# Recipes for successful companies

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## 1 Background

The Swiss economy is suffering from weak growth. For some years, its GDP has been growing at a rate well behind that of some other countries. Even if the extent of the growth deficit and the choice of suitable indicators for measuring the growth differential are disputed, few would argue with the statement that Switzerland is lagging behind.

Not all sectors and industries are equally affected by the slow growth. Generally speaking, the industries geared to the domestic market are seen as the main reasons for the relative low level of economic growth in the economy as a whole. Owing to isolation from (international) competition, their prices are regarded as comparatively too high and growth in the industry low. By contrast, export-oriented companies, which have always had to face up to global competition, specialised early on and are thus deemed to be decidedly more competitive. The difference in labour productivity between domestic and export-oriented companies is often cited as an indicator of this.

The growth differentials between the various sectors of the Swiss economy are indeed striking, especially in an international sector comparison. However, the different growth rates cannot be explained only in terms of the export ratio. Moreover, individual companies in the same sector perform differently, as no industry is a homogeneous whole.

## 2 Question and relevance

Different sectors in an economy or different companies in a sector may therefore have greatly varying growth rates. What distinguishes successful from unsuccessful companies? Are there success factors that are universally valid? Can economic policy provide impetus for successful business activity?

A microeconomic approach to this macroeconomic question is certainly appropriate. For instance, the OECD has recently made more resources available for research into the direct entrepreneurial environment. The focus is on the optimal allocation of resources in relatively narrowly defined sectors (market entries and exits of new or mature companies) and on the (productivity) development of existing companies.

## 3 Survey

In order to answer the basic question as to whether there are recipes for success for corporate growth, the Swiss National Bank's delegates for regional economic relations conducted a series of interviews with entrepreneurs as part of their regular special reporting in spring 2004. The most important findings, supplemented with further feedback from company visits, are briefly summarised here.

### 3.1 Company selection and statistics

The companies were chosen from all regions in Switzerland. Sales growth, profitability and increase in the number of jobs were taken as success criteria. As no representative database on successful companies – based on objective criteria – was available, the delegates for regional economic relations were responsible for selecting successful companies from the regions concerned.

43 company visits were evaluated for the survey. The companies are in sectors that account for around 45% of the entire added value of the Swiss economy. If only those industries are included whose companies have a commercial purpose (i.e. excl. public administrations, associations, etc.), the coverage rate is considerably higher. The companies visited have above-average productivity levels and growth rates that are higher than the industry average.

The companies were also characterized by the properties summarised in table 2 below: They are all small or medium-sized enterprises (SMEs) and most are family-run limited companies, over half of which are managed by the owner.

**Companies visited** Table 1

| NOGA sector [1] | No. of visits | Change in nominal sales as a % p.a. over at least the last 5 years [2] | Nominal sales per employee in 2002 in CHF 1000 [2] |
|---|---|---|---|
| Food/confectionery | 7 | 4–6% (> 10%; > 20%) | 230 / 1000 |
| Textiles and clothing | 2 | 6–14% | 330 |
| Chemicals/pharmaceuticals | 5 | 15–20% | 400–600 |
| Plastics/packaging | 2 | 10–15% | 250 |
| Metal | 4 | 7–9% | 250–350 |
| Mechanical engineering and automotive | 5 | 8–10% (30%) | 150–450 |
| Electrotechnology/medical technology | 7 | 10–15% / 25% | 200–360 |
| Retail trade | 3 | < 10% (15%) | 250–350 |
| Hotels and catering | 2 | n.a. | n.a. |
| Transport | 2 | 10% | 160 |
| Corporate services | 2 | 30% | 150–250 |
| Other | 2 | n.a. | 320–500 |

1 General Classification of Economic Activities, Swiss Federal Statistical Office, own industry allocation of companies surveyed
2 Scope of answers, extreme values in parentheses
Source: Own surveys

## 3.2 List of questions

The main focus of the discussions with the companies was on the following topics:

**Market development**
- In what market environment does the company operate?

**Product innovation**
- What is innovation?
- What triggers innovation? Is it a structured process?
- What role does product innovation play in success?
- What role do innovation clusters play (proximity to universities/universities of applied sciences, competitors, customers or upstream service providers)?

**Process innovation**
- What importance is attached to optimising and restructuring company processes?
- Do process innovations cut costs, have an impact on locational decisions or even generate new business models?

**Marketing**
- How is marketing organised, what role does it play in business management?

**Qualitative aspects**
- How important are soft factors such as corporate culture, managers' leadership skills or the staff's professional qualifications in general?

## 4 Findings

The survey showed that there are no real recipes for company success and certainly none that are valid across the board. The following characteristics of successful entrepreneurship nonetheless emerge:

- **Market analysis:** Successful companies know their operating environment and the factors that drive their markets. They keep a keen eye on their competitors and their strategies, and thus their competitive environment, as well as on the legal and any political framework.
- **Flexibility:** It is virtually impossible to find a strategy that, once developed, can be successfully implemented. The discussions convey the impression that successful companies are those that manage to adapt rapidly to changes in their environment or within the company itself. Strategies that fit together logically and meticulously ex post, and are also perceived as strategies, are seldom planned that way ex ante.
- **Differentiation:** In the long term, companies only succeed if they manage to set themselves apart from their competitors. Successful companies are better than their competitors, either because they offer the same quality at a lower price or because they provide better quality (products).

**Further characteristics of the companies surveyed** Table 2

| Workforce | No. of companies | Public limited company | Family-run limited company or privately held limited company[1] | Managed by owner | 2002 sales in CHF millions[2] |
|---|---|---|---|---|---|
| < 100 | 7 | 0 | 7 | 3 | 5–85 |
| 101–250 | 9 | 3 | 6 | 5 | 30–250 (2500) |
| 251–500 | 8 | 2 | 6 | 2 | 70–250 |
| > 500 | 19 | 10 | 9 | 6 | 100–double-digit billion figures |

1 Incl. one cooperative and two limited companies owned by foundations
2 Scope of answers, extreme values in parentheses
Source: Own surveys

- **Product innovation:** Product innovation is the lifeblood of successful companies. Whether a change or improvement is an innovation will be decided by the market. Customers are only prepared to pay for something if it increases the benefit to them. Successful companies will therefore involve the customer early on in the innovation process.
- **Process innovation:** Successful companies optimise their processes either to cut costs or to improve processes. Successful companies facing cost-related competition base their success on process innovations. Company processes are fragmented and reorganized. The added-value chain can be extended or shortened, and vertical integration (upstream and downstream company processes) and horizontal integration (similar or related processes) can change.
- **Ability to cooperate:** Particular importance is attached to a company's ability to cooperate, regardless of the closeness of this cooperation or its legal form. Cooperation with universities/universities of applied sciences as well as with competitors, suppliers or customers with the aim of improving technology transfer, managing procurement or sales markets or developing new corporate processes with suppliers or customers are of paramount importance.
- **Customers' standpoint:** Successful companies always look at their position from the customer's standpoint. What are the customer's needs? To what extent are they prepared to pay?

## 4.1 Market growth

The choice of a suitable strategy depends greatly on the market environment. In growing markets, a company must grow just as quickly as the market if it wants to be successful. This calls, first and foremost, for a functioning innovation policy. New products must be developed in growth periods in particular. In the survey this was seen primarily in the rapidly growing medical technology and pharmaceutical industries. Companies can only achieve lasting success if they innovate continuously. Secondly, the company must be in a position to quickly expand its production capacity. Critical factors during the growth phase are financing for the innovation policy and for expanding production capacity, the development of a corporate culture geared to growth and maintaining a fast pace of innovation.

Other strategies are called for when markets are stagnant or contracting. Either the company will succeed in segmenting the market and finding a growth niche, or it must attempt to gain market share at the expense of its competitors. In this case the cost side is of crucial importance. Low costs make it possible to take up a strong position in a price-based competitive environment, to gain market share, to expand production and thus to achieve economies of scale.

In the consumer goods industry, it was found that pricing strategy does not have a great chance of success owing to international competition. Here, the companies surveyed rely on market segmentation and brand strategies. This strategy has proved advantageous to the retail trade too for many years. Examples are the organic foods or natural foods segments. However, typical representatives of the niche strategy also include capital goods companies. Successful companies often occupy a niche that is growing faster than the market. The core competency of these entrepreneurs is their ability to innovate, especially their products. Thanks to new materials or process innovations, they achieve solutions that set new standards of application, security or miniaturisation.

## 4.2 Product innovation

Virtually all of the companies visited named the ability to innovate as a key success factor. It is the only way to set oneself apart from competitors in the long term and to win out over lower-cost locations. Whether or not a change is a genuine innovation depends on how it is seen by the customer. Only if a change increases customer benefit, as reflected in his willingness to pay, can it be considered an innovation. "The marketability of changes determines how innovative they are."

Successful companies are able to use the customer's standpoint as a trigger and driver of innovation and to operate a "systematic innovation policy" within the company at the same time. When taking the customer's standpoint into account, the survey showed that mixed project teams, for instance, comprising providers and clients, can be very successful. These types of cooperation, however, require considerable trust between the partners. Typically, they are found in industrial companies, especially in technologically advanced areas such as the capital goods or customer synthesis/specialty chemicals industries. In the consumer goods industry or retail trade companies try to identify customer preferences via market monitoring or surveys. Direct contact at the personal level plays less of a role here.

Close cooperation between companies and universities of applied sciences/universities has proved useful where innovation policy is "more systematic and institutionalized". Small and medium-sized enterprises, in particular, depend on this geographical and specialism-related proximity and cooperation. It is no coincidence that SMEs attempt to influence the range of subjects offered at regional universities of applied sciences or to set up universities of applied sciences in their related fields. Technological cooperation can also come about between different companies. Examples were seen of former competitors who have been entirely able to find either temporary or permanent forms of cooperation that benefit both sides. Ultimately, this may lead to two or more companies joining forces or individual upstream or downstream processes being integrated and the depth of added value changed.

## 4.3 Process innovation

The survey showed that process innovation can serve several purposes at successful companies:

- Process innovation should achieve more efficient processes and help to cut costs. Just as product innovation is crucial for all companies, exploiting cost-cutting potential through process innovations is a must. Companies in consumer-related industries, such as the retail trade or food production, attach particular importance to this factor.
- Process innovation should help or allow companies to fragment and rearrange their processes. This leads to the "make or buy" question and may result in the outsourcing of individual processes as well as the integration of new ones. The added-value chain is therefore changed. This can ultimately lead to the global optimisation of the activities that companies carry out at various sites. This purpose was stated by companies in the textile and clothing industry, the mechanical engineering and automotive sectors and by electrotechnology and chemical/pharmaceutical companies, i.e. companies which operate globally or which are reviewing their business model, as well as former production facilities, which are now concentrating on engineering/design/sales/corporate centre functions and buying products instead of manufacturing them.
- Process innovation allows service companies to enter into new activities. This trend is visible with services, in particular; the borders between process and product innovation are fluid and barely distinguishable in this segment. Examples are modern logistics groups that have developed from transport companies, or manufacturers of products in the healthcare segment, whose added value is generated not primarily via the product's hardware but through training in fields of application.

## 4.4 Marketing

The survey showed that marketing plays a very important role. Here, efforts go beyond distribution channels, sales drives and the identification of the customer's willingness to pay. Marketing is quite simply a means of observing markets, identifying market trends or, as seen, guiding innovation policy. Marketing can thus be a tool for positioning the company and market segmentation. It can also be an expression of its corporate culture. The survey conveyed the impression that successful companies deliberately look at things from the customer's standpoint. The company's management leads by example and the approach is usually institutionalised in the form of organisational or leadership measures.

## 4.5 People make the difference

Despite the various facets of a company's success as revealed in the survey, it was seen that people ultimately play the key role. The conduct of a company's workforce, management and, in particular, owners is a key determinant of its success. Why a company is successful or unsuccessful is often impossible to determine objectively. Accordingly, all of the companies surveyed attach considerable importance to staff development. This is demonstrated by the fact that ongoing training is very important to entrepreneurs. Family-run companies in particular, or companies with a "patron", to borrow the French term, repeatedly emphasised the importance of loyalty not only towards their customers but also with regard to their employees. It is often difficult for SMEs to institutionalise the much-cited know-how transfer from universities or universities of applied sciences within their companies. They have to rely on maintaining the innovative capacity of their business from within. It is therefore especially important for employees to remain with the company for many years and to undergo ongoing training, and such companies support these principles.

The ownership structure of a company is an important factor. Family-run companies or private limited companies often emphasise that they are not subject to the same pressure as public companies to maximise profits and returns. These companies feel that their investment ratio is higher and – since their payback horizon is longer – that it is easier for them to develop better and sustainable new business segments. In general, business activity is geared less to satisfying the demands of the financial community than to safeguarding the company's long-term existence. The trend appears to be for successful public companies to focus on return and growth, while family-run companies or privately owned limited companies concentrate on sustainable development.

One of the disadvantages of family-run companies is seen as (overly) tight financial constraints, especially in growth periods. IPOs (initial public offerings) or going public are thus often unavoidable as a way of broadening the equity base in growth periods. However, successful public companies frequently address the – at least latent – conflict of interests between the need to finance growth and dilution of (original) owner interests. This is particularly important as companies often point out that financing growth through borrowing is becoming increasingly difficult. The banks' conservative valuations of company assets and a focus on the earning power of investments weigh on creditworthiness precisely in periods of growth and innovation. Companies with a constant cash flow are more positive about the commercial banks' lending policy, however.

Family-run companies or limited companies that are privately owned or owned by a small group of shareholders certainly see the danger that less pressure could also lead to lower risk awareness. Long payback horizons can lead to poor investments; a lack of pressure from the capital market can delay vital changes in corporate policy.

## 5 Macroeconomic conclusions

Growth is an important precondition for successful business activity. It is not enough to count on earnings power or profitability, the survey found. Hence, the following challenges arise for the company and the state:

- As an alternative to financing company growth with bank loans, some companies are proposing tax incentives to create risk capital.
- A growth policy at company level calls for an expansion of technical and human resources. The critical factor is the availability of a suitably qualified workforce. Training in selected scientific areas or increasing the appeal of the Swiss job market to international specialists are key tasks for government.

A company's ability to innovate is the tool that will allow it to achieve a lasting differentiation and growth strategy.

- SMEs depend on a close proximity to universities and universities of applied sciences. However, geographical proximity is only useful if it enables a lively exchange of knowledge and technology transfer. The interfaces between theory and practice must be increased, and exchange at the personal level as well as of know-how must be improved.
- Process innovation aimed at cutting costs increase labour productivity. As these are sectors which – as mentioned in section 4.3 – belong to the less dynamic domestic market, negative employment effects should be expected in the short term.
- At global companies, process innovation can lead to the optimisation of company locations. They tend to result in production cuts in Switzerland, especially if it is comparatively labour-intensive. At the same time, however, this trend results in the creation of new jobs that usually require higher qualifications and productivity.
- The fragmentation of working processes and the decentralised location of these activities around the globe is accentuating structural change. Locational appeal is based on comparative advantage. In the case of Switzerland, this advantage lies not in labour-intensive, manual activities but in specialised, high-quality processes and functions in the fields of research, company management and associated corporate services.