1: 23%
Group 2: 30%

Customers' holdup strong.
Stronger in Group 1.

Barriers to entry:
Group 1: Higher capital intensity
Group 1: Lower capacity utilization
Group 2: Growing demand

Barriers to entry higher for Group 1.

Note: Poland not included in the calculation.
✓ Statically significant differences between groups (sign. < 0.05).
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In both groups core drivers to success is the knowledge of the market, qualification of employees, innovations and image.

Group 2 is more flexible, has better marketing, while Group 2 is significantly better off in terms of patents and clusters.

Note: Poland not included in the calculation.

✓ Statically significant differences between groups (sign. < 0.05).
What more can we say about strategic behavior of CEE HCs?

**Group 1:**
1. Machinery, industrial equipment (36%)
2. Transportation, automotive industry (21%)

**Group 2:**
1. ICT, Nano technologies (37%)
2. Electrical industry, electronics (29%)

Note: Poland not included in the calculation.
Though Group 1 and Group 2 are HC type of companies, their approach towards value creation and value capturing is different.

<table>
<thead>
<tr>
<th></th>
<th>Group 1</th>
<th>Group 2</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Product</strong></td>
<td>Technologically complex (standard) product.</td>
<td>Knowledge complex (custom) product (solution).</td>
</tr>
<tr>
<td><strong>Attitude towards competition</strong></td>
<td>Push forward price/value advantage.</td>
<td>Push forward product design features.</td>
</tr>
<tr>
<td></td>
<td>Focus where you can better manage country risks.</td>
<td>Move quickly to the next generation of products.</td>
</tr>
<tr>
<td><strong>Tactics for avoiding customer holdup</strong></td>
<td>Enforce product as (proprietary) standard.</td>
<td>Intellectual protection weak.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Branding.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Professional articles.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Prestigious awards.</td>
</tr>
<tr>
<td><strong>Attitude towards suppliers</strong></td>
<td>Suppliers as competitors.</td>
<td>Suppliers as customers.</td>
</tr>
<tr>
<td></td>
<td>Suppliers as customers.</td>
<td>How can I create value for supplier?</td>
</tr>
<tr>
<td><strong>Sources of cost advantages</strong></td>
<td>Economies of scale.</td>
<td>Learning economies.</td>
</tr>
<tr>
<td><strong>Core capability</strong></td>
<td>Process design.</td>
<td>Product (solution) design.</td>
</tr>
</tbody>
</table>

Method: Inductive analysis of individual business success stories; second level abstraction of patterns of strategic behavior.
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Strong leadership is a core driver to success in both groups, however motivation and loyalty of employees is higher in Group 1.

Note: Poland not included in the calculation.

✓ Statically significant differences between groups (sign. < 0,05).
What more can we say about leadership practices of CEE HCs?

Group 1:
1. Machinery, industrial equipment (36%)
2. Transportation, automotive industry (21%)

Group 2:
1. ICT, Nano technologies (37%)
2. Electrical industry, electronics (29%)

Note: Poland not included in the calculation.
Based on scarce information about leadership practices, our presumption is that the later also differentiate between the two groups.

<table>
<thead>
<tr>
<th></th>
<th>Group 1</th>
<th>Group 2</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Role of a leader</strong></td>
<td>Resolving challenges and tensions.</td>
<td>Creating of new challenges and tensions.</td>
</tr>
<tr>
<td><strong>Core questions of a leader</strong></td>
<td>Living the customer reality! How to adjust standard product do the demands of individual customer?</td>
<td>Living the future! What needs to be changed by us, by customers to respond well to the future?</td>
</tr>
<tr>
<td><strong>Communication</strong></td>
<td>Clean communication lines. Core technological decisions decentralized to experts.</td>
<td>Spurious communications, lots of questioning. Core technological decisions centralized.</td>
</tr>
<tr>
<td><strong>Motivation</strong></td>
<td>Employees incentivized by better job &amp; higher salary.</td>
<td>Employees incentivized by quest for prestigious awards, professional recognition.</td>
</tr>
</tbody>
</table>

Method: Inductive analysis of individual business success stories; second level abstraction of patterns of strategic behavior.
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Strategic marketing: Matrix of competitive advantages

CEE HCs offer high quality products with good service.

Matrix of competitive advantages of CEE Hidden Champions:

Attributes:
1. Product quality
2. Price
3. Product efficiency
4. Closeness to customers
5. IT systems
6. Pre-sales advice
7. After-sales advice
8. On-time delivery
9. Flexibility in dealing with customer requests
10. Advertisement
11. Distribution
12. Cooperation with suppliers
13. Close to customers location of production
14. Possession of important patents

n=31
CEE HCs marketing-mix

High quality product accompanied with good level of services at a reasonable price are the fundamentals for attractive marketing mix.

**Product:**
- High quality
- High efficiency
- But not a breakthrough innovations

**Communication:**
- Not proficient in advertising
- Not that close to customers (both relations and geography)

**Pricing:**
- Standard (not premium)

**Sales:**
- High level of service
- Timely delivery
- Distribution not a strength

Favorable quality/ price relation
Products’ characteristics

CEE HCs offer rather durable goods produced with technologies with middle level of capital intensity

<table>
<thead>
<tr>
<th>Capital intensity</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low</td>
<td>16%</td>
</tr>
<tr>
<td>Middle</td>
<td>61%</td>
</tr>
<tr>
<td>High</td>
<td>23%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Lengths of product usage</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>&gt;10 years</td>
<td>19%</td>
</tr>
<tr>
<td>3-10 years</td>
<td>45%</td>
</tr>
<tr>
<td>0-2 years</td>
<td>26%</td>
</tr>
<tr>
<td>FMCG</td>
<td>6%</td>
</tr>
</tbody>
</table>
Technology and life cycle

CEE HCs are high-tech companies which products are in growth phase.

<table>
<thead>
<tr>
<th>Technological development</th>
<th>Life cycle</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low-tech</td>
<td>Introduction</td>
</tr>
<tr>
<td></td>
<td>Growth</td>
</tr>
<tr>
<td>Middle-tech</td>
<td>Maturity</td>
</tr>
<tr>
<td>High-tech</td>
<td>Late</td>
</tr>
</tbody>
</table>
Innovations of CEE HCs are driven by both market & technology. Those companies are extremely innovative – some of them are R&D focused.

**Average:**
- R&D as % of revenues: 19%
- Patents per 1’000 employee: 97

**Top-10 innovators:**
- R&D as % of revenues: 39%
- Patents per 1’000 employee: 277
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Summary

- There are Hidden Champions in S/CEE!
- They constitute the avant-garde of the region economy:
  - Their growth rates out-performs GDP growth
  - Their share of export is 2 times higher then region average
- CEE HCs are much younger then their DACH counterparts but they are catching with:
  - **Ambition**: they are usually first generation of entrepreneurs who are success hungry
  - **Innovations**: high R&D spendings and patents per employee
  - Marketing strategy **focused on growth**: high quality at a reasonable prices
- Major challenges are: succession, financing and managing growth and internationalization.
- Future for those companies look bright:
  - Their major products are at the early or growth stage and are rather high-tech
  - They are still foreign markets to be conquered

➤ It is great that those companies exists but S/CEE needs more Hidden Champions!