



## Business in “insignificant” markets

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The Pareto 80/20 formula, which states that 20% of the most important markets, customers or products account for 80% of the success results in the withdrawal from, or the non-entry into - at first sight - insignificant markets. However, opportunities for activity within these market segments often exist, not only to generate turnover, but also to realise profits. Only an adapted approach can lead to success in this context and its consistent implementation is a controlling task.

### Definition of insignificant markets

The existence of insignificant markets presupposes the existence of different sub-markets. This is only the case if a division of the overall market is possible. Two extremes rule out different markets: on the one hand, a uniform market may exist, such as for information on the internet, which is categorically available to the same extent in every place in the world; on the other hand, products can be so complex that the production takes place locally, yet can only be performed through specifically provided specialists, such as in large-scale plant engineering, so that here the same providers equally compete on a global scale. The services considered in this text sit between these two extremes. That is, products of a medium complexity which are demanded locally. This fundamentally concerns most products. They may be machines and products which are produced elsewhere, but require explanation, professional installation or regular maintenance, or that are sold directly to the end consumer in smaller volumes, as either shipment is uneconomical or not acceptable to the customer.

		Necessity of personal support	
		Low	High
Complexity of the service	difficult	Data processing facilities	plant engineering
	easy	Books, consumer items	Groceries, long-life consumer goods, property equipment

Four typical characteristics of insignificant markets can be noted accordingly.

- On an international scale, the complexity of the uniform market is too high or too costly to overcome. This includes language barriers, an insufficient legal framework, if for example, the necessary legal protection is not granted, or corruption is thereby preventing implementation.
- Inadequate infrastructure is another point. In many countries, transport and storage options are limited, permanent and stable power supply is not given, or the protection of property, sometimes also that of staff, is not guaranteed.
- The number of potential customers is considered too low. Either the population is simply too low, or the price expectations of the manufacturer and the payment options of the customer exclude each other.
- A lack of trained staff and the excessive investment in their training and in forging lasting bonds of loyalty between them and the company are deemed further arguments for exclusion.

To think only in an international dimension is insufficient in this context. Such markets also exist in the national sphere. While the above noted failings may not be present, they are substituted by other reasons for ruling out an involvement.

- The development of the overall population, in particular that of people with purchasing power, varies across Germany. While some metropolises report increasing population figures, the rural population is in decline. Particularly some of the East German regions show dramatic developments. This is linked to an even more substantial decline in purchasing power.
- Even in a country with excellent infrastructure, such as Germany, poor accessibility may represent an exclusion criterion for involvement. If permanent and short-notice accessibility is required, this can often only be ensured through a tightly knit net of offices and branches. If distances are too large, and the additional costs are not acknowledged by the customer, the activity becomes uneconomical.
- The relevant regions are often unattractive for the employees. It is almost impossible to find employees who are willing to relocate. Where a willingness to relocate exists, this often applies to inexperienced entry-level employees who by themselves are not able to meet all requirements.

The first task of controlling will be to determine whether the listed conditions exist in the company, and whether the services provided by the company encourage a more intensive analysis of the opportunities and risks on the basis of preliminary results. In the next step, it may be reasonable to consider the creation of appropriate conditions in a targeted manner. This happens, for instance, if a company that in the past exclusively operated in production, now supplies end consumers and offers additional services, such as installation or service and maintenance provision. As the competitive pressure tends to be lower in these areas and the potential profits are higher, many companies pursue these areas. To avoid fuelling unnecessary conflicts with current partners and to gain first experiences, entry via insignificant markets may be the right strategy.

No later than at the point of conclusion of the first considerations, company management is informed and the basic concept is presented. This will determine the subsequent approach.

## **Reasons for involvement**

Services in markets that already offer these conditions cannot be offered at the same cost as those in the main markets. Any illusions must be cleared up before market entry.

Nevertheless, countless reasons for market entry can be found.

The arguments presented above with respect to the lack of attractiveness are also known to the competition. Therefore, there are usually fewer competitors. If they are active in the market regardless, only a few, reduced services are usually offered. Employees often regard their responsibility as “deportation”. Therefore, new tasks are sought, both internal and external to the company, and fluctuation is high accordingly. Strong commitment is hereby not developed; excitement is not sparked amongst the customers. Thus, competition is very simply less intensive than in markets which are more aggressively contested.

A variety of costs on these regions is significantly below the average values. While fuel and energy prices are certainly comparable, land and property costs and wages are substantially lower, plus generous funds are often provided through the federal states, local officials are available as contacts, and they are often happy to provide support on a variety of issues. In addition, a large number of qualified staff are available. Quite a few people are looking for opportunities to return to their home region and are willing to accept a pay cut in order to do so.

The customers are well aware of the situation in the region. The economic decline is a reality and people and companies leave the area. Developments in the opposite direction can rarely be recorded. Consequently, new or increased involvement is perceived positively. In contrast to other markets, new providers have a head start. The customers also know about the disadvantages of their region, long transport routes and low volume receipts. If additional costs can be justified, customers are generally prepared, and often also able, to carry these.

However, misjudgement should be avoided: remote does not equal “backward”. The customers are indeed capable of gathering relevant information and of comparing offers accordingly. If individuals are not able to do so, family members offer assistance, particularly with respect to larger offers that require explanation.

At this point in time, precise calculations can certainly not yet be performed. However, controlling is able to collect preliminary information. This is the point at which potential markets ought to be defined and inspected, and contact to selected contact persons should be initiated. The preparation of detailed investment plans is not yet required. The focus is rather on gaining first impressions. This may well be achieved within the scope of a business trip with a slight detour and stop over. Competent and committed contacts, for instance in economic development, are easy to locate. Due to the difficult situation in the region, both public and private entities often offer an unusual openness and willingness to help.

## **Analysis of the value chain**

The objective of entry into insignificant markets is no different to other business activities. The goal is the realisation of profits. This need not happen in the short-term, but definitely in the medium term. As a higher degree of insecurity exists than is the case with typical investment decisions, risk minimising measures will be the focus throughout the preparation of market entry. This is even the case against the background of a low probability of rapid action by the competition due to the market situation.

Accordingly, the value chain is analysed with respect to flexible or outsourcing options.

Here, the activities at the location of the customer will be a key aspect. It has to be made clear to everyone involved that the business model that is successful in the main market is bound to fail here. Tasks that are performed by internal staff at established locations have to be dele-

gated to local partners. Their options need to be evaluated realistically. Complex solutions should be minimised at least at the initial stage; a standard offer that can be mastered without years of experience ought to be provided. This limitation can and should be explained offensively, only where it is acceptable to create the impression of incompetence of local staff. The focus should be on emphasising their flexibility.

It is more beneficial to the company to execute market entry on a small scale with stable income than to aim for a digression of fixed costs through unrealistic sales figures. This is why the flexibility of costs is of major importance. In this respect, the local partners are placed in a key role. At this point, the reference to partners instead of employees is deliberate. Where firm instructions to dependent employees are the right solution in established markets, entrepreneurial freedom is only limited in insignificant markets if it is necessary in order to retain the identity of the company as a whole. Entrepreneurial cooperation is the preferred maxim, whereby opportunities and risks are borne in partnership. The partner can cover typical fixed costs, such as personnel, property and vehicle costs. If they operate in comparable business areas, they often have excess capacity, the use of which does not create any additional costs. Of course, local partners should not be taken advantage of and the use of their capacities should be rewarded. However, this should be on a variable basis, even at the price of higher initial costs, rather than as a one-off provision of capacities.

Further, the most appropriate legal form of cooperation needs to be established. This can range from stronger emphasis of performance-related remuneration components to complete independence.

## **Conveying the decision within the company**

As presented above, the offer in insignificant markets differs from that in the primary markets. In the majority of cases, this means a reduction or outsourcing of activities. This typically affects direct customer interaction which is not realised through internal staff, but is outsourced to an external partner. This may be parallel to a reduction in the range of services offered. Employees often react with anxiety to these changes and assume that such measures are in fact only a test which, following a successful implementation, will equally be established in the primary markets, resulting in redundancies. This objection must be debilitated and the changed business model in the new markets needs to be portrayed. After all, the utilisation of service provision and the increase in sales also safeguards jobs at the primary location. Convincing employees is therefore of major importance, given that on the operational level they are the ones in immediate contact with the new contact persons. An understanding of their situation needs to be developed, particularly in the initial stage.

Further, the sales department must also be informed of the decision. If customers hear about the new offers, it cannot be ruled out that comparable offers are requested. In that event, sales must be able to explain the reasons behind the regional division to the customers.

Controlling will perform the information of employees of the company and present the reasons and objectives of the project. The arguments presented above are portrayed and any questions that may arise are answered in this context. Personnel may support this appearance, not the other way around.

## **Market presence**

Offering the same range at the same prices as in the primary region will entail insufficient revenues. Nevertheless, clear priorities should be set prior to market entry. Services of a

slightly lower quality at slightly higher prices will rarely be a successful strategy. Naturally, price transparency is high in the age of the internet; however, customers are generally willing to accept higher prices that they can comprehend. This also holds true for the completeness or speed of various components of the offer. In this regard, it is equally important not to create a false impression of equal services being offered in all sub-markets. This is often the reason for a withdrawal of unsatisfactory results in insignificant markets.

So-called cafeteria systems, where the customer is able to cancel certain components of the service package, should be considered critically. Particularly in rural regions, many opportunities for neighbourhood assistance exist, whereby services may be performed privately which would otherwise be a component of the service offer. Transport, as well as professional installation and commissioning should be considered here. However, the resulting need for price transparency is seldom desirable. Further, optional components are often rejected, even if no appropriate alternatives exist. Subsequent inadequate functionality, complaints and disagreements would cause discontent and a dramatic increase in costs.

The actual market entry can often be achieved more cost-efficiently than in other regions. Due to the reduced economic attractiveness, negative economic news dominates. The public and the press are inclined to pick up on positive news and allow it to spread.

Controlling will identify funding opportunities and initiate contact with the relevant entities. As funding is linked to the compliance with certain conditions, the planning of the project will place controlling in the best position to evaluate where pledges may be made and where this simply is unrealistic. This not only concerns legal relevance, given that cooperation based on trust is the essential foundation for any further funding or investment in the relevant markets.

## **Selection of responsible persons within the company**

Companies that have low expectations in certain markets place employees in positions of responsibility of whom equally low expectations are held. The impression that “discontinued models” are responsible for discontinued markets can often not be concealed. The conditions presented above should, however, lead to the opposite approach. There are few better opportunities to prepare junior staff for management tasks than to transfer responsibility to them here. It is because these markets are relatively insignificant for the company as a whole that junior employees can prove themselves here, not in a specialised part of the business, but in a role of responsibility for all aspects. Even if a return to specialised tasks is realised at a later stage, the insight that is gained in other areas of the value chain of the company will retain value.

This overall responsibility is also expressed in terms of remuneration. Low fixed amounts are linked to strong performance incentives, which are deliberately uncapped. Strong personal commitment and a willingness to move their lives to not necessarily attractive regions must be rewarded. Due to the overall responsibility, the determination of performance indicators is unproblematic.

Particularly in the initial stage, local partners require an immediate contact person. This person should be employed at the main location and always be available. As the scope and the intensity of his services are almost impossible to determine in advance, flexibility is recommended. Often, experienced managerial staff who are retired, but have a desire to remain active on a freelance basis to a certain extent, are often a valid option. Here, flexible remuneration should equally be agreed on, which limits the financial risk for the company and promotes entrepreneurial action. These solutions largely allow the disburdening of the contact persons within the company, and the additional expense with respect to support can be limited.

Controlling not only dictates these developments, but leads by example. Each controlling department should be seconded by ambitious employees who largely want to prove themselves in terms of independent responsibility for a project.

## **Selection of local partners**

In sparsely populated regions, the same services are generally demanded and provided as in large cities. However, the structure of the providers moves from specialists to generalists. Niche markets based on sufficient demand are not in existence here. Therefore, a wide range of services is offered. As the local partners must be able to largely act autonomously, their selection is a major success factor. Intensive discussion at local level is imperative. Persons who may not appear to be one hundred per cent suitable at first sight can prove to be good partners, which is why personal talks should be held with a large number of interested parties.

Primarily, certain flexibility with respect to the demands is necessary. Often, highly qualified and motivated people are employed below capacity. This not only refers to people looking for work, but also retirees who want to return to their home region after termination of their professional life and who still have a desire to be economically active. The concept of entrepreneurship is granted a stronger significance than on the primary markets, as extensive specialisation is not possible. The persons responsible will provide not only the sale, but also the performance and settlement of the service as well as subsequent service, and will therefore act as an entrepreneur in the spirit of the word.

Common convictions and values cannot be presupposed but must be created. If no previous points of contact exist and the partner only has general market and product knowledge, plans must be made for time to be spent together. Apart from visits to the company headquarters and the support of operative procedures, the future design of every individual step in the new market must be determined. Sustainable practical procedures can only be obtained by a mutual search for solutions, not by a one-sided specification. The creation of mutual convictions requires time; a fortnightly fast-track tour through all departments does not suffice for this purpose. Rather, a designated personal contact partner should intensively support the implementation and continue to act as a central point of contact at a later stage.

Appropriate incentives for future cooperation need to be found. The usual forms of remuneration of the company's employees will rarely prove suitable due to the different business model. Autonomous activity will often be the better solution, whereby personnel must assess the lawfulness. In any case, the expectations of the partners must be taken into account. A complete package must be put together, as apart from the operative performance. Property and vehicles also form part of the overall solution.

Even the usual specification of objectives and their relevant checks cannot be realised in the markets described here. Rather, a strong strategic check should be implemented, whilst operative freedom is created. Opportunities and risks are certainly higher here than in "regular" business decisions. Therefore, generous but firm expenditure specifications should be determined. These investments defined in advance represent the maximum commitment. Where those limits are exceeded, the project is terminated. This stance must be shown clearly to all parties involved at the start of the project in order to avoid later irritation and disappointment.

With all these risks, markets considered insignificant may in fact turn out to be successful objects. This then feeds the desire at the headquarters to introduce the usual procedures that are established in the primary market. The removal of the current partner would result, as he would no longer fit into the adjusted business model. This, however must be refrained from. The local representative is the central point of contact for existing and potential customers. If he were pushed out of business, his move to the competition would entail a sensitive weakening. While non-competitive clauses may be agreed by contract, the compliance with these is difficult to enforce. This is why any planned changes to the business model must be communicated to the partner at an early stage and mutually agreeable solutions must be found. The provision of a time limit in combination with an offer for permanent takeover will also be able to satisfy the company's own demands.

Controlling will reflect this situation in the business plans and accept limits, even in the event of success, which necessarily exist in insignificant markets and cannot be pushed beyond a certain extent. With all the euphoria following a successful start, the same targets cannot be defined for the region of Uckermark, as for that of Hochtaunus.

## Case study

A stair lift supplier is firmly established within a radius of 50 km of his company headquarters. Adverts, close contact to medical supply retailers and personal recommendations ensure a strong market position. Even if individual competitors are able to provide cheaper offers, his particular strength is in customer service. Most customers are elderly and equipment is not always used appropriately. A typical usage error is the failure to drive the lift into the final position, resulting in the omission of the recharge of the battery. Even such minor issues cannot be solved over the telephone, but require a visit by a service technician that is highly competent in the interaction with elderly people. Due to the limited regional scope, the optional service contract provides for the performance of three such visits free of charge. Further, a pledge is made for a service visit to be performed within a maximum of two hours in the event of an emergency. This is an important factor for the customers, who regularly live in their own home, which often features living rooms on the ground floor and bedrooms on the first floor.

To gain the support of the specialist areas involved, the relevant targets were agreed before the start of the project and the support of controlling as the department responsible for the project was defined. Figure 2 summarises requirements and agreed measures.

Specialist area	Requirement	Controlling measures
Marketing	Comparable market presence	Central responsibility Training of the employees of the contract partner
Sale	Consideration of journey times, pooling of appointments, adjustments of success evaluation to the lower prices	Adjusted targets, amended determination of success
Preparation of work	Equal quality of measurements	Intensive training of the local partner

<b>Procurement/ production</b>	Same requirements	
<b>Installation</b>	Consideration of travel times, clarification of issues of overnight stays	Agreement with personnel with respect to adapted operative agreements
<b>Service</b>	Maintenance of central tour planning, documentation of maintenance services, compliance with quality requirements	Training of the metal worker, support throughout the initial stage
<b>Accounting</b>	Provision for timely invoicing	Equipment of the partner with a mobile data collection module for the daily transfer of performed services
<b>Controlling</b>	Monthly target-actual comparison, quick achievement of break-even	Separate reporting until break-even is achieved

For the first year, Controlling agrees monthly discussion with all specialist areas of the realisation of requirements and pledges rapid action if needed. In order to not overtax the new partner, a member of controlling is nominated as a central point of contact for all issues.

Despite the slow-growing market, no opportunities for growth are detected in the wider area surrounding the company location, as other, similar competitors are active here. However, a market analysis of various regions showed that about 250 km to the northeast, no comparable companies exist. So far, the offer is limited to providers operating on a national scale, which do not operate local offices in the region. A medium-sized town was selected as a future location. A medical supply retailer operates here. The owner is invited to the headquarters, the business model is explained, the benefits of the company's equipment are illustrated and reference equipment is installed. The costs of € 6,000 were borne by the company. The distribution will primarily be performed through the medical supply retailer. One member of staff that is particularly experienced in the interaction with elderly people will take responsibility for the sales, a performance component of € 300 per sale is agreed, whereby this does not differ from the agreement in the primary market. The technical tasks, in particular the determination of the staircase measurements at the customer's location for the manufacturing of the lift, are performed by a local metalworker. The installation is performed by employees at the headquarters. The installation costs are the same, however, additional journey times of about 5 hours must be accounted for. These employees also perform the maintenance at a later stage. Advertisements were placed in the local newspaper and commercials were broadcast on the local radio. All existing formats could be utilised in this context. The increased level of advertisement was reduced to regular marketing activities after three months. Due to the lower costs, only slightly increased expenditure per installation is incurred.

To facilitate the sale of the first reference installations, a temporary promotional offer is made. Within the scope of this promotion, reference installations could be sold at cost. Throughout the first financial year, a total of 16 installations were sold and the relevant service contracts concluded. In subsequent years, a target of 25 installations is aimed for.

Start-up and investment costs totalled € 18,000. At a spread across five years and a target of 116 installations at that point, this equals € 155 per installation. Further, additional costs of € 200 for the journey of the fitters for the installation must be considered, which increases the



total cost to € 355. At an average price of € 12,000 per installation, the additional costs therefore equal 3%. This certainly is a significant amount at an average profitability of 8% in the new equipment business; especially since the higher coordination effort and occasional travel expenses for initial and further training have not yet been considered. Realistically, a neutral result can therefore be expected, however, not a significant increase in revenue.

The stronger results of the maintenance business are of much greater interest. In general, one maintenance contract at €300 can be concluded each year. This includes a yearly visit of about two hours duration, the average journey time is set at one hour, as the offer is primarily realised with a 50 kilometre radius. Material costs are low, if present at all, and are charged to the customer. No additional revenue is aimed for here, as these costs are transparent and excessive rates create the impression of exploitation. A remuneration of €150 per visit was agreed with the local partner. This leaves the company with revenue of € 150. As the average useful life of a stair lift is five years, a medium-term stock of 125 installations with yearly revenues in the maintenance business of €18,750 is aimed for. The additional long-term costs are incurred in the new business, however, a cost-neutral sale continues to be targeted. At average yearly revenues of € 12,000 x 25 = € 300,000 and fixed costs of 15%, a digression of fixed costs of € 45,000 is achieved. This improves results by € 63,750. While the prices for new installations are about 10% lower than in the primary market, the regional distance means that a negative impact on the pricing levels is not expected.

In this case, the focus of controlling was not on the achievement of target results in the primary market, but rather in the achievement of an at least neutral result in the new equipment business after amortisation of the initial investment and to increase revenues with a growing service portfolio. On the basis of the experience gained, further insignificant markets are now actively sought.