

If you want to become an international player, forget about emulating the success strategies of the global multinationals like Dell or Coca-Cola. Business strategist Professor Bernd Venohr has been studying the success factors shared by Germany's mid-sized world leaders, and he believes these lessons are far more relevant to Irish SMEs.

Mary Sweetman reports.

HOW MID-SIZED COMPANIES CAN BECOME **GLOBAL LEADERS**

Business strategy predominantly originates in the US – a large and fairly homogenous economy driven by powerful multinationals and their globally recognisable brands. But how applicable are lessons from these giants to ambitious Irish SMEs striving to expand their global footprint? Are there more relevant models and success stories closer to home?

Bernd Venohr certainly thinks so. The Professor of Strategic Management at Germany's largest business school - the Berlin School of Economics – he has spent most of his career working as a management consultant, including 13 years with Bain and Company and five years as Managing Director and Partner with Accenture. Now embedded in academia, he is analysing the success factors behind a distinct brand of German companies, originally identified 15 years ago by Hermann Simon, in his book *'Die heimlichen Gewinner'* or *'Hidden Champions'*. What's remarkable about these companies is that they enjoy relative obscurity - often located in rural areas, and predominantly family-owned - yet they have grown, quietly but quickly, to claim the number one or two positions worldwide in their market niches.

In particular, Professor Venohr's research is focused on 'mid-sized companies' with a turnover between €1 billion and €50 million - somewhere in scale between large multinationals and the EU definition of an SME.

"The US is very much a large-scale market, with big multinationals, and they have definitely cracked the code there," he told *The Market*. "But I would say Germany has really cracked the code on how to succeed as a small or medium-sized company in the global economy."

Certainly, they play a major role in the country's economy. Germany - the biggest exporter in the world - is the only large economy outside China that is continuing to grow its share in world trade. And in 2004, some 3,200 mid-sized companies contributed a whopping 30 per cent to this export figure. So what are their secrets?

THINK NICHE, TAKE IT GLOBAL, BRING IN OUTSIDE MANAGEMENT, KEEP INNOVATING AND ALIGN YOURSELF TO SOPHISTICATED CUSTOMERS.

1) THINK NICHE AND TAKE IT GLOBAL

One common thread Germany's 'midsized champions' share is a needle-eye sharp product focus, often zooming in on the most esoteric sector or supplying the most obscure part or component. However, this is coupled with an ambition to achieve broad geographic market adoption. "Why not crack global markets, when you create your own niche and become the best?" is how Professor Venohr sums up the philosophy.

"Niches work," he argues. "This has is something unappreciated in management literature, because they think too much in terms of mass-markets. However, very few markets are really mass markets; if you analyse the global market, you may find it has 1,000s of segments."

"A key lesson for Irish companies," he says, "is to always think niche. That means looking for a narrowly defined group of customers and developing some very good solutions for them."

The secret, he adds, is to focus on customers who are globally at the top of their game. Germany's mid-sized companies have clustered around their leaders in automotive and engineering sectors. But this doesn't make sense for Irish companies; there's simply nothing to build on.

"On the other hand, Ireland has five or six very strong sectors: food and drink; pharmaceuticals and medical devices; software, technology, and financial services, created mostly on the back of foreign direct investment," Venohr says. "There is already a good network in these industries, a good research base and some sophisticated customers, which companies could expand from."

He underlines the point by citing the example of an Irish business whose customers include the locally-based subsidiaries of two global leaders in the food and beverage industry. Working closely to meet the needs of these two highly sophisticated customers, the company developed very specific solutions, which it can now export to the beverages industry worldwide.

The German model of going global is particular apt for small Irish companies, he believes, because the population here is so small that there is no significant internal market. But the challenge is in building up global distribution

networks. "Your foreign operations are usually not profitable from year one, and this is something Irish companies should look at in a more patient way, with a more long-term focus," he argues. "Here the Germans really have shown tremendous position and built up those networks over 20 or 30 years." Generally, they resist the temptation to take the easy route of signing up a distributor. Instead, in important markets, a German company is more likely to set up a local subsidiary and service network, so it can stay close to its customers. "This gives you tremendous insights into customer problems and then feeds into the innovation process, providing a sustainable niche position," Venohr says.

2) BRING IN OUTSIDE MANAGEMENT

The merits of family ownership/private finance versus a public listing or venture capital make perennial fodder for business debates. On this score, Venohr believes that the second success factor Germany's midsized champions share is their ability to take the best from both worlds.

"Building up sales and distribution networks takes a lot of time, so that's where the long-term horizon is really helpful. If you have very greedy shareholders, who are short-term focused, you have a problem. What really helps in family ownership is a long-term commitment to cracking world markets."

On the other hand, succession is a major weakness in family-owned companies. "In many cases, unfortunately, this leads to disaster," Venohr says. "It is unlikely that the son or daughter will be as good as the founding entrepreneur, and by the second or third generation, they are usually very challenged."

What's significant in Germany is that, since mid-sized companies are largely family-owned, there is a willingness to accept short-term pain for longer term gain. But in contrast to the UK and France, where there tends to be automatic coupling of family ownership with family management, they are also open to bringing in outside management.

"Quite often - and this is another lesson for Ireland - they recruit people from large multinational operations in Germany, like the Procter and Gambles and the HPs of this

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world.” Venohr believes this is a win-win proposition. “They are bringing in professional management experience, and for the manager, it’s a great opportunity to run their own business and to really apply their professional management skills.”

3) COMMIT TO ABSOLUTE EFFICIENCY AND CONTINUOUS INNOVATION

The mid-sized champions third success factor is that they live up to that German stereotypical image of absolute efficiency, using such tools and strategies as total quality management and continuous improvement to relentlessly root out waste and optimise quality.

“Something that has contributed to this is that German companies took advantage of the opening up of the former Eastern Europe, and we have seen many parts of the supply chain being moved there,” Venohr says.

Significantly, German global leaders also spend two to three times as much as their industry peers on R&D. On this score, Venohr is irked by what he sees as the tendency for sloppy, misleading characterisation of what constitutes ‘high-’ versus ‘low-’ tech in management literature. “Hi-tech is superficially defined as telecoms, IT and biotech, but that’s not necessarily true,” he argues. “Some companies in these areas may be merely applying IT skills; whereas you can see real technological wonders from bottle filling machines to automatic harvesters in any number of sectors defined as low-tech.”

The lesson for Irish companies, he says, is to realise that innovation should be on their agenda regardless of whether or not they are superficially labelled ‘hi-tech’. Like their German counterparts, they need to constantly ask themselves how they can use R&D and IT innovations to drive continuous improvement.

THE BUSINESS ENVIRONMENT MATTERS TOO: LESSON FOR GOVERNMENT

In summary, Venohr’s formula for building a global business is: think niche, take it global, bring in outside

management, keep innovating, and, align yourself to sophisticated customers.

While it sounds simple, he readily accepts that the business environment matters too: Ireland isn’t Germany.

For instance, Germany has a tremendous network of research institutes tasked with transferring knowledge from universities into companies. “In Germany, this system is working really well, and it’s really a government job to establish those institutes, who then help companies become world class. What you can learn from Germany is to go beyond the headlines and really take innovation seriously, investing for a medium-term horizon and accepting that you won’t get pay back in year one or two,” he argues.

The balancing of family ownership with professional external management may prove a harder nut to crack. German companies are open to this, Venohr says, due to a range of complex factors - from the German psyche to inheritance laws and Germany’s unique financing system. For instance, some 50 per cent of finance for small and medium-sized enterprises is still provided by community banks. “These banks provide financing at a very reasonable cost; they are not run for profit maximisation, they have some community responsibilities. They are very important, especially at the early stages, they don’t give out large loans, but they are probably a bit more patient than the large banks run out of the city,” Venohr explains.

On this score, while he acknowledges Ireland may have a much healthier venture capital environment than Germany, he suggests there is a need for alternative funding options, less focused on short-term return on investment. “Maybe the Government could encourage banks to provide for rapidly growing mid-sized companies not falling in the bracket of being a typical venture-backed company, he says.”

Of course, as well as serving as role models, Germany’s mid-sized champions represent a considerable - yet largely unrecognised - economic force. “So I would definitely say there are opportunities for Irish companies to sell to and partner with them,” Venohr concludes. **M**

FOR FURTHER INFORMATION ABOUT PROFESSOR BERND VENOHR’S RESEARCH PLUS HIS DATABASE OF OVER 1,500 TOP PERFORMING, MID-SIZED GERMAN COMPANIES, VISIT THE ENGLISH LANGUAGE VERSION OF HIS WEBSITE: WWW.GERMANWORLDMARKETLEADERS.COM. FOR INFORMATION ON DOING BUSINESS IN GERMANY, TALK TO DEIRDRE MCPARTLIN, EMAIL DEIRDRE.MCPARTLIN@ENTERPRISE-IRELAND.COM