# WHY ARE SOME FIRMS ABLE TO START UP WITH AND SUSTAIN FAST GROWTH RATES?

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## ABSTRACT

*One of the most important contemporary management issues, also pertinent for the labor welfare, is the growth strategy. With the global financial meltdown, the macro market situation has come under huge stress. The effects of terrorism in the global societies in general, and in South Asian region in particular, is also of huge concern in the growth rates. We need to understand how the nascent firms in India, that have achieved growth over the past ten to fifteen years, could sustain their growth rates, and how new firms could emerge to support and expand the growth rates at the local and national levels. This paper presents a framework for analyzing technological basis for growth strategies.*

Growth is important for the continued success, vitality, dynamism, and viability of all organizations. Considerable empirical research has been conducted to understand the factors explaining growth of firms. Accumulated evidence suggests that the growth rates tend to have a tent like Laplace or symmetric exponential distribution – with a majority of firms showing a moderate/ minimal growth rate, some showing a much lower/ negative growth rate, and some generating a much higher/ positive growth rate (Bottazzi et al., 2007). The majority central mass of firms tend to be most sensitive to the macro environment conditions – when the conditions are adverse, for most of the firms in the center growth rate falls; but when the conditions are conducive, growth rates of many firms in the center becomes higher. On the other hand, the growth rates of the firms at the tails is less sensitive to the macro conditions (Higson et al, 2002)

Overall, there is a considerable regularity in the data at the disaggregated industry and national level indicating that some firms are able to sustain higher growth rates, even under adverse macro conditions. Unfortunately, beyond that, we know little about what allows some firms to sustain these higher growth rates. What we do know is that small firms tend to grow faster than the larger firms – i.e. firm growth tends to be negatively related with size (Sutton, 1997). However, among the larger firms, there appears to be no correlation with size and growth rate (Geroski and Gugler, 2004). We also know that the younger firms tend to show higher growth rates (Fizaine, 1968), albeit in certain situations, the older firms tend to show faster growth by virtue of their experience (Das, 1995). However, more innovative firms do not necessarily enjoy higher growth rate – and where they do, the effects tend to be short-lived; still innovation is an essential feature for the higher growth firms (Coad, 2007b). Similarly, there is limited relationship between financial performance and growth rate – as Coad (2007a: 15) finds, "it may be more useful to consider a firm's profit rate and its subsequent growth rate as entirely independent." There appears to be little correlation of firm growth rate with even labor or multi level productivity measures. Baily et al. (1996) find that about a third of labor productivity growth is attributable to growing firms, about a third to downsizing firms, and the remaining third is attributable to the processes of entry and exit.

Some studies have also examined the correlation of firm growth rate with the ownership/ management/ governance characteristics. Owner/family managed

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firms and women led firms are deemed to have lower growth rate compared to the professionals managed and men led firms – there is some evidence to support this (Hay and Kamshad, 1994; McPherson, 1996), but it is not clear if this correlation is due to the specific values of the owner/family managed firms and women led firms, because many owner/ family managed firms and women led firms are amongst the samples of fast growing firms. A promising line of inquiry on the factors explaining why some firms are able to start up at young age with fast growth rate, and are then able to sustain that growth rate, is offered by the network view of the firms. Powell et al (1996) observe that the degree of centrality, or the amount of experience in a network of firms contributes to a firm's growth rate. While the experience in a network of firms is relevant, the concept and importance of network over the past ten years has evolved significantly. In fact, it would not be untrue to say that we are living in a networked world. A world networked by communication and transportation channels, and by organizational and institutional systems. The hallmark of our age is networked growth – growth of all kinds, and at all levels, and involving all resources, communities, and people. The networked growth is exciting because it offers several new opportunities for multi-faceted development. The networked growth is challenging because lop-sided and uneven development can undermine the accomplishments. The networked growth is inspiring because development in one domain can be a positive role model for further development in additional and complementary domains.

Consider the case of Hyderabad-based Karvy Group, the largest non-banking financial institution in India, and one of the participants in the GLOBE CEO study in India from the state of Andhra Pradesh. Karvy was founded by a group of recently graduated chartered accountants in 1979. In 1982, the group, led by C. Parthasarthy, began providing a value-add service to the corporate clients – automation of the physical financial accounts. It was able to network the public sector banks that were just beginning to automate their financial accounts. In 1984, Karvy prepared a small automated project appraisal package using BASIC computer language, aligned with the requirements of the term lending institutions in India. It was able to network the finance departments of a number of major clients. In 1985, Karvy saw an opportunity to network its strengths in finance and automation, and to apply that to automation of shares accounting, by offering share registration and transfer service in Hyderabad. By 1991, it had networked that service to four metros – Chennai, Mumbai, Delhi, and Kolkata.

Karvy now decided to network the individual customers, by setting up investor service centers and distributing financial service products to them. By 1995, it leveraged that network to start offering financial services to the corporations, including advice on raising the funds. In 2000, Karvy was networking its various service expertise through information technology, and evolving a model of personal finance advisor, knowledgeable of various products – then being marketed by different product managers – required by every customer. At the same time, it decided to roll out information technology services for the international market. In October 2005, Karvy entered the Business Process Outsourcing business, first offering a full range of finance and accounting back-office services, and then extending into human resource services, and investment and economic research and analytics. Today, Karvy service standards have become the international benchmarks, particularly for the financial services industry. This has been despite the experience of all the founders being limited to Hyderabad at the time of founding Karvy. Yet, Karvy well networked the founder expertise in accounting and their interest in information technology to become the premier integrated financial services provider in India, and to enter the global arena, within a period of 25 years (Gupta et al, 2006).

How are some companies able to start up with and then enjoy continuous networked growth, while other companies become trapped in their traditional paths, or get destroyed when they seek to jump into new paths? Is it possible to codify certain growth strategies in the networked economy that may be used by the start-ups and early stage firms, and then be sustained even as they become established firms? Here we present a framework of growth strategies for the start-ups and early stage firms in a networked economy. The framework shows hidden opportunities for value creation, capture, and sustenance in existing networks – howsoever small and primal – in proportion to the actually exploited and tapped opportunities. It pinpoints specific avenues for generating

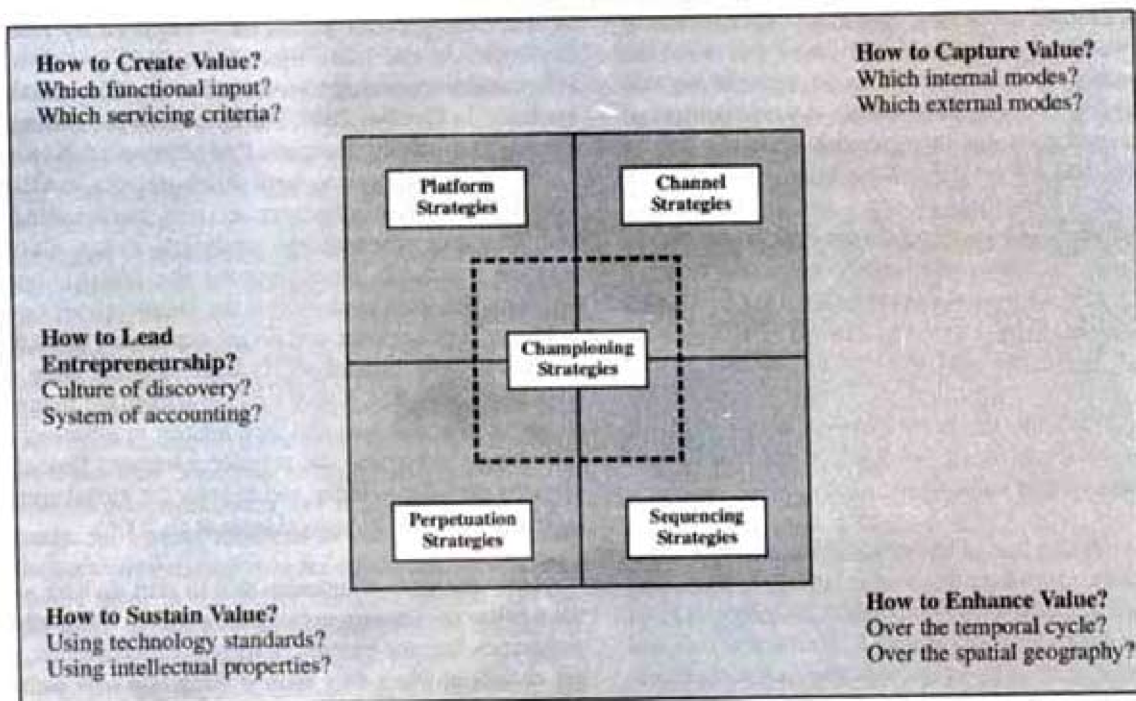
growth, and highlights the endowments internally available for facilitating this growth.

## FRAMEWORK OF GROWTH STRATEGIES IN A NETWORKED WORLD

The proposed framework of growth strategies in a networked world is based on three of the five steps in Gupta's (2006) technological model, as given in Exhibit 1.

In the complete technological model, growth strategies are a function of value creation (platforms), value capture (channels), value sustenance (perpetuation), value enhancement (sequencing), and entrepreneurial leadership (championing). For the purposes of the start-ups and early stage firms in a networked world, the first three are most relevant, though the other two steps may also be used by some of the firms to enhance value and assume leadership from a very early stage or even inception. We will accordingly focus on elaborating upon the strategies associated with the first three steps.

**Exhibit 1:** Technological Model of Growth Strategies, Gupta et al (2006)




## PLATFORM STRATEGIES: HOW TO CREATE VALUE?

The very first step in a networked growth strategy is to identify and decide upon the platform(s) for value creation. It is useful to decide a dominating platform that would underpin the value creation process and efforts. The platform that dominates at one time or for one set of application need not remain dominant forever or for every application. However, it is useful for a dominating platform to still build upon the pre-dominating platform, leveraging its positives and compensating for or even correcting its negatives. Successive or simultaneous development of platform in terms of varying functional inputs and servicing propositions is critical for rapid and market leading growth.

In fact, the deciding factor in creating value and succeeding is not the dominating platform, but the entire network of functional inputs and servicing propositions on which that platform is constructed and deployed. The dominating platform for Karvy was accounting and finance, where the founders had a professional background. Over the years, a dominant focus was put on information technology for creating value from the accounting and finance competency. Eventually, the market leading position of Karvy came not only from accounting and finance and information technology, but also from complementary set of platform competencies such as in human resources, customer relations, and research and development. Value was created not only by using these competencies in finance and accounting business, but also by using them as businesses in their own right – such as back-office human resource services offered globally.

To assess and quantify the platform competencies, and the value created from their exploitation as businesses in their own right, it is critical to have a strategic framework. In the new age, companies use both functional inputs and servicing outputs as their platforms. Functional platforms are specific value levers used by the companies for creating value, while servicing platforms are overall business propositions offered by the companies as integrated value creation.

## FUNCTIONAL PLATFORMS

Gupta's '9M' framework provides a useful approach for assessing functional platforms (see Gupta et al, 2006). The 9M's include manpower, material, method, money, manufacturing, machine, marketing, motivating, and manipulating (see Exhibit 2). The start-ups usually rely on one of these as their dominating value lever. The new age professional services firms typically rely on human resources, as manpower tends to constitute a significant share of their cost. The new age manufacturing firms typically rely on supply chain, as materials tend to constitute a significant share of their cost. During their start-up years, most Silicon Valley firms have relied on research and development, seeking to discover new methods for networking, communication, and computing. At the Wall Street firms, on the other hand, the emphasis has been on innovative finance and accounting to support, control, and accelerate the monetary power. Facing severe shortage of resources, the post-War Japanese firms successfully relied on their operations for creating value, achieving a high-performance manufacturing. Gradually, they have learnt to use the information technology and tapped the artificial machinery intelligence to improve their administrative and support services.

For the European firms, customer relations has conventionally been key to their ability to drive value from the premium and luxury segments, endowing them with great marketing power, despite high resource as well as operating costs. In the newly vibrant African nations, the firms are pioneering new models of distinctive leadership, where the members are intrinsically motivated through humane consideration for the betterment of their communities, to help come out of the centuries of impoverishment, destitute, corruption, violence, and diseases. Finally, among the most successful of Indian start-ups, a strong sense of fiduciary mission is evident. They are seeking to manipulate a range of diverse cultural practices, diverse work values, diverse constituency interests, diverse organizational goals, and diverse identities – at personal, family, community, national, and global levels – to create and accrue rapid value.

We noted the significance of networking the entire platform of functional inputs for the eventual success. For each functional platform, both content as well as process is relevant. Content refers to the proportionate significance of a particular platform, and the mental composition of that platform. Process refers to the management of a particular platform, and the maneuvering power that platform offers. In case of Karvy, from a content perspective, human resources are proportionately the most significant platform, because of the high muscle power – i.e. negotiating strength – of human resources in a professional services firm. These human resources can be decomposed into several mentally relevant groups, such as in terms of their domain competencies, gender, managerial skills, and cultural savvy. However, from a process perspective, human resource management at Karvy is still evolving in terms of practices and is not yet a benchmark for the industry. Further, that human resource has been maneuvered in diverse domains largely in India only, and had to be focused on delivering primarily back-end services to international clients for creating value from the global market.

**Exhibit 2:** Gupta's 9 M Framework for Functional Platforms

| Strategic Functions | Functional Strategies |
|---|---|
| 1. Manpower | Human resource |
| 2. Material | Supply chain |
| 3. Method | Research and development |
| 4. Money | Finance and accounting |
| 5. Manufacturing | Operations |
| 6. Machine | Information systems |
| 7. Marketing | Customer relations |
| 8. Motivating | Leadership |
| 9. Manipulating | Fiduciary |

## SERVICING PLATFORMS

The firms create value not only with their functional inputs, but also with the business propositions they offer. Five fundamental business propositions can be assessed using the '5Y' model – economy, quality, variety, productivity, and agility (see Exhibit 3). Economy refers to the cost-effectiveness of a firm's services. Quality refers to the conformance to customer specifications, needs, and preferences. Variety refers to the robustness in meeting the diverse needs of a customer, and of a group of customers. Productivity refers to the resources consumed for delivering a product or a service. Agility refers to the speed and flexibility in adapting to changes and deviations.

Value is created when the firm effectively manages and balances synergies and trade-offs among the 5Y's. Synergies arise when the firm is able to deliver all the 5 Y's proficiently, without compromising on its fiduciary mission for profitability as well as sustainability. Toyota, for instance, has shown that better quality and greater agility implies more productivity, more economy, and more variety. It has been able to move both downmarket as well as upmarket in the automotive industry, and has maintained a rather resilient growth trajectory.

Trade-off occurs when the firm must emphasize one business proposition over others, if it has to satisfice all its fiduciary stakeholders at least to some extent. Toyota, for instance, had to forego economy and open its factories in the US where the cost of quality and variety was higher, in order to satisfy the US government which had put voluntary export restraints on it during the 1980s.

**EXHIBIT 3: 5 Y'S OF SERVICING PLATFORM**

## CHANNEL STRATEGIES: HOW TO CAPTURE VALUE?

Once a firm decides how it will create value, and discovers where the value can be created, the next step is to actually capture the value. The fact that value can be created does not imply that the value will automatically be created. The inter-play of market forces certainly generates incentives for being efficient and creating most value. However, the impact of market forces is moderated by the human factor – one needs at least one human to start a process at a connected local place for the global process of market force inter-play to initiate. Even then, the trading factor moderates the global process

- the same level of traded value may be attained by different platforms of value creation, and knowledge gaps may limit the speed of raising the traded value level.

To capture value, it is critical to manage both the human factor within the organizational channels, as well as the trading factor without the organizational channels.

## WITHIN (INTERNAL) ORGANIZATIONAL CHANNELS

Within an organization, value is captured when the platforms – i.e. functional resources and servicing propositions – are appropriable. If other firms can imitate, replicate, substitute, or bypass a firm's platforms, then the value potential of those platforms is eroded. For instance, the value of Amazon's platform for online book purchases was eroded as Barnes and Noble replicated the online model. To ensure value capture, the firms often seek to lock-in their platforms, such as through patents, copyrights, and business secret clauses. Though the value of the locked platforms is more appropriable, the level of this value itself is lower. The locking sustains and enhances the knowledge gaps in the market.

On the other hand, when the key to open the lock is shared with other firms in the market, the value of the platform increases – though it also becomes less appropriable. For instance, when Barnes and Noble also entered the online model of books marketing, it increased the trust of the customers in online purchases by virtue of its long established reputation. Thus, the size of the online market increased for books as well as for other products, allowing Amazon to become a one stop point for a range of products.

Strategic unlocking of platforms can therefore help firms attain right levels of appropriability and enhancement in the value of their platforms. The locks on the platform can be explicit or implicit. For instance, a firm that operates only in one nation puts an implicit spatial lock on its platform, because that platform then is less known in other nations.

## WITHOUT (EXTERNAL) ORGANIZATIONAL CHANNELS

Without an organization, value is captured when the equity is invested in trading external platforms. More equity intensive options offer more real options for value add, as the firm gains direct experience and maintains direct control over platforms to add value. However, more equity intensive options also absorb more resources with which to value add. Therefore, it is important to strategically decide the mode of equity investment. In descending order of equity intensity, the following are the major channels for capturing value.

- **Incubators:** Incubators created as special entities outside the mainstream organization are most equity intensive – they demand greatest amount of resources for the longest time. They also offer most real options for development of new technologies and ideas in multiple directions.
- **Outright acquisitions:** Value in currently under-developed platforms may be captured through outright acquisitions of firms with more developed complementary and supplementary resources.
- **Joint ventures:** Two or more firms may collaborate to capture value in their respective under-developed platforms.
- **Licensing:** A firm generally stands in the middle of certain firms with more developed platforms, and others with less developed platforms. More developed platforms may be licensed from some firms for learning and scale augmentation, and less developed platforms may be licensed to other firms for capturing value.
- **Sub-contracting:** Less developed platforms may be subcontracted to other firms in exchange for a share of the value from their more developed platforms. Similarly, less developed platforms may be subcontracted from other firms and value may be captured by offering them services based on more developed platforms.

## PERPETUATION STRATEGIES: HOW TO SUSTAIN VALUE?

Once value has been created and captured, the firm needs to take steps to ensure that the value is sustained. Value can be sustained if the platform of firm remains competitive and constructive. Platform is a foundation upon which a firm must build competitive standards. If a platform is not appropriately enhanced, then it may lose its competitiveness. For instance, the strategy consulting firms in the US are losing value in their strategy formulation business because the tools and frameworks

developed by them are now being taught in all undergraduate and graduate level business classes. They are also losing value in their strategy implementation business because their domain expertise is less useful in the new age of domain-focused organizations, than it used to be in the older age of domain-diversified organizations.

To sustain value, standards using platforms must be appropriately formulated, and appropriately implemented.

## FORMULATING THE COMPETITIVE STANDARDS

A firm is expected to satisfy the demands of its diverse stakeholders, and stakeholders like to maintain stake in the firm only until those demands are met competitively. A focus on meeting those demands competitively, however, does not ensure forever value perpetuation. Sometimes, a firm has to educate its stakeholders that its platform may be more valuable if it does not serve those demands, and instead meets alternative demands. For instance, Karvy stopped serving its clients with its automated financial service package, once computers with spreadsheets started being used more pervasively in the industry. Instead of still trying to compete, Karvy redeployed its platform for automating share transfer and register services.

Thus, a firm needs to have competitive standards for the correlation between its technologies and its stakeholders – including customers, vendors, communities, partners, and workforce – when the market forces so demand. Deploying those technologies on the basis of only emotive and sympathetic social capital may result in diminished value, where the existing relationships would be significantly challenged. Not all stakeholders may be able to withstand this challenge, and many may decide to break their ties.

## IMPLEMENTING USING INTELLECTUAL PROPERTIES

Once competitive standards have been formulated for the technologies serving the stakeholders, those standards need to be implemented using appropriate intellectual properties (IP). When evaluating alternative demands, the standards may give complete liberty to a firm to look for unknown knowledge about unknown something, even if that may likely generate only unknown IP value, requiring unknown time and money to develop and diffuse, and necessitating discounted capital budgeting approaches for appraising if the current value could be sustained. Or, the standards may call for a more disciplined approach to service real aspirations of real communities in real time to improve the reality of this world, using accelerated accrual value.

More liberal standards are effective only if a firm has captured sufficient value, or has networked supportive stakeholders, that allow it resiliency should lot of developed resources need to be deployed for a lot of time. If a firm needs to catch up and is behind, and has not been able to capture full value from its platforms, then it can first generate greater value through a more disciplined approach, and thereby sustain its value. The evolution of Karvy's businesses suggests that the latter approach works well even when the resources are limited, as in the case of most start-ups. Over its evolution, Karvy has sought to create and capture value through various 9 M's, developing a dynamic relationship among them. Information technology competency was used not only to run the business, but also evolved into a business. Similarly, human resource competency is now being used not only to run the business, but is being evolved into a business itself.

## CONCLUSIONS

Past empirical research indicates that some firms are able to sustain rapid growth rates, particularly from their early formative start up period. A majority tend to have limited growth rate that is highly contingent on the macro environment conditions. While others appear to be permanently failing and are slow growing. A promising line of investigation into the explanation of these empirical regularities is offered by the network view of strategy. Given the increased significance of networking in the contemporary strategic environment, we asked why certain start-ups are able to generate continuous networked growth, while others get trapped or destroyed in the networked world. The framework of networked growth provides valuable guidelines.

Successful start-ups grow their monetary power by creating value from each element of their functional platform – whether it is manpower, or material, or method,

or machinery, or marketing. They also generate value through their fiduciary mission, leadership, and operations.

Successful start-ups offer valuable business propositions – they are themselves and help their stakeholders to be – agile, cost-effective, productive, quality, and diverse.

Successful start-ups capture value by strategically unlocking their within organization resources and platforms.

Successful start-ups capture additional value by investing their equity in channels without organization that allow opportunities to exploit their under-developed resources and platforms as well.

Successful start-ups sustain current value by formulating competitive standards for the correlation between their technologies and relationships with their stakeholders. They do not take emotive and sympathetic social capital for granted.

Successful start-ups perpetuate accelerated value by using intellectual properties available within and without organization for solving the technology gaps, and thus realizing rapid networked growth.

They thus accumulate abundant resources within and without organization for taking up broader challenges that require fundamentally new discoveries and innovations. Further empirical research would be desirable to test these predictions.

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