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# How can SMEs support growth in a low-growth region?

# A longitudinal study of SME growth facilitation

**Annabeth Aagaard & Martin Senderowitz** 

#### Abstract

The objective of this paper is to obtain application-oriented knowledge of what creates growth in small and medium-sized enterprises (SMEs). The paper aims at identifying and describing key internal business processes that contribute to growth through a longitudinal study of eleven SME case companies located in a low-growth region. The findings of the study reveal six key growth-facilitating themes that are critical when actively supporting firm growth in a low-growth region.

#### Key words

Growth factors, small and medium size enterprises (SME's), longitudinal multiple case study

#### 1. Introduction

In recent years, a large number of studies of small-firm growth have been performed and reviewed (Delmar, 1997; Wiklund and Shepherd, 2003; Sadler-Smith et al., 2003; Davidsson et al., 2010; Love and Roper, 2014). Although the topic of small-firm growth has received quite extensive attention, several reviewers deliver with relatively critical accounts. The criticism concerns both theoretical and methodological shortcomings (Storey 1994; Gilbert, et al., 2006; Davidsson et al., 2010; McKelvie and Wiklund, 2010; Wright and Stigliani, 2013). In spite of the longitudinal and process nature of the concept of "growth", many growth studies are cross-sectional. In growth and entrepreneurship research, there is a general wish for more longitudinal "real time" research (Davidsson et al., 2010; Wright and Stigliani, 2013). As described in the theory section below, a large number of firm growth factors exist (Gilbert et al., 2006; Davidsson et al., 2010). These growth factors can both be internal/organisational factors and external market factors and they can act both as positive *drivers* of growth and as negative *barriers* or *obstacles* for growth.

Extant growth and SME literature has extensively addressed how firms' grow is related to favourable external conditions and how firms do not grow due to unfavourable market conditions (barriers) (Wright and Stigliani, 2013). However, current empirical research on firm growth in adverse conditions is scarce, and knowledge of how firms may grow (i.e. the mechanisms and drivers) in spite of generally unfavourable, external conditions is limited (Bamiatzi and Kirchmaier, 2014). This explorative study investigates key drivers of growth for SMEs in an external context characterised by low growth and economic recession. The study investigates how a number of Danish SMEs have achieved high growth rates in spite of unfavourable external conditions. These SMEs are facing the specific challenges of few highly specialised employees, low funding opportunities for SMEs, few large companies from which to attract larger groups of employees, and educated/specialised citizens moving to high-growth regions with more possibilities. Growth in the context of low-growth regions is an unexplored area within SME and growth research, and the findings presented here are relevant and applicable for managers in SMEs as well as for policy makers and institutions supporting growth and business development in low-growth regions. This paper provides insight into the key facilitators of growth in Danish SMEs in a low-growth area. The research question of this paper is: »How can SMEs in low-growth regions actively support firm growth and which facilitating activities are applied?«

To answer this research question, we examined eleven Danish SMEs over a period of 18 months within a specific region of Denmark characterised by low growth and a less favourable socio-economic situation compared to growth rates and the financial situation in the rest of the country. In the next section of the paper, we discuss and elaborate on the theoretical perspectives of firm growth and SMEs, including internal and external growth factors. After the theoretical discussion, we present the methods applied in the study. We then present the empirical findings, and we conclude with a discussion of the results and the implications of the study.

#### 2. Firm growth and growth facilitators

From the review of growth studies (Penrose, 1959/95; Gilbert et al., 2006; Garnsey et al., 2006; Davidsson et al., 2010; Senderovitz, 2010; Wright and Stigliani, 2013), it is clear that growth factors can make out a very long "laundry list" of factors that may facilitate or hinder growth. Growth factors can roughly speaking be divided into internal (within the firm) and external (environmental) factors, even if it may in some instances be difficult to determine what is truly external and truly internal (Davidsson et al., 2010). The industry development is usually seen as an external factor, whereas in a Porterian world, industry affiliation is seen as a strategic choice made by the firm (Porter, 1980, 1985). Similarly, opportunities may be viewed as external factors, i.e. factors "out there" to be discovered, or as factors that the firm should create and develop internally (Shane and Venkataraman, 2000; Dew et al., 2009).

### 2.1 Internal growth factors facilitating or hindering growth

In her seminal work on firm growth, Penrose (1959/95) argues that firm resources play a key role in achieving growth and competitive advantages. Limited resources mean limited possibilities for growth. It is through the internal resources in general and management resources in particular that the firm may develop unique entrepreneurial (managerial) services which are, in turn, seen as a prerequisite to firm growth and to achieving competitive advantage. According to Penrose, the internal resource use is a key determinant of firm growth. Internal inducements to expansion arise from the existence of currently unused productive services, resources and specialised knowledge which, according to Penrose, are always to be found in any firm (Penrose 1959/95, p. 66). The issue of management capacity has been elaborated on and categorised by Storey (1994) as management motivation, education, management experience, number of founders and functional skills. A number of studies have investigated the relationship between growth aspirations and actual growth. These studies in general find that managers with higher aspirations achieve higher actual growth. In this view, it is up to the management of the firms to lay the foundations for growth (Wiklund and Shepherd, 2003; Delmar and Wiklund, 2008; Stam and Wenneberg, 2009).

#### 2.2 External factors facilitating or hindering growth

External factors also influence growth. These factors include macro-economic development, market conditions, environmental dynamism, access to external financial capital, access to other external resources and network, and access to general human capital (education level) and specific human capital (experience) (Wiklund and Shepherd, 2003). Growing ventures are highly dependent on the local environment for resources needed for their operations, and the ability to acquire resources locally has substantial implications for the levels of growth the firms will attain. The growth of the individual firm is also influenced by the growth of the industry and the economic and financial situation of the country and region as well as the industry dynamism (Gilbert et al., 2006; Bamiatzi and Kirschmaier, 2014). In general, firm growth appears to correlate with the general macro-economic and regional financial trends.

Summarising, from a theoretical perspective we argue that achieving growth may be a matter of management capacity, growth aspiration, willingness and skills, but that fundamental facilitators and obstacles in the environment play a key role for firm growth.

#### 3. Methodology and empirical context

The objective of the paper is to obtain application-oriented knowledge of what creates growth in SMEs. To investigating this, we use an exploratory longitudinal multiple case study design. This article is based on a research project conducted in collaboration with Danish Regions (Danske Regioner) with an aim to enhance SME growth in a low-growth region. The research project falls in two phases. The first phase identi-

fied growth processes in SME growth companies in the specific low-growth region of South and Western Zealand in Denmark, where 38 randomly selected companies were contacted. The case companies were selected based on their size (private SMEs) , their location in or in close proximity to the region of South and Western Zealand, a positive growth record during the past 3 years, and, finally, case companies were selected representing different industries. The fourth criterion was included because industrial characteristics may affect growth potential. We contacted 38 case companies, expecting that approximately half of them would accept the invitation to participate in an interview. Out of the 38 case companies, 20 companies accepted to participate in the project and through site visits and individual interviews with the CEOs and other key personnel, we made extended company portraits of these 20 companies. The data collected during the interview sessions were analysed using meaning categorisation (Kvale and Brinkman, 2009), where similar statements from the interviews were grouped within related themes, and six key growth themes were derived through an abductive process (Danermark et al., 2002), going »back and forth« between theory and the empirical evidence (company portraits and data from the interviews).

These themes were explored further during the second phase of the project in which 11 out of the 20 firms were selected for further in-depth longitudinal analyses (see Figure 1). The eleven firms were selected based on relevance to the project objectives, variation across different industries (four production/retail, five service/knowledge service and two building & construction), and willingness and ability to participate in the in-depth studies.

We investigated the 11 firms over a period of 18 months, where management and employee representatives were interviewed to explore the specific contents of the identified growth themes and the actual growth-facilitating activities involved. The data derived from the interview sessions were analysed through meaning–categorisation, and the facilitating activities within each of the six growth themes are explained in detail in the findings.

#### 3.1 The empirical context

The firms in this study are located in the Southern and Western part of Zealand. The four key growth and social-economic challenges of this region are related to low productivity in the region's own businesses; globally oriented industries gradually moving to other regions; difficulty attracting and retaining highly skilled employees; and finally that innovation is concentrated on a few, but very innovative companies. In addition, the region is challenged by the demographic development. If the projections of the age composition hold, the reduction in the number of people in the working age (as predicted by 2015) will significantly decrease the level of prosperity and growth in the region (Copenhagen Economics, 2005).

#### 4. Findings

In the following section, we will describe the growth facilitating activities according to the six growth themes and the contexts in which the activities unfold for the respective firms. Figure 1 shows the case companies with an indication of primary and secondary growth themes as some growth themes were of higher priority in some of the case companies. The identified growth themes include: 1. Strategic thinking, 2. Self-managed teams, 3. Management of public fundraising, 4. Open source innovation, 5. Middle-sourcing and 6. Local and regional networks.

Figure 1: Company overview and growth themes					
Company	Industry	Offerings	No of employees	Primary themes	Secondary themes
Westrup	Production	A global export and production company of agricultural machinery	80	1;4;5	2;3;6
Toftebo maskinfabrik	Production	A small blacksmith shop manufacturing its own products in stainless steel and specializes in playground equipment	9	2;6	1;3;4;5
RM Fintech	Production	A precision engineering workshop that specializes in the machining of precision components and other precision mechanical productions.	26	2;5;6	1;3;4
Ostebørsen	Retail/ production	A small trading company that buys and sells luxury cheese and carry out events	18	1;2;6	3;4;5
Geocenter Møns Klint	Service	An experience and conference center with more than yearly 500 events, 3D cinema, expeditions, snorkeling trips and nature walks	25	1;2;3	4;5;6
Vilcon	Service	A conference center, which consists of three centers	15	1;2;4;6	3;5
Kragerup gods	Service	A conference center with a Go-High activity areas and an integrated course program	70	2;3;4	1;5;6
Gerlev legepark	Service	An activity park that is part of a Sports Academy that offers different play projects to the private and public sector	12	3;4;6	1;2;5
Casalogic	Knowledge service	A consulting company that provides It-infrastruc- ture services and solutions to companies using 'Open Source' systems	12	4;6	1;2;3;5
Urhøj Smedie	Building and construction	A smithy that supply plumbing, ventilation and other energy preserving solutions	26	1;5;6	2;3;4
Altan.dk	Building and construction	A construction company, which designs, supplies and installs balconies on existing blocks of flats.	85	1;2;6	3;4;5

After a description of each growth theme, we present a small real-life narrative to illustrate how SMEs may work with the specific themes in practice.

#### Growth facilitating theme 1: Strategic thinking

What does working with strategic thinking imply?

Existing research underlines that the SMEs' approach to strategy is inherently different from that seen in large companies (Hofer and Charan, 1984; Sadler-Smith et al., 2003; Evald and Senderovitz, 2013). The management in a small firm usually consists of a single or very few individuals who then, naturally, have to carry out all managerial and strategic tasks and responsibilities. One of the important issues in terms of strategic thinking is how to balance the tension between strategic *planning and goal setting* for setting targets and giving the firm a clear sense of direction on the one side, and to stay *flexible and improvisational* for being able to explore and exploit the unexpected events and contingencies on the other side. Managing this balance may be one of the most important factors influencing smaller firms' growth and competitive advantages (March, 1991; Hitt et al., 2011).

#### How do SMEs work with strategic thinking in practice?

Ostebørsen's ability to improvise and make quick iterative moves according to the changes in food trends and customers' taste has made them competitive and able to achieve high growth rates. However, as the organisation is growing, the management feels that too many decisions are made going in various directions; and they need to become more structured and have a more formal, clear strategy and work in one, unified direction. The challenge is to plan ahead and remain flexible and agile. In this process, the two owner managers have started mapping the individual functional areas of the company including the related actions and each employee's required competences and responsibilities while leaving room and flexibility for each team of employees to make their own independent decisions. They thereby try to maintain a balance between improvisation and planning.

#### Growth facilitating theme 2: Self-managed teams

What does the establishment of self-managed teams imply?

Establishing self-managed teams means deliberately giving autonomy and formal decision-making power to a team of employees without the classic direct supervision of a line manager. By giving responsibility to small teams of employees and allowing them to exercise a high level of self-management, the team should – according to the firms – carry out key decisions without management's involvement and the firm thus attain a higher level of flexibility and efficiency. The informants from all eleven case companies indicated that they had been able to ensure higher growth through the application of self-managed teams in different functions of their organisations.

#### How do SMEs work with self-managed teams in practice?

GeoCenter Møns Klint applies self-managed teams in its development and innovation function. In this function six people with very different skills (e.g. biology, geology, project management, financial management and creative skills) are put into play by their collaboration on specific projects. The growth potential in the application of self-managed ad hoc based teams at GeoCenter Møns Klint lies in the benefits that come with the small and flexible organisational way in which the event-oriented businesses of the company are organised. This allows them to be more efficient, more flexible and have fewer fixed costs than would be the case with a permanent development organisation.

#### Growth facilitating theme 3: Management of public fundraising

What does management of public fundraising imply?

SMEs' ability to attract external funding for development projects, particularly from the public sector, is a way to overcome the regional resource scarceness within the private sector. Public funding can help the SMEs obtain growth by financing and supporting firm-b ased development projects serving, e.g., a cultural or a leisure-oriented purpose. Some of the companies have experienced declining sales in recent years; however, with effective project management targeted towards public project funds, the companies have been able to develop and grow strategically into other businesses and industries. In order to obtain adequate public funds, it is important to duly prepare project descriptions, which includes integrating »administrative« public procedures and obtaining public-private-collaboration experience with new technologies; and it is important to develop personal relations (local, regional, national) for project collaboration and fundraising.

#### How do SMEs manage public fundraising in practice?

**Kragerup Gods** has developed and created growth through an investment project in an experience centre offering »Go-high activity areas« and they have developed an integrated course programme. Owing to a publically funded investment project, Kragerup Gods has been able to develop and attract new business and reach new target groups, which has improved their competitive advantage and corporate branding in comparison to other, traditional conference centres.

#### Growth facilitation theme 4: Open source innovation

What does working with open source innovation imply?

Open source innovation focuses on the interaction between producers and users of innovation, and employee-driven innovation is focused on innovation initiated and facilitated by staff. These two innovation approaches conceptualise companies' processes of interactive learning at the micro level (Lundvall, 2009). Both research and practice show that both a formal and an informal approach to these innovation processes may

be taken (Smith, Ulhoj & Kersting, 2012). In the present cases, active and continuous dialogue with customers to detect their needs is a key growth-facilitating activity that generates new solutions. The customer is, indeed, the key driver of the innovation processes, providing input for tailored services and products to suit the specific needs of customers whenever possible. This approach gives smaller firms a potentially competitive advantage compared with larger companies with more formalised processes that lend themselves less readily to such flexibility.

#### How do SMEs work with opening the innovation processes in practice?

**Vilcon** is experiencing a growth dilemma: the owner is a key driver of the business innovation processes, but may become a bottleneck hampering the company's continued innovation and growth. The solution for Vilcon has been to create an open and forthcoming culture, where ideas can come from anyone inside or outside the organisation; and once »matured« the ideas may be integrated quickly and efficiently owing to the firm's flat and team-oriented structure which promotes the implementation of user-producer and employee-driven innovation. At Vilcon, customers' needs and requests and customers' interaction with the employees often initiate ideas for new products or services.

#### Growth facilitating theme 5: Middle-sourcing

What does working with middle-sourcing imply?

Middle-sourcing occurs when similar production/operations are taking place simultaneously in two (or more) different – but collaborating – companies. Middle-sourcing may be seen as an »alternative« to outsourcing, where the production of (part of) a product is removed completely from the focal firm. In SMEs, outsourcing may be counter-productive for various reasons; first, because transaction costs may be higher than expected; second, because smaller firms may encounter difficulties dealing with the management challenges of international outsourcing co-operations; and, finally, companies which have experienced ongoing improvements and efficiencies in a Danish context, may find that this may not necessarily continue when production is outsourced to foreign countries. To address these challenges of outsourcing, middle-sourcing is emerging as a viable alternative that achieves competitive advantage and flexibility while minimising production-related risks and maintaining the potential for continued improvement.

#### How do SMEs work with middle-sourcing in practice?

The two companies **FM Fintech** and **Hardi** are in the same line of business and they produce similar (albeit not identical) products. Originally, Hardi planned to outsource their production completely to FM Fintech. However, the two firms decided to engage in middle-sourcing instead to stimulate the flexibility and the competitive advantages of both companies. By applying middle-sourcing, they assist each other in gaining access

to larger customers, and they both minimise their individual risks. They can enhance flexibility and potentially exploit each other's production capacity in peak situations and enhance flexibility and reduce costs. For FM Fintech and Hardi, a positive side effect is that the production and business stay in the local region (as opposed to outsourcing to other countries/regions), which creates a local demand for skilled labour.

#### Growth facilitating theme 6: Local /regional relations based networks

What does working with local/regional relation based networks imply?

SMEs are highly dependent on local/regional relation-based networks in their pursuit of growth and development. A key challenge of SMEs relates to the fact that they have fewer internal knowledge resources because of the smaller number of their employees. The local/regional relation-based networks do not only provide opportunities for collective learning and knowledge development, they also provide access to resources and potential collaboration. This creates a good foundation for innovation and growth among the SMEs – both as individual organisations and as groups (Keeble & Wilkinson, 1999). Characteristic of success in these types of networks is a high level of mutual trust and interest among the networking partners, as the networks are not based on formal contractual relations. However, a regulative factor is proximity, as 'everybody knows everybody' in local/regional communities. So if one network partner does not deliver or live up to the expected level of co-operation, that partner may be excluded. The incentive to be trustworthy as a network partner may therefore be expected to be relatively high in these types of networks.

How do SMEs work with local /regional relation-based networks in practice?

**Toftebo** is actively networking with similar companies that otherwise could be seen as direct competitors. Such co-operation with the »competitors« is based as much on social relations as on business deals. In this network, solutions are created in a mutual and flexible process that does not rely on formal agreements or contracts. This network helps Toftebo gain competitive advantages, flexibility and access to more and larger assignments and contracts that they would otherwise be able to carry out themselves. In Toftebo's local region, demand is rather confined, and collaborating with other similar, otherwise competing firms makes it possible to gain larger-scale orders outside the local area in with they normally operate.

In summary, the eleven case companies revealed that a logical and hierarchical order of the six growth factors exists. Fundamentally, the case companies all had clear growth intentions and shared an interest in strategic thinking and worked diligently on nurturing their strategic growth potential through various strategic initiatives. This appeared to be a prerequisite for their success and growth. The lack of resources in these small firms was accommodated by organisational designs focusing on self-managed teams. By allowing the employees room to explore and to take on responsi-

bilities, the case companies gained access to more knowledge and innovation potential from their dedicated employees.

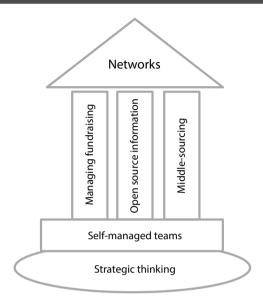
The strategic thinking combined with the self-managed organisation of employees was supported in particular by three key activities: open source innovation, middlesourcing and fundraising. Open source innovation was applied by all the case eleven case companies in various ways and resort to self-managed teams allowed the firms to 'think outside the box' and to open up the development and innovation potential. Middle-sourcing was applied as a way to ensure flexibility, primarily by the production companies. Furthermore, fundraising was applied to gain access to resources for new development activities, yet primarily by the service companies. However, all three activities were undertaken in an attempt to gain flexibility (either financial, innovation/resource-wise and/or to achieve production flexibility) and as a way to navigate effectively as a local/regional SME in a low-growth region in a post-fiscal crisis time. Finally, the case companies' local and regional based networks contributed to all the other five growth facilitators by providing knowledge, collaboration, innovation and by facilitating joint growth; hence, the networks were therefore used extensively by all eleven case companies. Figure 2 below illustrates the logical order of the six growth-facilitating themes.

#### 5. Discussion

The study reveals that firms achieve growth by applying an interplay of internally and externally oriented activities. The different characteristics of the eleven case companies indicated variations in which growth facilitators were most optimal in supporting growth in the specific context, industry and situation of the case companies. In line with contingency theory (Galbraith 2012; Van de Ven et al. 2013), the practical implications of the findings stress the need for SMEs to identify and develop their unique set of combinations of growth facilitating activities in pursuit and support of growth, as no one solution or specific set of growth facilitators fits everybody. However, a larger comparative study would have to be carried out to be able to identify the correlations between industry, company situation and growth facilitating activities.

Strategic thinking is a key element in ensuring growth in SMEs. Existing research has stressed that strategy in SMEs is different from strategy in large organisations. However, little is known about how SMEs actually apply strategic thinking, manage their organisations on a daily basis and to which extent they use emergent and/or planned actions. The findings of the present study revealed different combinations of actions where the SMEs were combining their flexile emergent actions with more planned activities to various degrees. These findings are not conclusive, and a large study of strategic thinking among SMEs could provide further knowledge in relations to how combination of planned and emergent actions or combinations hereof generate

Figure 2: The six growth facilitation activities



more growth in certain types of SMEs, contexts and situations. The successful application of the autonomous teams and self-management as growth facilitators implies, in practice, that SMEs invest in developing the employees' professional skills to be able to handle more and different assignments, including their ability to organise, plan and communicate at many different levels. The new project economy may be an important and neglected growth facilitator for SMEs. The study show that administrative capabilities and effective processes encompassing preparation of project descriptions that include integration of public procedures, as well as the use of personal network (local, regional, national) for project collaboration and fundraising, are important for attracting new public funding.

It is a common theme in the public debate that wage competition (primarily in the industry) from low-wage countries constitutes a serious challenge for maintaining and expanding employment in Denmark. Conversely, the case companies have applied middle-sourcing activities to ensure a movement in the opposite direction – maintaining flexibility as well as production and jobs in Denmark. Middle-sourcing as a business strategy is perhaps one of the findings with the greatest growth potential. It is also a phenomenon that is not (yet) well-identified and included as part of the economic policy efforts. The recommendation is therefore to consider this opportunity and to further examine how middle-sourcing may take place in a Danish low-growth regional context.

In regard to user-producer and employee-driven innovation, SMEs need to be aware of the fact that the lack of process formalisation and involvement of external knowledge

(apart from that of the customers) may represent challenges. Knowledge sought primarily among a few company employees may represent a potential limitation to new innovative solutions. If you ask the same people each time, then you are like to only get the same response and approach. This finding stresses that extended interaction with external partners is important to ensure innovative solutions and development. However, the customer's knowledge - or lack of knowledge - may potentially be a barrier to radical innovation if companies focus too much on solving each customer's hereand-now needs. As a business strategy, user-producer and employee-driven innovation may demand the fewest resources for generating positive growth for businesses. The findings of the present study support the existing research, suggesting that SMEs participating in networks enhance their competitive advantage and growth. Conversely, much of present research focuses on the professionalization and formalisation of the networks. However, the cases presented here show that there is a wide selection of collaborative networks that are informal, and the findings stress the need for companies to nurture their local networks and harvest the growth potential even more. The informal networks should not necessarily be changed into more formal ones, as it appears that the level of informality may actually be the strength of the networks for the SMEs.

The six growth-facilitating themes were present in all the case companies. However, some of the case companies portrayed these growth themes to a much larger extent than the others and some of the themes were critical to their ability to generate growth. The growth themes and facilitating activities identified in the present paper will hopefully inspire both theoretical and applied studies in the field of SME growth.

#### 6. Conclusion

The findings provide demonstrate a chronology of growth facilitators, and the identified six growth themes and related activities may serve as inspiration for SMEs. A longitudinal study of eleven cases may be considered acceptable for preliminary and exploratory conclusions; yet, no statistical generalisation can be made based on the present study. The findings and contributions of this paper offer suggestions for future research. Of particular interest would be to perform similar research across different companies and industries to determine whether the present findings are generic or industry/context-specific. One could speculate whether the industrial context would emphasize certain growth facilitators over others because of the similarities in industrial context and characteristics. This study was performed in a regional context of Denmark, and the findings may therefore also be influenced by regional/national characteristics. Given the implications of the present study, a quantitative, comparative study of applied growth facilitators across different industries and different regional/national contexts is called for to test the combinations and generalisability of the six growth factors.

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