

Merck: A Family Success Story

Past Issues Apr-Jun 2011 Family Business Face to Face
Published on May-08-2011

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Ajay Bhalla, Professor of Global Innovation Management at Cass Business School in London and Associate Faculty, Thomas Schmidheiny Chair of Family Business and Wealth Management, Indian School of Business (ISB) talks with Dr Frank Stangenberg – Haverkamp, Chairman, Board of Partners, E Merck KG, Germany on challenges that family businesses face in sustaining the family and business as two separate institutions and how they can overcome them.

Ajay Bhalla: Sustainability of family and business are twin pedals to measure success in family business. Merck is not only the world's oldest pharmaceutical firm with a turnover of Euro 7.9 billion, it also happens to be a 13th generation family business. How did the family achieve the balance of securing growth in the business while retaining the family ownership over multiple generations?

Dr Frank: There is an inherent need for growth because the family is growing. We are 130 family members within sixty years. So if the business is not growing to support those 130 then you will lose the business and you will lose the family. My parents still had a very high percentage of the business but now of course my kids will only have 1 or 1 1/2 %. So we have to make sure that this 1% is valuable and also gives you as much dividend if you want to take it out as the 8% or 10% or 15%.

You make an interesting point. As families evolve, individual members or branches would like to see their wealth increase with the size of the business. How do you manage this tension at Merck?

You have to do two things. Firstly, you have to make the family attractive, as an institution. It is easy if you live in Darmstadt, where the company is located; we employ more than 10,000 people there, everybody knows us. But, if you live abroad or in Munich, the family doesn't mean anything to them. Secondly, the financial aspect is very important. The wealth has to increase in a way that it is attractive even for small family shareholders. I believe family companies only survive if the economic background is also right.

Let's shift the focus to family governance. It's an important topic, which is vital to aligning within-family and family-business interests in mid-sized and large family firms in India and elsewhere. The family has a convincing voice in the strategic direction of Merck. There have been three key events in the firm: In 1995, the company went public and then two acquisitions followed in 2007 and 2010 respectively. Have there been any other events that tested the family's resolve?

One very important event is the changeover from one generation to the next, whether that goes smoothly or not. That is the acid test. Because, one of the problems in families is that the old generation can't let go. But we were very fortunate. There are always some points of aggravation in every family, but basically we have always managed this transition peacefully. So the family board already has two members of the twelfth generation.

Do you believe that it is important to bring in the next generation early on in the family business?

Well, in case of Merck, they have to finish their university degree and they have to start working on their own profession. But, in their early 30s they are already on the family board. In ten years, this family board should be predominantly manned by the twelfth generation. My generation is 60-70 years and we should be out.

Family firms often disappear after the third generation, but Merck has been going strong at the twelfth generation. Does the tension that the family firm will remain a family firm disappear as the talent pool becomes bigger for the family?

That works only in theory. That is true, the family is bigger but in the end there are very few, who have the necessary skills. Even if you have 130 partners or 220 family members you don't suddenly have 30 people to choose from. There will only be three or four really top quality people who can take on a leading role.

Nurturing talent within the family is vital. However, the question arises if they should do this within the family firm or outside the family firm. Do you facilitate or allow family members to choose their own professions?

They have, they do. There is a German saying that the first generation built the business up, the second maintains it and the third wastes it. You know the same applies to India. So once you overcome this, then it gets much easier but you always have to find people who are willing to dedicate their business life at the end with all the consequences to it. I will give you an example of two family members. One works for another pharmaceutical company and the other works for a large German family business. He is a qualified chartered accountant working in the finance section. It is very difficult for them because they are always under pressure to be the best in their company because they want to return to Merck one day. But they can only come to Merck if they make a career on their own. So it is very difficult for them to live with this tension.

Merck listed publicly in 1995 and has subsequently made multiple acquisitions. As you go through major decisions like these, do they put pressure on the family cohesion and longevity?

No, not at all. The Merck family is relatively removed from the operative business and they are always involved in it. They have no automatic say in the big acquisitions. But there is a consultative process, and it is also based on trust. The family simply trusts the family members who work in the business that we will take the right decisions. You need to keep inclusiveness in the family. It is imperative for the people to meet and talk to each other. We try to do that with the big family.

From a family governance perspective, did this formal process evolve as a result of some crisis event? I understand value sets exist in any family business but how did the family governance process such as the democratic board, the partner election and the vetting process evolve?

Don't forget the company is very old. The first family contract was done in 1882 or '83. Until then, women could not inherit assets of the company. But then our forefathers decided that they wanted women to have a share. Then the first family contract was drafted. This contract developed step by step up to where it is today. Today, it is about 150 pages and it is like a law. There is a family contract based on it. Everything evolved out of this. Of course, the values have always been inherent. But the whole value discussion came about 15-20 years ago. Then of course, we have got values. We are living on a set of values, trust, integrity, etc.

What role does education play in ensuring that a broader pool of family members is aware of family governance mechanisms and how they are implemented in practice?

Yes, you have to educate them all the time. That is the reason why we have at least one meeting a year with the youngsters, two meetings of two different age groups and the AGMs – to educate them on these things. Typically, the next session will be in March. In the morning, they will be introduced to our research laboratories that do basic research. In the afternoon, they will look at some laboratory equipment that do basic research there will be a session on this. There will also be a session on family contracts, family values, business structure, P&L accounts and on how to read a balance sheet.

What you described is vital in terms of keeping that attachment to the family but that held just once a year. Is there anything else that can build the attachment within family and to Merck as a family business?

No, it is more that, because we have got the AGM, then we always have a second general meeting for the whole family that will take also place in September this year where we discuss changes in our family constitution, or acquisitions. It will not be so formal at the AGM, but it will be a proper meeting and then we have one meeting for those between ages 15 and 21 and then another meeting for those between ages 21 and 30. So, there are three gatherings a year, where the younger generation can participate.

Then of course, there are private events. There is one family member who lives in Switzerland, so we have a ski weekend there. For the whole week we meet at the hotel – you have to book it yourself and pay it yourself. There would be 40-50 family members coming there.

It is very crucial for the family to retain its identity. So, who is responsible for championing this in your family?

It was not a single person. It was the family board because this board deals with family matters. This board was created when we went public. Before that we did not have the family board. We just had the board of partners.

I wanted to touch on the interface between family and its involvement in Merck operations. You mentioned that family members are not involved in the operational roles. What was the rationale for the decision that family members would actually stay away from operational roles?

Family members wanted to do things by themselves. When I was young, I wanted to do my own thing. But, if you have been away you simply cannot rejoin a pharmaceutical chemical business on an operative level when you are 45 or 48. It is too late. You can't do that because you don't have a holding company, and you have inter-related businesses and operative businesses. That is the reason why I joined at the top level, where you are involved in the strategy and a choice of human resource policy.

It is common in Indian family businesses, where a younger family member does an MBA and then wants to start his or her own business rather than join the existing family business. This is difficult for senior family members who often feel, "What did I build the business for if you are going to start your own business?" Do you associate with such tension in Merck?

This is true. I would always take the view that it is up to you. I am building up this business for my kids. If they want to join, yes, I would always be far more detached. I joined Merck because I enjoyed it.

Is there acceptance in the family that you always have the fallback option of coming to Merck because you were not successful in your own venture or you changed your mind?

No, what we need is specific training. The business we are doing is so highly focused and complex because we have more than 100,000 pharmaceutical chemical products. You should start early in this field.

What would be your message to Asian family businesses, especially how they can build sustainable family and business?

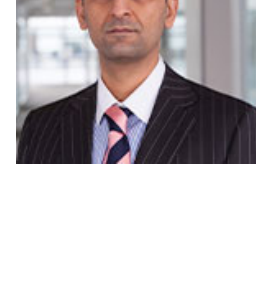
If you look at why Merck has been successful, there are several reasons. Firstly, as a family you need to be modest, very modest, and be an example for other people. Secondly, treat the people who work for you well. We always say in Merck, "You are part of our worldwide family." Even if they are ordinary workers or gardeners or chauffeurs or low-grade workers, treat them all well because cost cutting is not everything. We may not be the most cost effective company, but at least people like working for us and are loyal. Finally, remain competitive. Also, within the family make sure that the changeover from one generation to the next is smooth and that the younger generation is trained to be part of the family and cherish the family business. You have to educate and train them.

About Authors



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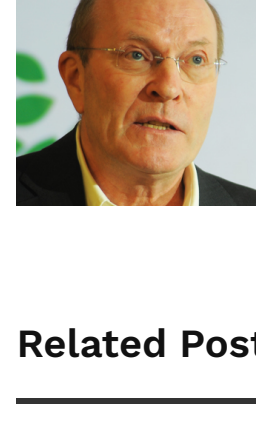
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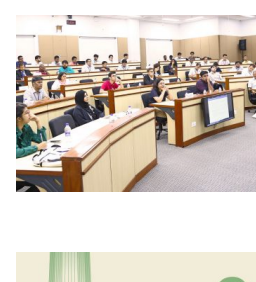
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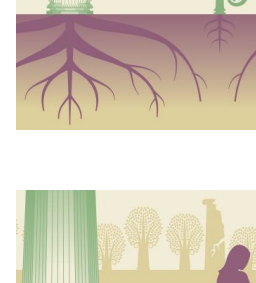
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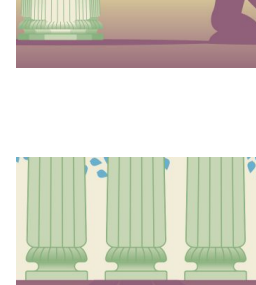
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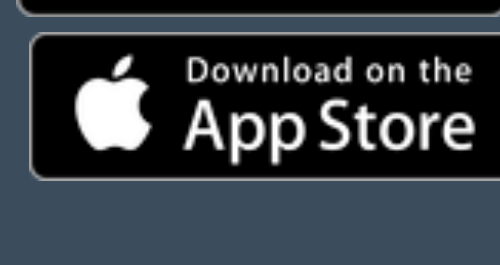
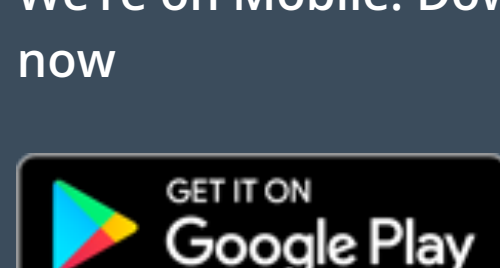
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ISSN: 2582-1180 (Online)
Publisher:
Indian School of Business
Gachibowli, Hyderabad
Telangana - 500 111