

# Latvian *Hidden* CHAMPIONS

**Arnis Sauka**

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# Latvian Hidden Champions

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## Foreword

This is the fourteenth TeliaSonera Institute Discussion Paper. The Institute, located at the Stockholm School of Economics in Riga and generously supported by TeliaSonera, aims to promote applied economic research in the fields of entrepreneurship, telecommunication and information technology.

The current Paper presents five case studies of Latvian entrepreneurial success stories. The companies studied range from those already internationally recognized and leaders in their respective niches (hidden champions) through companies that show clear potential to become leaders, to a start-up with high growth potential.

This as well as previous TeliaSonera Institute Discussion Papers can be downloaded from the SSE Riga website, [www.sseriga.edu](http://www.sseriga.edu). Hard copies can be ordered from [office@sseriga.edu](mailto:office@sseriga.edu).

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## 1. Business environment in Latvia since 2004: introduction

After joining the European Union and NATO in 2004, Latvia experienced the fastest growth rates in the European Union, reaching GDP growth of +12.2% in 2006<sup>2</sup>. This was, however, followed by a sharp slowdown, starting in early 2008 – a consequence of the world financial crisis, with Latvia's GDP falling to approximately -18% in 2009<sup>3</sup>. The depth of the crisis in Latvia was also fostered by greatly increased consumption resulting from the easy access to cheap bank loans<sup>4</sup> that occurred during the years of rapid economic growth in Latvia. After the 'credit bubble' collapsed in early 2008, to stabilize the financial sector Latvia had to borrow some 7.5 billion EUR from the European Commission and the World Bank as well as other organizations and governments<sup>5</sup>.

The deep recession, among other things, also led to a reassessment of the role of entrepreneurship within the country, i.e. both the quantity and quality of Latvian companies and the quality of the business environment in Latvia. As for the quantity of the firms, even though positive signs as regards nascent entrepreneurship rates exist (Rastrigina, 2010), unfortunately Latvia has one of the lowest scores in the European Union as measured by SMEs per 1000 inhabitants (Latvian National Development Plan 2007-2013<sup>6</sup>). Furthermore, various international reports and indicators (such as the Innovation Union Scoreboard 2010<sup>7</sup>, the Global Entrepreneurship Monitor<sup>8</sup>, the Global Competitiveness Report 2010-2011<sup>9</sup> and others) show that there is also considerable potential to increase the quality of both Latvian firms and the Latvian business environment.

One of the key challenges with regards to the Latvian business environment and economic development seems to be a relatively high level of shadow economy in the country. Namely, according to Sauka and Putnins (2011) the size of the shadow economy<sup>10</sup> in Latvia reached 38.1% of GDP in 2010 and is close to double that of the neighboring countries of Estonia (19.4%) and Lithuania (18.8%). According to Sauka and Putnins (2011), the strong dissatisfaction in Latvia with the tax system and the government in particular – the inconsistency of tax policy and how the government spends taxpayers' money – is likely to be one of the main factors driving the large difference between the three countries in the size of their shadow economies. Other factors

<sup>2</sup> <http://balticexport.com/?article=latvijas-ekonomika&lang=lv>

<sup>3</sup> Source: [www.csb.gov.lv](http://www.csb.gov.lv)

<sup>4</sup> ... and overoptimistic forecasts as regards the future growth of the Latvian economy that influenced consumption behavior.

<sup>5</sup> Source: <http://balticexport.com/?article=latvijas-ekonomika&lang=lv>

<sup>6</sup> Source: [http://www.nap.lv/upload/nap/national\\_development\\_plan\\_2007-2013\\_eng.pdf](http://www.nap.lv/upload/nap/national_development_plan_2007-2013_eng.pdf)

It is worth noting, however, that the number of SMEs is considerably higher in the capital city of Latvia, Riga, reaching the EU average of approximately 50 SMEs per 1000 inhabitants (Sauka and Welter, 2010).

<sup>7</sup> Source:

[http://ec.europa.eu/enterprise/policies/innovation/facts-figures-analysis/innovationscoreboard/index\\_en.htm](http://ec.europa.eu/enterprise/policies/innovation/facts-figures-analysis/innovationscoreboard/index_en.htm)

<sup>8</sup> See reports for Latvia at <http://biceps.org/en/GEM>

<sup>9</sup> Source: [http://www3.weforum.org/docs/WEF\\_GlobalCompetitivenessReport\\_2010-11.pdf](http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2010-11.pdf)

<sup>10</sup> Here, the term "shadow economy" is used to refer to all legal production of goods and services that is deliberately concealed from public authorities. This definition corresponds to what the Organisation for Economic Co-operation and Development (OECD) in their comprehensive 2002 handbook "Measuring the Non-observed Economy" as well as the System of National Accounts (SNA 1993) refer to as "underground production". It is also consistent with definitions employed by other researchers (e.g., the World Bank study of 162 countries by Schnieder, Buehn and Montenegro (2010)).

explaining the large amount of tax evasion in Latvia include optimizing expenses by avoiding taxes and thus increasing the competitive advantage of the companies, weak legal enforcement, societal traditions of avoiding taxes as well as low standards of ethics and morality.

These findings, as well as various international indicators compiled by the World Bank, EBRD and other international organizations aiming to measure the quality of institutions, at least partly explain why the competitiveness of Latvian companies scores only 70 in the world ranking (Global Competitiveness Report 2010-2011). Here, it can be argued that improving the way government communicates with entrepreneurs and regaining the trust of entrepreneurs by demonstrating good practice as regards reducing governmental spending and implementing reliable tax policies are, among other things, the main challenges to overcome in order to improve the overall entrepreneurship climate in Latvia (Sauka and Welter, 2011).

In light of these arguments, emphasizing the role of the external environment, several studies also draw attention to the company-specific characteristics which impede the competitiveness of Latvian firms. A recent study by Sauka (2011), for instance, shows that firms in Latvia are often forced to operate at rather high costs (i.e. an outcome of technologies or premises purchased during 2007/2008 at high prices) at the same time overall offering low value added products and services. Sauka (2011) also suggests that to become more competitive, Latvian companies should increase the level of innovations considerably, be more active while working with their competitors and take more calculated business risks.

Furthermore, Latvian companies seem to be remarkably passive in using communication networks – a widely recognized tool used by successful, competitive companies around the world to attract external resources at low cost (or no cost at all) in order to achieve a competitive advantage (Simon, 2009; Cason, 2009). In this light, as reported by Sauka (2011), in general Latvian companies are virtually ignoring the opportunities that might be provided by cooperation with business laboratories, universities and research institutes – a potential source of innovations and market intelligence – as well as municipalities and business promotion organizations: resources often used by companies across the world to penetrate new export markets as well as establish the position of the company in the local market. Thus, not only overcoming burdens created by the external environment but also more careful planning of internal firm strategies are the key challenges which have to be addressed by many Latvian companies in order to increase their competitiveness and, perhaps, qualify for the ‘hidden champions title’ in the foreseeable future.

To summarize, this is no doubt a very critical view, aimed at identifying core areas to be improved in order to increase the competitiveness of Latvian companies and Latvia’s overall business environment, which in turn should lead to better economic performance. On a more positive note, however, following a steady decline of the economy as a result of the crisis in 2008, the Latvian economy actually began to recover in 2010 with +3.3% GDP growth forecast already in 2011 (Eurostat, 2011). There are, of course, various reasons for this undoubtedly remarkable achievement, but one of the most important ones is a steady export increase

among Latvian companies. Namely, in 2010 Latvian exports increased by almost 30% as compared to the previous year, approximately 70% going to EU countries. The most important commodity groups of Latvian exports are wood and wood products (19.3% in 2010), followed by metal products, machinery and mechanical appliances as well as electrical equipment (LIAA, 2011<sup>11</sup>).

Furthermore, contrary to the years before the crisis, from 2010 onwards more rapid growth of the industrial sector, not the service sector, can also be observed in Latvia<sup>12</sup>. This can be seen as a positive trend, not least since most of the current hidden champions in Latvia represent the industrial sector, focusing on producing high value added, innovative products that often require technical skills. In many cases such technical skills and knowledge, as demonstrated by owner-managers of Latvian companies – and not at all easy for their rivals to imitate – is still a heritage from ‘Soviet times’.

Continuing on the positive note, being a relatively small country – and only 20 years after escaping the Soviet regime – Latvia can still be proud of having internationally successful companies. In this context, following H. Simon’s (2009) classification, one can distinguish between (1) real hidden champions – companies such as Aerodium and Blue Microphones that have already achieved remarkable success in the international arena, (2) potential hidden champions, such as MADARA Cosmetics and Aboards, i.e. companies that show clear potential to become leaders in their respective market niches and (3) start-ups with potential for considerable growth, such as Mammu, a company that seem to be on its way to remarkable success. The main characteristics of all these companies are summarized in Exhibit 2.

In order to identify the key drivers of their success, in the following sections of the paper real hidden champions – Aerodium and Blue Microphones – are explored in more depth. These sections are then followed by a brief introduction to the potential hidden champions of Latvia – Madara Cosmetics and Aboards – as well as a start-up with growth potential, Mammu. In the concluding section, the main similarities and differences of Latvian success stories, as compared to their counterparts from the rest of the world, are summarized.

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<sup>11</sup> [http://www.liaa.gov.lv/eng/trade\\_with\\_latvia/foreign\\_trade\\_statistics/](http://www.liaa.gov.lv/eng/trade_with_latvia/foreign_trade_statistics/)

<sup>12</sup> <http://balticexport.com/?article=latvijas-ekonomika&lang=lv>

**Exhibit 2: Latvian Hidden Champions:**

Name	Market leadership definition	Revenues 2010 (in M €)	Revenues 2000 (in M €)	Average employees 2010
<b>Aerodium</b>	Pioneers in developing vertical wind tunnel technology that suits wider market needs. Among the world leaders in the respective industry through combining technological expertise, promotional activities and customer service among other things.	5,1	n/a <sup>13</sup>	100
<b>Blue Microphones</b>	Producer of high quality microphones for the mass market. One of the leaders in the U.S. market and often perceived as the 'Mercedes' of microphones.	10	0.07	45
<b>MADARA Cosmetics</b>	Leader in the cosmetics market in Latvia. Emerging leader in the eco-cosmetics market niche in Europe.	2.1	n/a	40
<b>Aboards</b>	Producer of high quality kite boards and kite boarding equipment. Through successful distribution and focus on high quality products the company has established a strong position in a very noisy market full of rivals.	0.25	n/a	5
<b>Mammu</b>	Young start-up, social business aimed at creating a major social movement around the world.	0.02	n/a	6

Source: Author

## 2. Aerodium

### 2.1. From idea to business start-up

The idea to launch Aerodium came incidentally, when Ivars Beitans's attention was caught by devices called 'vertical wind tunnels'. As the head of the Latvian Bungee Jumping Association and a stuntman as well as passionate traveller, Ivars simply could not resist trying them out himself. His technical background made him think that the flying experience, which he ultimately enjoyed in various countries could be brought to a new level, mainly by improving the technology of the wind tunnels. Knowing that even the best product requires substantial marketing and promotion, Ivars contacted Ansis Egle, who was a sports enthusiast, and had experience in marketing and promotional activities.

By the end of 2004, when the discussion between Ivars and Ansis took place, Aerodium Ltd. had already been registered in the company register and the first wind tunnel had been delivered to Riga. "When we entered the market at the end of 2004, we entered an industry which had already existed for 25 years: since the day the French-Canadian inventor Jean St. Germain created the first recreational vertical wind tunnel in Montreal, Canada", says Ansis Egle. Similarly to the industry, the first wind tunnel as well as the name of the Latvian company came from Canada-Aerodium Canada, a company with an established name and reputation in the world market.

As explained by Ansis: "As in the PC industry when PC technology was only developing, in this industry it is common to buy a ready-made product from a supplier as 'raw material', and then invest know-how to create your own product." The initial product Aerodium bought from

<sup>13</sup> Here and further in Exhibit 2 'n/a' means that company did not yet exist back in 2000.

Aerodium Canada was indeed nothing more than ‘raw material’ “If Aerodium Canada had dared to sell the wind tunnel in the quality in which it was delivered to us, say in a sensitive market like Russia, they would have been in trouble. The device simply did not work as it should have; actually, it did not work at all!” explains Ansis. Luckily for Aerodium, it was typical for the industry that products did not deliver their promised value. Thus, since the very beginning of their business, Aerodium was simply pushed to identify problems and look for technological solutions. “We took this very seriously and started with basic things: aerodynamics and construction. Ivars Beitans’s technical knowledge was and still is invaluable in this regard: he is the inventor of most of the technologies invested in our products!”

## **2.2. Entering the global arena in the first years of operation**

“Only a few months later, after arriving from Canada, the wind tunnel looked completely different,” says Ansis Egle. Indeed, technological investment paid off, and following the advertising campaign, the success of launching the wind tunnel in Latvia surpassed all the expectations of the Aerodium team. “In the summer of 2005 there was a queue of people waiting from early in the morning until midnight every day for an opportunity to fly: these were customers not only from Latvia, but also from neighbouring countries such as Lithuania, Estonia, Sweden, and Finland. The demand was simply huge!” remembers Ansis, explaining that this wind tunnel was the first of its kind in Eastern Europe; thus, Aerodium could enjoy the first mover’s advantage to the full extent.

Achieving a fast success in the region, Aerodium was looking for possibilities to enter global markets, and “the difference in this regard was made in 2006, when Aerodium won the tender for the Winter Olympics in Torino, Italy.” Aerodium’s show at the Torino Olympic Games was a big success and attracted lots of attention: “During the closing ceremony, live TV coverage reached 500 million viewers worldwide who saw that flying was possible,” says Ansis, emphasizing that “it was indeed a turning point not only for Aerodium but the whole industry as nobody had ever had the idea to put a vertical wind tunnel in an entertainment show, and nobody had ever carried out such a performance publicly.”

Impressed by the show, many companies tried to enter the market. According to Ansis, “It was like an explosion which lasted for some 2 years and then faded away. The reason for this is that companies simply took this thing too easy: it only looks like all you need is an engine and propeller to make people fly. Actually, huge know-how is required to ensure successful operation of the device, and lots of technological solutions and also patience are required of the producers.” Indeed, none of the companies which emerged as a result of the show in Torino were still active after 2008. One of the takeaways from this experience thus seems to be that in case technology or anything else that brings value added to the product or service is relatively easy to replicate, exposing oneself to a wider audience is indeed risky and will most probably attract too many rivals already in the early phase of the business start-up. As demonstrated

by Aerodium, however, introducing a product that is very hard to imitate – due to unique knowledge, substantial financial investments and time – can allow a company to target wider market segments more openly and help it to establish a solid foundation for long term success.

### **2.3. Our formula for success: strategy through innovation in everything we do**

The key to the Aerodium strategy is innovation, especially when it comes to technological development of the wind tunnels. To be precise, approximately 30% of the profits are invested back in R&D, which has resulted in a number of patents. As emphasized by Ansis Egle, “We are innovating in order to create demand for Aerodium products on the world market, and, in our business, this is only possible if you have better technology than your competitors. Technology-wise we are indeed very ambitious: if there is an opportunity, we do everything it takes to take advantage of it.”

Innovation in technology has led to another competitive advantage for the company: a diversified product range. As Ansis puts it: “If our competitors are fine with producing the wind tunnel, setting it up and collecting money, then we want to achieve much more than that. Our strategy is market expansion through segmentation, offering the right product for each market segment.” And how do they do that? After Torino the company realized that big shows also involve big investments, which leads to a high price for the customer. Thus, Ivars Beitans thought about ways to optimize the cost structure while at the same time serving customers who cannot access or afford the flying experience in big tunnels. Ultimately, he came up with the idea of the ‘mini-tunnel’.

Apart from the mini-tunnel Aerodium also has other types of tunnels, each of them designed for a specific target market. As Ansis explains, in general, the company’s revenue stream rests on three market segments. The first are customers who usually buy only once, such as military forces. These are the markets in Pakistan, Saudi Arabia, also Malaysia, Korea, India and Greece. The second segment is show business, and we are very active in participating in various show business events around the world. The third segment is comprised of people who would simply like to enjoy the flying experience. For this we have tunnels in Latvia, Denmark, Bulgaria and other countries.” Thus, so far it seems that combining technological innovation with clever market segmentation at the same time as providing a diversified product range is a business model that has brought success to Aerodium and is perhaps also worthy of consideration by other growth oriented companies.

“Indeed, diversity of products, technological know-how and market segmentation are three elements which form the success formula in our industry: the formula for our happiness,” confirms Ansis. The other two are customers’ trust of our brand and globalization strategy. To gain trust, at the very beginning of their business operation the company owners were wise enough to establish a network with Aerodium Canada. “With improved technology, we soon

started to outperformed Aerodium Canada and they simply offered to sell Aerodium Canada to Aerodium”, explains Ansis. When it comes to entering global markets, Aerodium has realized that the best strategy for penetrating new markets is forming partnerships with local companies. “Yes, we share our technology and success, but this allows us to understand the market better. And it is much better than having risk capitalists on your neck who have unlimited control of your business,” says Ansis. “Furthermore, it is clear that we simply cannot enter the market, set up the technology and operate it from a distance.”

“Our customers say that one of the things they really like about Aerodium is the service we provide, and this is yet another determinant of our success,” emphasizes Ansis Egle. There are many ways in which Aerodium makes sure that every customer feels satisfied with their first flying experience. For instance, Aerodium records customers’ flying experiences and delivers a CD to help strengthen the memory and enable customers to share their experiences with others. “This is the only way in which we manage to increase value added to the customer, at the same time making sure that these customers do some marketing for us: this involves relatively low costs and generates great returns,” explains Ansis. Thus, Aerodium demonstrates that customer satisfaction lies not only in providing an invaluable experience, which in this case is not doable without involving high technology. In addition, creating customer satisfaction and thus loyalty by further extending this memorable, emotionally rich experience also plays a significant role. To illustrate this further, an example from a restaurant business would be serving free, good quality coffee after an unforgettable lunch that has taken the chef hours to prepare; after all, these are all small, often unexpected ‘pleasures’ people in general value and remember most.

One way to provide the best value for both existing and new customers is, of course, also by delivering the right product and service in the right place at the right time. And this is not achievable without good relationships with suppliers. However, managing relationships with suppliers is not an easy task due to the specifics of the product. “We can hardly find two wind tunnels that are the same; usually each tunnel has its own modification. This means that each tunnel requires new drawings and the technology changes to a greater or lesser degree: in a word, we constantly work with something which is new and has never been produced. For this, we also constantly need to look for new suppliers who can provide the best solutions for each case,” explains Ansis, adding that being aware of what competitors do is also very crucial at this stage.

Aerodium’s chief competitor is the Florida-based firm Sky Venture, an experienced company working in the market since the beginning of the 90s and currently dominating the North America market. Having some 50% of the market share in Europe, Aerodium also has several competitors in Switzerland and Germany. “Then we had L1 in the US, but they disappeared... All in all, the good news is that our competitors have recently started to seek out contact with us, and in our opinion this only indicates how strong we are,” explains Ansis.

“You can have great suppliers and the best knowledge about the competitors, but in the end it is the employees who drive your business and underestimating this factor is the biggest sin any company can commit,” emphasizes Ansis. And how do they find the best employees? “Well, they are the ones with a spark in their eyes. This is true for the owners of the company, and the selection of employees is primarily based on their motivation and willingness to achieve something together with us. Employees of Aerodium are very much aware that this is a unique product they are working on and our common aim is leadership in the world market. Routine? This is hardly possible in our business as things constantly change just as our products change,” adds Ansis, confirming findings from previous research that creating the unquestionable commitment of employees that are passionate for the product they deliver is indeed crucial for success on the global level (i.e. Chaston, 2010).

## 2.4. What next?

In a relatively short period of time Aerodium has grown both financially and employment-wise. As for today, the company employs people at their branches in Bulgaria, Libya, Denmark and other countries, overall having the equivalent of some 100 full-time employees around the world. Financially, regardless of the financial crisis, Aerodium’s turnover increased by 28% in 2010 as compared to 2009, and with constant improvements in technology as well as promotional activities, the company continues to grow.

The company also has a clear idea of how to maintain and increase their market position: “We are looking in the direction of Asian and North American markets,” says Ansis Egle, highlighting that there are various activities, such as cooperation with Shaolin monks in China, which are being implemented. “In general, we keep our eyes open and try to take advantage of any opportunity which could help us to further penetrate the global arena,” says Ansis, demonstrating a clear pattern of proactive leadership in Aerodium, sensitive to opportunities and quick to adapt to them. Indeed, Aerodium is not planning to stop, and this is reflected in their vision: to create a worldwide movement consisting of enthusiasts who love to fly. “Trust me, the flying experience is a unique feeling and we can offer such a feeling while guaranteeing safety. This means that flying actually qualifies as a sports activity, with championships for amateurs and professionals. If we achieve this in 5-10 years, I will be happy,” concludes Ansis Egle, leaving us with the impression that Aerodium intends to continue flying globally... and high, despite the challenges that are very likely to be faced while attempting to take advantage of further market opportunities.

## 3. Blue Microphones

### 3.1. From hobby to opportunity recognition

Martins Saulespurenis, the founder of Blue Microphones, has always been interested in music and technology. Still, his passion for music came first, long before Martins graduated university as an engineer and started to work for Academy of Music of Latvia as a director of sound recording studio. “Jazz music was of particular interest to me, but this was the 50s and 60s in Latvia, and access to any jazz records in the Soviet Union was highly restricted.” Thus, searching for jazz records, he decided to send a letter to a journal in England, expressing his eagerness to find people who would be interested in exchanging jazz records. As Martins remembers, “At that time not too many people dared to do such things as any contact with the rest of the world was seen as a threat to the Soviet regime.”

The next step towards launching his own business was Martins’ first visit to the US back in 1988, just after the ‘Iron Curtain’ fell and travelling outside the USSR was possible. During his stay in the US, one of his pen pals introduced him to a teacher who was very interested in Latvian music. According to Martins: “This person made a very interesting offer, asking whether my son would be interested in coming to the US to study. To educate his son in the US, Martins had to cover certain expenses; thus, he started to think seriously about how to make money.

“During the Soviet era the main film studios were all equipped with relatively good microphones, mainly of Austrian origin,” explains Martins, adding that he was lucky to get free access to microphones which were damaged or simply worn and thus considered to be of no value. “This is where I could use all my technical knowledge, attempting to reconstruct them and then sell outside Latvia.” Martins managed to sell some of those reconstructed microphones during his first visit to the US: “This turned out to be quite successful, as my first deal in the US was worth about 6000 USD. Thus, not only did I realize that the ‘old junk’ I had access to, if properly reconstructed, had a value. This also helped me to raise some start-up capital both for my son’s education in the US and for my further business activities.”

### 3.2. Launching and development of Blue Microphones

Blue Microphones was established in May, 1995, and registered across the ocean, in the US. As Martin explains, “I was never really interested in launching a business in Latvia, in particular during the times when the environment was very harsh there”, thus demonstrating that in case business opportunities for a particular business are hard or impossible to realize in one region of the world, this not a reason to stop implementing them elsewhere. Already in the autumn of 1995, Blue Microphones was presented at one of the foremost US exhibitions dealing with sound and technology, leading to very important new contacts and generating sales. In the beginning Martins was the only owner of the company; however, he cooperated closely

with Bernard Wise, better known as Skipper: “He was a professional musician I had known for several years already, and he was busy making music. Skipper was of particular help in the very first years of Blue Microphones’ operations, as he was able to bring in new customers and helped in many other ways,” says Martins. It is no surprise that when Skipper’s contract with his former employer JVC expired in 1998, he formally joined Blue Microphones.

During the first two years of operations Blue Microphones’ main products were reconstructed microphones. However, this changed in 1997, when one of the leading recording studios in the US ordered the same microphone they had bought previously. “Well, we did not have this type of microphone for reconstruction and it was indeed impossible to get it anywhere soon,” remembers Martins, adding that “since it was an expensive microphone, to keep the customer, we literally had no choice but to follow their advice to produce the microphone ourselves.” Overall, with the production of microphones Blue Microphones’ sales amounts also increased substantially. For instance, the annual turnover of the company was around 40 000 USD in 1996, reaching 10 million USD in 2009 and 14 million USD (approximately 10 million EUR) in 2010.

Still, Martins emphasizes the importance of the decision to produce the first microphone, which, using his words, “happened almost by accident, but shaped the whole strategy of Blue Microphones.” According to Martins: “Entering the market with the most expensive microphone – this was the main reason for our success. In fact, the first microphone we produced is still the most expensive one in our product range, costing some 5000 USD per piece. If we compare ourselves with, for instance, the automobile industry, we positioned ourselves as ‘the Mercedes of microphones’ in the market. This means high value added, high prestige and also a high price for our product and brand in general.” Furthermore, one lesson to be learned from the further success as brought on by this decision is that sometimes positioning a product in, for instance, a certain price category or distinctive market segment – overall not appealing to competitors – might provide enough of a time gap to establish oneself in this market before, following success, imitations from rivals appear.

Indeed, this strategy helped Blue Microphones not only to get established but also to maintain a good position in the market. That is, soon many companies had appeared on the market and they were trying to copy Blue Microphones, mainly with made-in-China products that had a much lower price. “Well,” says Martins, “this was not a problem for us as the value added and prestige which came with using Blue Microphones was more important than simply a lower price.” The reliability of the Blue Microphones brand name would not, of course, have been possible without innovation and investment in R&D. “In this regard, both my own and Bernard Wise’s knowledge was very helpful,” says Martins. Being a musician, Skipper knew exactly what sound engineers require, and Martins knew how to implement these requirements technology-wise. They also soon realized that in order to be successful it is important to diversify the product range, and this, as for many hidden champions around the world (i.e. Simon, 2009), became another cornerstone of Blue Microphones’ strategy.

The diversification strategy was to design each microphone for a specific use. “For instance, we offered microphones which are best for female voices, while other microphones were designed for a lower voice; then there were microphones for drums, different kinds of guitars or any other particular instrument,” explains Martins. Overall, the way Blue Microphones diversified products was very innovative in this market, as at that time most of the major producers were trying to offer ‘universal microphones.’ Martins explains: “Using a ‘universal microphone’ meant that, when recording music, sound engineers had to adjust the ‘upper’ and ‘lower’ levels of the sound in order to emphasize a voice or instrument. One of our innovations in the market was microphones which did all that with built-in technology: without interruption from sound engineers – and engineers like this a lot!” It is thus only logical to conclude that knowing the core users of your product and what the users’ task-related problems are, at the same time being able to solve these problems, seems to be one of the keys to attracting and retaining loyal customers – something that is crucial for virtually any business.

Networking is another success determinant of Blue Microphones, and in this light, Martins emphasizes the importance of personal contacts, especially when it comes to the distribution of Blue Microphones products. As Martins explains: “When I made my first visit to the US in the late 1980s, there were many small shops selling music equipment – just like grocers today. This, however, soon changed, with big distribution chains starting to enter the market.” As Martins remembers: “Guitar Center, one of the biggest distribution chains specializing in records and musical instruments, opened its doors just a few blocks away from where I lived. I was lucky to meet with one of the managers of this centre, and we soon found a common language, which in turn opened doors for Blue Microphones at Guitar Center.” Indeed, in this industry it was very unusual for a retail chain to work directly with a manufacturer, especially a small manufacturer. Today, however, Blue Microphones are among the 3 best-selling microphone brands at Guitar Centers all over the US.

With their products on offer at Guitar Center, Blue Microphones had much better chances of moving their products at other major chains as well. This turned out to be crucial for their business, as small shops that specialized in records and musical instruments soon disappeared from the market. “Today, there are some 3-4 big chains which dominate the entire US market in this industry, and we are present in most of them, which, of course is a huge competitive advantage,” says Martins. The way products were distributed, however, was only one of the major changes that occurred in the industry. There was another change which in fact required a change in the initial Blue Microphones strategy.

In the early years, the company’s main target audience was professional studios: an obvious choice for a company offering high quality microphones starting at 1000 USD a piece. Changes in the market, however, were brought about by new developments in IT, more specifically, the possibility to record in digital format. Martins explains: “Previously most musicians used the services of big recording studios because they could not afford their own. With the development of technology, creating a recording studio which would have previously required the investment

of half a million USD was now achievable with some 40,000 USD or less.” This had important implications for Blue Microphones, as accordingly, there was simply no serious market for very expensive products.

Blue Microphones found a simple and very effective solution for this market change: “Now,” says Martins, “customers could finally buy ‘the Mercedes of microphones’ for a lower price while still benefiting from the brand ‘Blue Microphones.’ And many really appreciated this!” The first Blue microphone for the mass market was produced in Latvia, but the company could not proceed with this strategy as production costs were simply too high. “It turned out that we had to sell the microphone for 99 USD, and the only way to ensure such a price is to produce microphones in China,” explains Martins. Once Blue Microphones managed to reach the 99 USD selling price, the sales of their first mass market microphone progressed very quickly. In fact, not only did the company manage to sell about 100,000 of these microphones, they were also able to remain on the market with the same microphone for more than 5 years: this is indeed a unique achievement considering how quickly IT-related products fade! Arguably, however, all this would have hardly been possible if Blue Microphones had not managed to reach the economies of scale prior to the competition shifting from emphasis on quality to emphasis on price – another takeaway from this remarkable experience for growth-oriented businesses.

Regardless of the relatively cheap price, Blue Microphones still positioned themselves as a value added brand, which in turn required investments in R&D. According to Martins, “The best strategy is to become even better, and this is what Blue Microphones is continuously trying to achieve. All our microphones, regardless of their price, have some unique features, and this is how we maintain the reputation of our brand name even while selling at lower prices. Investment in R&D is simply a prerequisite for growth,” he continues, “as, with digital microphones, we have become part of the IT industry, which indeed develops very quickly. Innovations in the production of microphones are also driven by demand from the market, which is in turn influenced by the introduction of new technologies in related fields. This is like a never ending circle, and we cannot afford to not be part of it,” he concludes, once again emphasizing the crucial importance of being alert to all market opportunities (e.g. Simon, 2009), including those created by major changes in the market place, such as change in distribution patterns or pricing, or change in the industry as a whole as a result of new technology.

### **3.3. Moving forward in a different capacity**

Martins and his business partner sold Blue Microphones to Transom Capital Group in April 2008. Martins is now chief engineer, responsible for the final products and having only a small share, but his business partner is president of Blue Microphones. “Because of this, we cannot talk about Blue Microphones as our company anymore,” says Martins. “Still, the company is moving forward and we are happy to be part of it.”

“Speaking of further development, it is, of course, important to know what our competitors are doing in the market,” continues Martins, admitting that Blue Microphones has always had difficulty entering the European market. Two leading companies completely dominate this market: AKG from Austria and Neumann from Germany. According to Martins, customers’ loyalty to these brands in Europe makes entry into Europe “more than simply complicated.” Partly because of this, Blue Microphones’ principal market since the day the company was established has been the US: even today, approximately 4/5 of Blue Microphones’ sales are in the US, where company has some 80% market share in segments, such as USB microphones. Having a turnover of more than 10 million USD, Blue Microphones employs some 45 employees, which indeed says a lot about the efficiency of the company.

Overall, and in many ways due to the ability of Blue Microphones to achieve economy of scale in previous years, during the last two years the company’s growth has been based on mass market products, including microphones for mobile phones, stage microphones and the like. Partly because of this, Blue Microphones’ product promotion strategy has also experienced some changes in recent years. The company no longer uses advertisements in mass media, instead focusing on gaining market visibility through musicians, TV shows, movies and books. “For instance, Blue Microphones offers young musicians the opportunity to buy its microphones for a considerably cheaper price, Blue Microphones products can be seen in movies such as ‘Star Trek’, and leading TV shows in the US, such as ‘American Idol’, are using our microphones,” explains Martins. Blue Microphones is also making extensive use of PR tools, keeping in touch with journal editors writing on technological development in the music industry.

“What happens with Blue Microphones in the future will not really depend much on me or my business partner,” continues Martins, pointing out that strategy decisions are now made by the new owners of the firm. “And this, of course, is the way it should actually be,” he adds. “Innovations in technology, product diversification, a good network with suppliers and distributors and the passion of the people working for Blue Microphones has been, and most probably will remain, the main determinants of its “success formula”, says Martins, concluding that “these are the reasons why Blue Microphones has never had any ‘bad years’ and only experienced growth – since the very beginning, when it first entered the market.”

## **4. Potential hidden champions**

### **4.1. MADARA Cosmetics**

MADARA Cosmetics Ltd. was established in 2006 as a high-quality ecological skin care brand targeting the high price segment. The company is a good example of a business founded in the highly competitive cosmetics market, yet able to successfully establish itself in a market niche, focusing on green/eco products. In a relatively short period of time MADARA Cosmetics managed to enter more than 30 markets and achieved remarkable financial growth indicators.

That is, with a sales turnover of 170 000 EUR in 2007 and 550 000 EUR in 2008, the company reached 2.1 million EUR in 2010 and is expecting an increase of 60% in 2011.

According to the owner and CEO of the MADARA Cosmetics, Lotte Tisenkopfa-Iltnerē, several factors are keys to this success. First the 'green lifestyle' of the owners set a high quality standard for the products MADARA cosmetics offers, as "we not only produce for customers but also use all the products ourselves." Spotting the high and growing demand for eco cosmetics in Europe, Japan and Malaysia, and entering these markets quickly, with the help of an investor and an established network of local distributors, each of them responsible for a certain market – these are other factors that contributed to the fast growth of the company and a possible takeaway for other growth-oriented SMEs hoping to enter new markets with limited financial resources. The CEO also emphasizes the importance of human capital, namely the professionalism of the MADARA Cosmetics team, as well as constant innovation in products and product design in achieving its success. Overall, MADARA Cosmetics is among the select few Latvian companies which are on their way to becoming leaders in their market niche. This is their aim at least: to be one of the 3 top-of-mind brands in Europe in 20 years in the field of eco cosmetics.

#### **4.2. Aboards**

Aboards Ltd. was established in 2006 and specializes in producing good quality kiteboards and kiteboarding equipment in a high price segment. In just 4 years' time Aboards has achieved remarkable success: though partaking in a very competitive market the company has acquired some 5% of the world market share. According to the CEO and owner of Aboards, Kriss Spulis, there have been several key success determinants for the company. First, the company's early export orientation was crucial. Today, with the help of local dealers who are in turn responsible for developing the brand in the respective region, and mainly using the B2B approach, the company exports over 90% of its production to more than 30 countries on 5 continents. Not only the distribution but also the manufacturing process is globalized; that is, the firm has manufacturing sites in various countries in Europe, Asia and beyond. Further keys to success have been constant innovation, the owner's competence in technology, a clever marketing strategy on an international level, quality control and logistics. Finally, regular and hard work is highlighted as a factor which has enabled the company to grow quickly: "To go a long way you need to keep on taking small steps," explains the CEO of Aboards, pointing out that, taking small steps, the company is aiming to go as far as possible.

## 5. Start-up with potential for considerable growth: MAMMU

There are also Latvian companies which are just emerging, but clearly demonstrate the potential to become market leaders in their niche. One such company is MAMMU. Founded in 2010, MAMMU is a social business which is already a best-case example for the creative think tank Grameen Creative Lab of Dr. Yunus, who promotes the MAMMU business model worldwide at all major social business events. According to the co-owner of MAMMU, Fionn Dobbin, “The key idea for MAMMU is to support mothers in need by giving them a chance to earn money.” With the help of top designers and photographers, mothers in need are involved in manufacturing fashionable scarves – MAMMU’s chief product – using green materials. Though only recently established, MAMMU is on its way to becoming a social movement around the world. Currently the company exports its scarves to the US, France, Germany, Denmark, the UK and Luxembourg, with a foundation laid for entry into many other countries worldwide.

## 6. Latvian Hidden Champions vs. a stylized hidden champion company

Being among the best in their industry, hidden champions are growth-oriented, highly ambitious firms aimed at market leadership and even having market leadership as an identifying characteristic (Simon, 2009). Similarly to, for instance, MADARA Cosmetics and MAMMU, these companies are never shy about announcing their aims and ambitions even when relatively young and small. Furthermore, according to Simon (2009), hidden champions are oriented towards the long term and possess a clear vision and ‘inner flame’. They are also able to pass on this ‘inner flame’ to others. And this holds true not only for employees who, sharing common values, are often as enthusiastic about reaching the company targets as the owners themselves, but also for customers. Apart from being growth-orientated, the ability to achieve constant, fast and long term growth, even in mature markets or industries, is a factor that distinguishes hidden champions from firms that ‘merely’ grow quickly, and it is certainly a prerequisite for moving from the ‘hidden champion’ to the ‘big champion’ category (Simon, 2009).

In explaining the growth drivers of hidden champions, Simon (2009) emphasizes globalization and innovation as being of crucial importance. Through innovation, these companies manage to create their own markets or demand for their often high-tech products. Thus not only innovation per se but also the ability to market the innovation is considered to be of major importance. Furthermore, product diversification as a strategy enabling the growth and further penetration of international markets has been highlighted as a very important characteristic of hidden champions. In this context, technical knowledge, often on the part of the firms’ owners, plays a very important role, and neither Aerodium nor Blue Microphones are exceptions with regard to all the previously mentioned ‘general characteristics’ of hidden champions.

Also, the way in which Aerodium and Blue Microphones bring innovations to global markets corresponds to the 'general' strategies of hidden champions. Namely, a key to success in internationalization efforts is maintaining a close relationship with every market, mainly using the knowledge of local people, who are often distributors or other cooperation partners (Simon, 2009). The main reason behind the importance of close relationships with markets is, of course, the ability to handle issues related to mentality, legislation and other specifics of the particular markets. Such relationships are, however, also crucial when it comes to providing high quality and timely service to the customer, as demonstrated by the case of Aerodium.

Hidden champions are very focus-oriented companies which specialize in their particular market niche or business activity, going 'deep, not broad' (Simon, 2009). In the case of Blue Microphones and Aerodium, not to mention Aboards, narrow focus does not, however, mean 'putting all your eggs in one basket'. Even though they are focused, these companies have managed to diversify their product range to the extent that they are no longer dependent on a single product or market. All in all, similarly to Aerodium and Blue Microphones, hidden champions concentrate on what they do best, often outsourcing other activities, thus becoming as efficient as possible (Simon, 1999). Furthermore, confirming findings of previous studies (see Chaston, 2010 for a review), all cases from Latvia also demonstrate the very great importance of the role of owner managers. Namely, it is their lifestyle, interests and hobbies, and even more importantly, specific knowledge, that has helped them to launch innovative products and also sustain a competitive advantage in the respective market niche.

Also pricing and human resource management strategies of both Latvian hidden champions and most regional leaders – along with the influential personalities of their owners – seem to be very much in line with what is thought to characterise hidden champions from other countries. Furthermore, like most hidden champions around the world Latvians handle their success strategies with discretion. Thus, it would not be surprising if there were other success factors or strategies, or perhaps a particular combination of these, which have not only brought Latvian hidden champions to where they are now but will also enable their future success.

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