

1 The crucial role of key account management

Fast track

For over 15 years, the authors have been researching global best practice in the domain of account management, sponsored by many of the world's leading companies. The following topics in particular have been the focus of our research:

- **Key account selection:** Only a few selected customers can be included in the key account programme.
- **Classification of key accounts:** Derogatory labels like A, B, C, or gold, silver, bronze should be avoided at all cost.
- **Key account profitability:** The power of customers and their increased purchasing power has led to greater demands on the services of their suppliers. Unfortunately, many traditional accounting systems are incapable of accurately capturing all of the associated costs of dealing with major customers. Consequently, many suppliers are acting in ignorance of which customers make or lose them money.
- **Key account needs analysis:** A deep understanding of the customer's business is essential to success.
- **Strategic planning for key accounts:** Just as a three- to five-year strategy is essential for any business, so strategic plans for selected customers, signed off by the customers themselves, are also critical to success.
- **Roles and skills of key account managers:** Selling and negotiation skills are no longer sufficient on their own.
- **Other issues:** Information technology, organization structure and internal marketing all contribute to creating successful key account programmes.

The challenges that all organizations face today are:

- **Market maturity:** In most sectors, mature markets have transferred power from suppliers to customers, as suppliers compete for a share of a decreasing number of customers.

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- **Globalization:** Market maturity has led to an increasing number of industries in which only a handful of truly global companies dominate the landscape. Hence, any supplier who cannot offer a seamless service in every part of the world where the customer operates will not win the business.
- **Customer power:** With their new-found power, customers are increasingly looking to selected suppliers to give them competitive advantage by product and process development.

All these developments mean that suppliers have to be much more stringent in their key account selection criteria. They must allocate their scarce resources intelligently across their customer base, taking account of the risks associated with different kinds of customers in order to build continuous shareholder value added.

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Introduction

Back in 1996, the authors started a research club in Cranfield University School of Management because it was obvious even then that the power had been transferred from suppliers to customers. Customers were exercising their new-found power by dropping suppliers who did not live up to their expectations and by forcing down prices from other suppliers.

This apocryphal story about the buying director of General Motors was never denied: He called his suppliers together in Detroit and announced that they were all to drop their prices by 20 per cent and asked for questions. One brave chief executive officer of a supplying company told the GM buying director that his technology was years ahead of any competitor, was already 20 per cent cheaper than his competitors and that he could not reduce his prices by 20 per cent. The GM buying director asked his commissionaires to escort this supplier out and announced that his company would never deal with GM ever again. He then asked for further questions!

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While no doubt the story has been embellished over the years, you will instantly recognize this particular type of obnoxious bullying buyer and the reality is that you sometimes need to deal with them because of their size. Nonetheless, there is an appropriate way of handling such customers so that the relationship is still profitable and this will be covered in Chapter 7.

The problem back in 1996 was that no business schools anywhere in the world had bothered to do any research into the transfer of power from supplier to customer, so the authors established a research club based in Cranfield with the sole purpose of researching global best practice in the domain of key account management. By 2011, this research club has been going for 15 years and has systematically researched best practice, not just on the supply side, but also on the customer side. This dyadic research approach was essential because, even back in 1996, it was obvious that supplier delusions about customer relationships were rife. Over the intervening years, the following topics have been the focus of our research.

Selecting key accounts

The authors heard a director of a major telecommunications company claim that they had 1000 key accounts! The chief executive of a health care company claimed that they had 200 key accounts.

Such numbers are, of course, totally ridiculous. A moment's thought will reveal that any supplying company has limited capacity to commit cross-functional resources to selected customers. Each of us has hundreds of friends, but we only have capacity to devote real quality time and love to a handful – maybe four or five.

The same principle applies to companies, who must decide extremely carefully which major customers they are prepared to allocate this scarce resource to. This issue is expanded in Chapter 2.

Categorizing key accounts

Even today, the authors hear of suppliers classifying their key accounts using fatuous labels like A, B, C or gold, silver and bronze. Imagine a call centre operator letting it slip that they were dealing with a C or a bronze customer! The mind boggles over such derogatory, supplier-centric labels. A more suitable and customer-friendly type of categorization is provided in Chapter 2.

Key account profitability

Our research reveals that about 85 per cent of Western European companies do not know whether they make or lose money from their biggest customers. They *think* they know, but most do not.

One of the authors used to be marketing and sales director of Canada Dry. Thirty years ago, two major retailers used to each buy about 3 million dozen bottles of ginger ale each year. One of these

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customers insisted on daily, just-in-time, store-by-store delivery, resulting in major stock-holding and delivery problems. They also insisted that the salesforce called daily to carry out merchandizing. Finally, they took about 145 days' credit. The other retailer, taking a similar amount of products, asked for stocks to be delivered centrally to their warehouse for them to carry out their own deliveries. They did not insist on merchandizing and paid their accounts in 45 days. Yet, the accounting system calculated that both customers were equally profitable, as it allocated overhead costs on the basis of volume bought.

We have enjoyed activity-based costing (ABC) for over 20 years, yet most companies still have not learned the lesson that it is the cost of dealing with the customer after the 'product has left the factory' that causes either profit or loss. Even today, most companies still do product profitability and marmalade their fixed costs to customers based on turnover, thus penalizing customers who are inexpensive to service and rewarding customers who are expensive to service.

Most companies still do product profitability and marmalade their fixed costs to customers.

Customer needs analysis

Readers would surely agree that suppliers must really understand the needs of their customers and amend their approach accordingly. Alas, this certainly was not the case back in 1996 and is still largely untrue today. When key account managers are trained to sell volume and are paid accordingly, they have little interest in giving up substantial amounts of time and energy in researching the processes, organizational intricacies, financial details, etc. of their customers. But without such an investment they will never be able to align their offers with their customers' needs.

Strategic planning for key accounts

This latter point is obviously related to the issue of preparing strategic plans for key accounts. The authors were recently running a key account management (KAM) workshop for a blue-chip supplier of expensive equipment for hospitals. On being told that one hospital had a multimillion pound budget for such equipment, we asked about the supplier's strategic plan for this hospital. Alarming, we were told that there was only a one-year forecast and budget. We were reminded of the famous saying that the good thing about not having a strategy is that failure comes as a complete surprise and is not preceded by a long period of worry and depression! Having strategic plans covering a period of at least three years, agreed with the customer, is a major factor in successful and profitable relationships, yet even today little exists beyond supplier-centric forecasts and budgets.

The good thing about not having a strategy is that failure comes as a complete surprise and is not preceded by a long period of worry and depression!

Roles and skills of key account managers

It was surprising to say the least, that little was known in 1996 about the roles and required skill sets of key account managers. Among other things, we supervised a major doctoral thesis on this topic, so we can speak with great authority on what world class key account managers should be doing and what skill sets they require.

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Rewards and performance

This intuitively simple topic becomes extremely complex in the context of the kinds of rewards that are appropriate for success in dealing with different types of key accounts. This is dealt with in Chapter 11.

Transitioning to KAM

The cultural and behavioural issues over time involved in changing from a product- or sales-orientated organization are extremely complex and need to be carefully planned for. This is dealt with in Chapter 13

Other issues

Other areas for our research efforts included the role of IT, organizational structures, measuring KAM effectiveness, communications and cultural issues, all of them covered extensively in this book.

The point we are making is that the material presented in this book is based on 15 years of in-depth research into global best practice KAM and is therefore unlike most other books on the topic, which tend to rely on anecdotal or second-hand evidence for the assertions that are made. This is the reason why we feel comfortable in describing this book as 'the definitive guide for practitioners', as the research club has been sponsored over the years by some of the most famous companies in the world and over 3 million euros have been invested in it.

1.1 Pressures that have led to growth in customer power

1.1.1 Summary of the pressures

The characteristics and techniques of KAM were not extensively explored apart from the need for a dedicated salesforce beyond the 1990s.

As we have indicated in our introductory comments, while sales and marketing strategists have for some time been convinced that effective KAM leads to increased sales, heightened profitability and improved sales productivity, the characteristics and techniques of KAM were not extensively explored, apart from the need for a dedicated salesforce beyond the 1990s. The impetus behind this unprecedented interest in the dynamics and mechanics of KAM comes from an awakening to the need to address changes in both the context and constructs of marketing.

The marketplace today is a different world from that which we knew before and the rules of engagement have evolved significantly. Such rapid and radical transformation warrants attention. For example, most organizations assume that KAM is an approach for the private sector, but over the last five years the public sector has become involved, seeing KAM as an approach to achieving goals independent of commercial interests. Parts of government are key customers for private companies; public sector organizations are also suppliers to private companies; and KAM has been deployed to manage the relationships between entirely public sector organizations too. Any organization, public or private, needs to respond to the constant changes in its environment, and KAM has become a popular and powerful response.

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Case study insight

ECITB: Transitioning to KAM in the public sector

The Electricity and Construction Industry Training Board is tasked with increasing competence within the Engineering Construction Industry, from apprentices through to technicians and managers. Its key customers are companies and contractors who employ trained people, but when the Board decided to embark on KAM, people inside the organization were not even all agreed about who the customers were: the Government, the employers, or the engineers and apprentices. The organization took some time to explore and understand KAM, and came to the conclusion that it was the right way to achieve the change of orientation and approach it wanted.

ECITB appointed three KAM champions as a core team to drive the programme and, after three years, KAM had been implemented, customer satisfaction was up and employee engagement was up. The Board rated the programme as a great success in bridging the gap, not uncommon between public institutions and commercial businesses, which had existed between the organization and many of its customer companies. The next stage on the journey was to increase the number of customers managed through account plans and roll out a CRM system that would follow the new way of working. It had taken some time to win 'hearts and minds' to KAM but progress, initially frustratingly slow, was now accelerating.

With hindsight, we can easily recognize those pressures in the business environment that have led to the ascendancy of KAM as a separate and significant discipline. These pressures were initially identified in a research report published by Cranfield and the Chartered Institute of Marketing entitled *Marketing, the Challenge of Change* (McDonald *et al.*, 1994) and are described in the following sections (Sections 1.1.2–1.1.5).

1.1.2 Rapid change

Time has become a major determinant of competitive advantage. The drive towards lean production systems has increased interdependency in supply chains. Any company that is complacent will be quickly overtaken. Ironically, the shorter the opportunity for success, the more important it becomes for companies to think strategically and for the long term. In so doing, the potential for minimizing the risks inherent in rapidly changing markets through supply chain partnerships is often an attractive option. The symptoms and challenges in responding to rapid change are listed in Table 1.1.

Any company that is complacent will be quickly overtaken.

Managers understand that, for a product or service to be commercially advantageous to the provider, value must be added faster than cost. The concept has been labelled 'lean supply' by purchasing

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Table 1.1
Responding to rapid
change

<i>Symptoms</i>	<i>Challenge</i>
Compressed time horizons	Ability to exploit markets more rapidly
Time-based competition	Process excellence and flexibility
Shorter product lifecycles	More effective new product development
Shorter technology lifecycles	More investment in skills and understanding of applications and technology
Transient customer preferences	Flexibility in approach to markets, accuracy in demand forecasting, and optimization in price setting
Increasingly diverse business area	Cultural sensitivity

professionals. Lean supply involves the study of the entire supply flow from raw materials to consumer as an integrated whole.

In theory, effective supply flow is an absolute. In practice, companies just have to keep applying continuous improvement to be leaner than the competition. Adopting an approach in which the supplier and customer are joint guardians of the value in transit is vital. Examination of the value in transit demands that both the supplier and customer open their 'books' and facilitate two-way assessment in order to optimize performance. There should be no blame and excuses.

Lean supply practice also lends itself to sharing some costs critical to mutual success.

Lean supply practice also lends itself to sharing some costs critical to mutual success. Joint research and development, joint merchandizing, integrated logistic and electronic data interchange (EDI) are just a few examples of the opportunities available for making things happen better, cheaper and faster.

This concept is equally applicable to service industries.

1.1.3 Process refinement

Companies must be flexible, not just to raise customer satisfaction but to avoid waste and loss.

Company activities have shifted away from producing predefined products or services towards having the capability to produce creative solutions for customer requirements. Companies must be flexible, not just to raise customer satisfaction, but to avoid waste and loss. The symptoms and challenges in refining the process are listed in Table 1.2.

The prerequisite for process redesign is access to information across organizational boundaries. Without that exchange of information, no streamlining can be achieved. Buyer-seller partners are increasingly sharing common databases. The obvious example is stock management. If point of sale data is transferred to commonly held databases of stock information, the suppliers of logistics services and goods can

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<i>Symptoms</i>	<i>Challenge</i>
Move to flexible manufacturing and control systems	Project orientation to deal with micro-segmentation
Materials substitution	Means to shift from single transaction focus to the forging of long-term relationships
Developments in technology	More investment in skills to realize innovations (such as microelectronics and the potential of technology robotics)
Concentration on core business	Embrace opportunities for suppliers to run non-core aspects of customer's business
Quality focus	Widespread involvement in quality initiatives
Collaborative working practices	Create greater customer commitment

Table 1.2
Refining the process

make sure that retail outlets are always fully stocked with the fastest moving lines. That enables everybody to make more money through the consumers obtaining what they want when they want it. Buyers and sellers also need to examine their current activities together in order to explore and optimize processes.

The output of process redesign (or re-engineering) should be enhanced customer value. Customers want quality through attention to detail. Any customer wanting to initiate new quality indicators with a supplier is more likely to do so if there is a strong element of trust and partnership. The closeness of customer relationships can be greatly enhanced through collaboration, both across and between organizations. Joint planning initiatives and coordinated working practices can be used to create mutual understanding, benefit and commitment.

The output of process redesign (or re-engineering) should be enhanced customer value.

Our way of depicting how organizations receive goods and services, add value and sell them into their end-user markets is Professor Michael Porter's value chain. Figure 1.1 depicts the standard Porter value chain model for a manufacturing organization and Figure 1.2 depicts a value chain for a service organization.

Within these models, companies will have functional specialists working together, ensuring a consistent and integrated approach to the development of value.

1.1.4 Redefining the marketplace and pleasing the customers

As well as the need to respond to rapid change through the refinement of processes, there is a need to recognize the changing nature of the

A product/market lifecycle is the aggregate sales at a point in time of all goods or services which satisfy the same or similar needs in a market.

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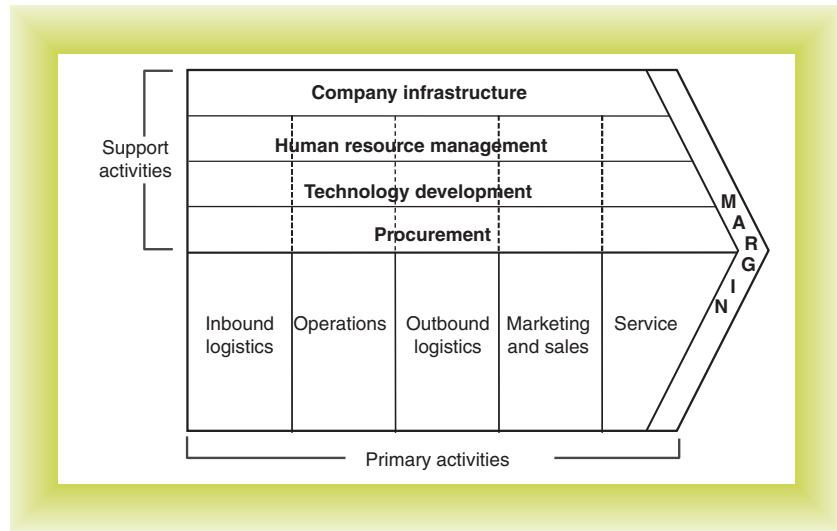


Figure 1.1
The value chain.

marketplace itself (Table 1.3). Many markets today are mature. For example, most people in Western Europe have cars, washing machines, dishwashers, televisions, calculators and so on, so competitors in these replacement markets need to innovate and to look elsewhere for growth.

Market maturity

Figure 1.3 illustrates the impact of market maturity on the key elements of business management. A product/market lifecycle is the aggregate sales at a point in time of all goods or services which satisfy the same or similar needs in a market. The final column clearly

							Reducing cost	Creating value
Infrastructure		– Legal, Accounting, Financial Management						
Human resource management		– Personnel, Pay, Recruitment, Training, Manpower Planning, etc.						
Product & Technology Development		– Product and Process Design, Market Testing, R&D, etc.						
Procurement		– Supplier Management, Funding, Subcontracting, Specification						
Recognize exchange potential	Initiate dialogue	Exchange information	Negotiate/tailor	Commit	Exchange value	Monitor	Reducing cost	
							Creating value	

Figure 1.2
Internal value chain: service companies.

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Symptoms	Challenge
Commoditization	Need for product/process differentiation
Lack of growth and over-capacity	Need to achieve growth within key accounts
Greater and stronger competition	Customer retention more vital than ever
Low margins	Greater pressure for cost reduction and quality improvement
Saturated markets	Need for new market creation and stimulation
Downsizing	Need to apply resource where it can deliver most value to customers

Table 1.3
Redefining the marketplace

illustrates the danger of allowing products and services to degenerate into commodities, with price availability and costs representing the only determinants of success. It is this danger more than any other that forces suppliers to pay more attention to key customers' specific requirements as a means of securing effective differentiation.

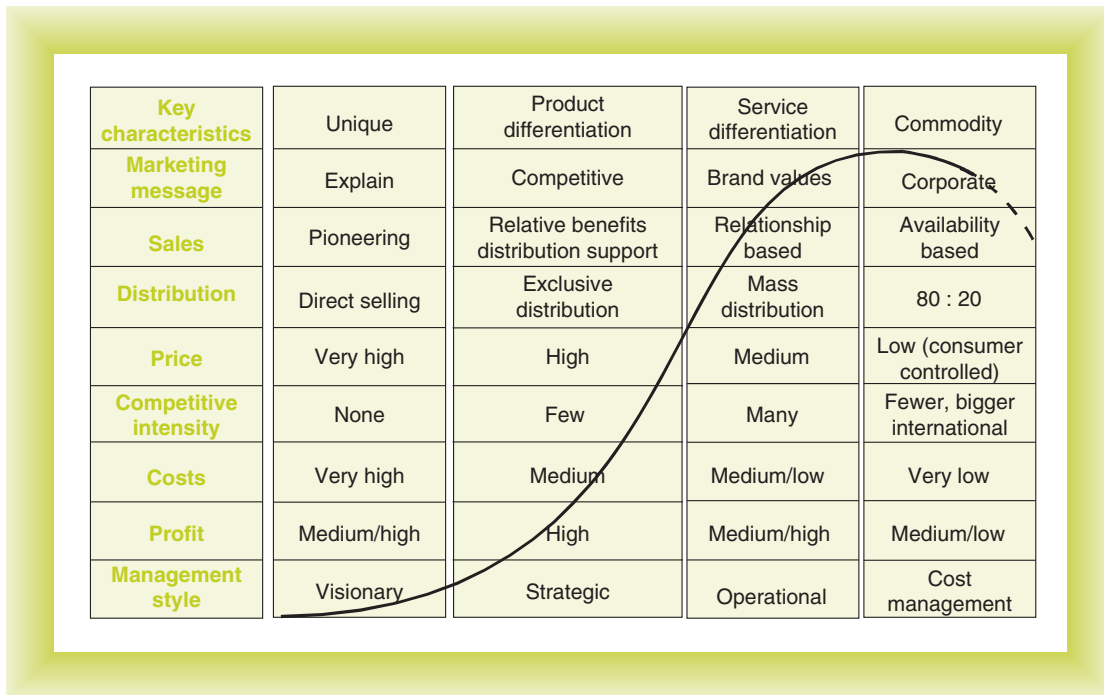


Figure 1.3 The product/market lifecycle and market characteristics.

The fact that most industry-to-industry product/service markets in the developed world are mature has clearly propelled the development of

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KAM. Suppliers know that they can only grow at the expense of a competitor and the obvious first option is to prise more of existing customers' business away from the opposition by means of account penetration. Highly professional KAM can facilitate the achievement of this objective.

Case study insight

IMI's response to market maturity

IMI was until recently a 'metal bashing' company based principally in the Midlands in the UK. Their Board redefined their market boundaries into five 'platform businesses' which they could dominate, put much of their manufacturing in South America and China, and began developing close relationships with selected global customers. As a result, they became one of the most profitable manufacturing companies in the world.

Business can only be won by being better than competitors and taking market share from them.

When inflation and growth were high in Western economies, companies enjoyed a comfort zone, which masked inefficiency. Now, most economies are experiencing low inflation and in many sectors across the world, prices are falling. In such a climate there is no room for complacency. Business can only be won by being better than competitors and taking market share from them. Product, process and people improvements are imperative. Under the kind of severe market pressures experienced in many economies in recent years, some companies throw out KAM with the cry 'Back to basics!' This is a mistake: in hard times, companies need to be much better, not more basic, as Norbord showed when the construction and housing market collapsed in 2009.

Case study insight

Norbord: KAM in tough times

Norbord is a manufacturer of wood based panels including chipboard, MDF and OSB (Oriented Strand Board). These products are predominantly used in the Construction, Furniture, and DIY sectors. New house building was one of the first casualties of the UK financial crisis, and Norbord's sales suffered as the bottom fell out of the market. The company had quite recently started its KAM initiative, and there were those in the company who felt that it was a luxury in those difficult times. Directors were clear, however, that if the company were to survive the recession, it would be, in part, by working even more closely with its strongest customers (its key accounts) rather than aggressively trying to find new customers in a very distressed marketplace. The strategy is paying dividends, and Norbord will come out of this recession with KAM more firmly embedded in its internal practises, and its approach to the marketplace.

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Customer power

The change within the business environment that is having the most dramatic impact on the development of KAM is the new-found expertise and power of customers and consumers in exercising choice (Table 1.4). Customer empowerment is not just a cultural change emanating from the growing popularity of adopting a customer focus; it is a consequence of mature markets. Nowadays, customers know that they can demand more from suppliers because suppliers must seek to retain customers – not just to maintain profitability, but also to stay in business.

Nowadays, customers know that they can demand more from suppliers because suppliers must seek to retain customers.

Symptoms	Challenge
Customers more demanding and more knowledgeable	Quality and traceability favour supply chain partnerships
Purchase behaviour strategic rather than tactical	A strategic and sympathetic approach to selling is required
Concentration of buying power	Selling companies need to add more value to succeed
Higher expectations	A greater investment and closer relation to the customer are required
Customer identity and role more complex	Need to better manage the complexities of multiple market channels

Table 1.4
Pleasing the customer

Customer power manifests itself in many ways. For example, there is the considerable concentration of industry, most recently on a transnational scale, which has made big customers even bigger (Figure 1.4). However, bigger customers do not necessarily mean more business

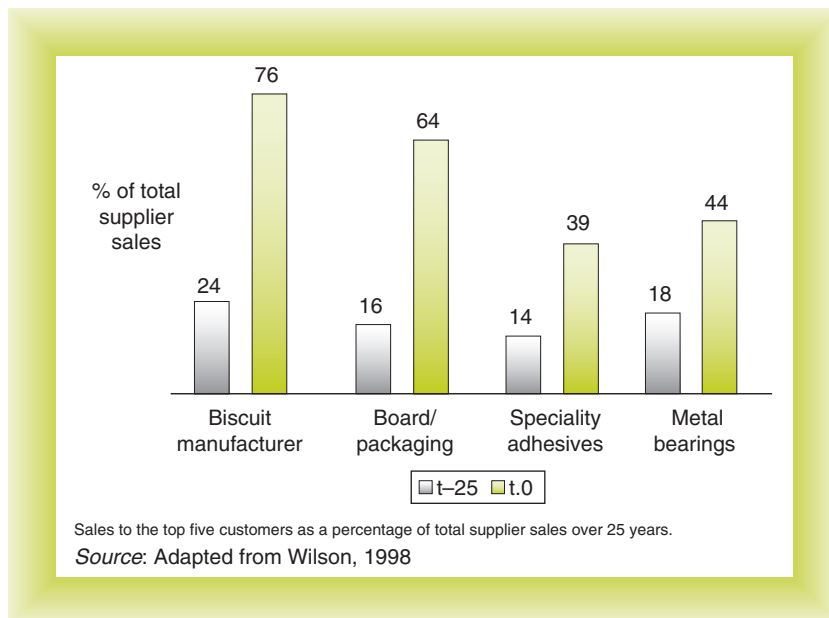


Figure 1.4
Concentration of buying power in industries.

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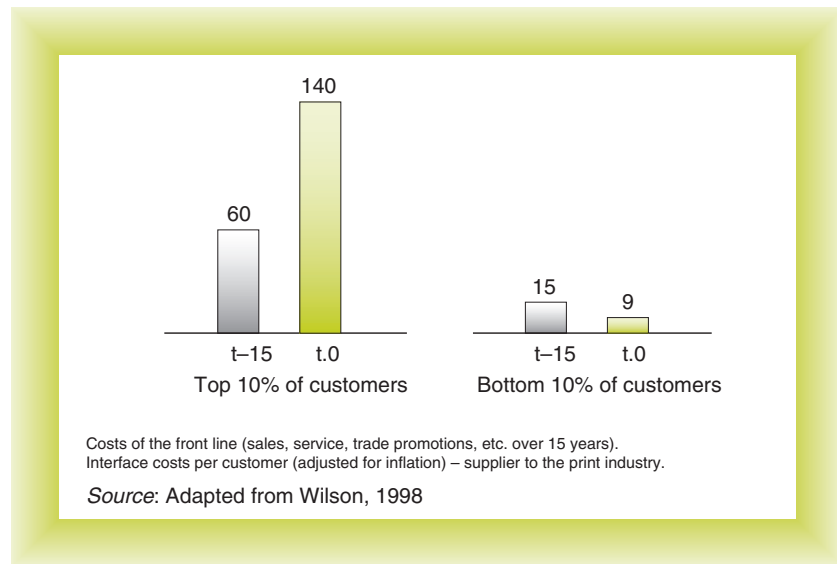


Figure 1.5
Cost of servicing the customer.

Suppliers who cannot meet the geographical scope and consistent outputs demanded by global customers are rationalized off lists of preferred suppliers.

opportunity. Suppliers who cannot meet the geographical scope and consistent outputs demanded by global customers are rationalized off lists of proposed suppliers. Customers want sophisticated solutions, which means that winning customer accounts can be very costly. It also means that retaining customers, which requires ongoing investment, is critical in achieving long-term profitability (Figure 1.5).

Case study insight

Key Industrial Equipment's response to the danger of commoditization

Key Industrial Equipment is a distributor of specialist products offering thousands of categories. In addition to offering a comprehensive range, the company has received industry recognition for innovation and service. It offers extremely rapid delivery, electronic data interchange and will take on the assembly of parts if the customer requires it. In discussions with customers, they place the emphasis on end-to-end value rather than on unit price.

Consumers will soon leap-frog any links in the supply chain that they feel do not add value.

The customer may have always been hailed as king but, not being a very well-informed monarch, the king was often at the mercy of his 'subjects' (suppliers). The rising power of consumer pressure groups and the popular media have changed all that. They have wrested power from companies and vested it in the ultimate users of their products and services. End-customers expect a great deal of respect, which is now often contractually assured in some sort of charter document. The logical extension of this consumer-driven scenario is cooperation between all organizations delivering value in the flow of supply from raw materials to the consumer. The concept of adding

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value is significant. Consumers will soon leap-frog any links in the supply chain that they feel do not add value.

Customers need raw materials to be converted into what they can use, taken to where they need them and presented to them for choice. Which company in the supply chain does any of these is irrelevant. Consumer champions are currently also casting a critical eye over the whole supply chain for ethical and environmental reasons. Trusted brand names have to ensure that their values are passed up the supply chain.

Consumers today know more about supply chains than might ever have interested them 10–20 years ago.

Consumers today know more about supply chains than might ever have interested them 10–20 years ago: they see it as relevant to the end-product they obtain. The idea of companies working together with their suppliers in order to deliver more value to the end-consumer is an attractive one, a matter of common sense. This is particularly pertinent to businesses which operate across national boundaries where the value chain is exceedingly complex and cultural sensitivities must be respected.

1.1.5 Globalization

The globalization of business has had many side-effects, including a greater interdependency between global customers and suppliers who have the capability to meet each other's increasingly complex needs (Table 1.5). These suppliers also realize the extent to which they can grow with their key customers if they consistently succeed in meeting their customers' expectations cost-effectively.

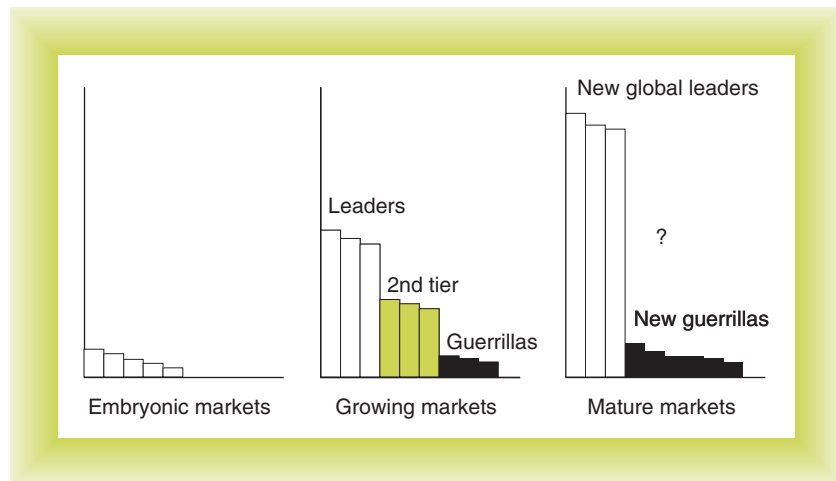
Symptoms	Challenge
Industry players undifferentiated	Restructuring to achieve wider scope (restructuring of domestic operations to compete internationally)
Greater and stronger competition	Customer retention more vital than ever
Lower margins	Greater pressure for cost reduction and quality improvement
Greater customer choice	Need to customize offers
Larger and more complex markets	Need to become customer-focused in larger and more disparate markets

Table 1.5
Coping with globalization

Figure 1.6 shows that as industries mature, the end-result is often only a handful of truly global companies dominating an industry. Hence, there are only 10 car companies in the world and four firms of accountants, while in the UK, for example, four supermarkets account for about 80 per cent of all fast-moving consumer products.

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Figure 1.6
Evolution of market
maturity.



1.1.6 Implications

The impact of all these changes – the imperative of keeping pace with rapid change, the requirement of refining processes, the necessity of redefining the character of the marketplace, the need for satisfying increasingly sophisticated customers/consumers and the obligation of facing the growing scope and scale of competition – has reverberated through the business relationship itself. It has encouraged KAM away from the traditional construct of a single relationship between salesperson and buyer, and towards the concept of strategic customers, where key customers command attention on vital statistics measuring more than simply their size.

CHECKPOINT

Pressures on businesses today

- Do you know how the pressures described above affect your company?

We see an increasing number of companies starting to build models of account attractiveness, matching their resources to the profit and status of any potential given customer or prospect. We also witness increasing professionalism among purchasers and decision-making units in buying companies as they evaluate the longer-term value offered by suppliers (the quality of products, processes and people) rather than solely the price deal.

1.2 Why understanding relationships is so important

The intercompany relationship is the 'glue' that binds companies together.

The relationship between two organizations has an existence beyond the obvious types of interaction, such as product and service adaptation, operational delivery and underlying strategy. All of these

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contribute to the nature and development of the relationship as well as depending on it (Figure 1.7). The intercompany relationship is affected by these interfaces and may also buffer turbulence arising from them. It is the 'glue' that binds companies together more or less closely and the medium through which interactions take place to deliver action.

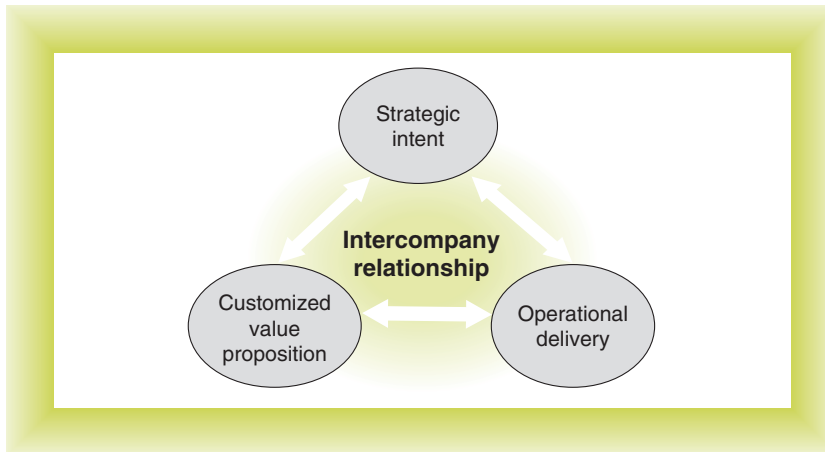


Figure 1.7
The relationship as a medium.

Clearly, understanding the nature and potential of the customer relationship is critical in assessing opportunities and managing business development. We need to know where we stand now with our customer and what further engagement might entail. We will also need a sound appreciation of their market position, and internal strengths and constraints (see Chapter 7).

Understanding key relationships is both important and challenging because:

- the risks are ambiguous and the stakes are high,
- supplier–buyer interactions are already complex and lie at the heart of major change, and
- key relationships operate at different levels which require different behaviours.

1.2.1 Relationship risks

One of the primary reasons for developing relationships is risk reduction. There are risks associated with building close relationships with key customers as well as risks associated with not building them. In theory, there should be less chance of relationship breakdown where there is joint commitment, barriers to exit and mutual understanding and trust (see Chapters 3 and 4). However, while these attributes may appear highly desirable, they actually carry risks of their own. For example:

- The risk of being vulnerable to opportunism and not obtaining a satisfactory saving or return on investment in the relationship.

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- The risk of committing to one partner at the exclusion of others and 'backing the wrong horse'.
- The risk of misunderstanding the relationship and failing to achieve reciprocal security.

1.2.2 Satisfactory return

The major question must be 'If we put time, effort and money into developing closer relationships with our trading partners, will they be more profitable?' The answer is not clear-cut, though it may be summed up as 'Yes, possibly, but not automatically'.

Traditionally, customer cost accounting has been rudimentary.

There is ample evidence from numerous sources indicating that suppliers have great difficulty in measuring the real profitability of their customers. Traditionally, accounting systems have used a geographical or business unit and/or product basis of analysis and customer cost accounting has been rudimentary. Substantial costs such as special customized developments, high-level, intercompany contacts and various additional services are very rarely allocated to individual customers. Thus, real customer profitability is difficult to analyse in practice and these intrinsic difficulties are compounded by inherent challenges to internal vested interests.

Alarming, although few suppliers can assess the profitability of individual key accounts accurately, many suspect that, ultimately, they lose money on them. While Chapter 6 explores this problem in greater detail, the issue is introduced here to highlight some fundamental points.

- Close relationships with key accounts have substantial cost implications.
- The mismanagement of just a few large accounts can be potentially (disastrously) loss-making.
- Customer relationships should be carefully selected and prioritized for the prudent investment of scarce resources (see Chapter 2).

CHECKPOINT

Customer profitability

- Do you know the profitability of individual customers?

All too often the cost of pursuing a closer relationship is not anticipated and properly quantified.

The cost of building close, sophisticated, groundbreaking, new relationships should not be underestimated. Frequent, multilevel, multi-function communication alone represents a considerable expense. Further, relationships development usually entails investment in initiatives such as joint marketing, new restructuring, electronic commerce, staff retraining and stockholding. All too often the cost of pursuing a closer relationship is not anticipated and properly quantified.

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Firmness can pay off handsomely: one loss-making company, admittedly with dominant shares in its core markets, implemented ‘an aggressively upward pricing policy’ with great success and achieved a return to excellent profits within two years.

1.2.3 Implications of joint commitment

In many cases, the commitment of the buying company is greater than that of the selling company (although the latter would not see it this way). Where it does not make sense to multisource a product or service, the buying company may be obliged to adopt a sole supplier. Meanwhile, the selling company will continue to supply other customers. The buying company must ensure that it has made the right choice, not only in relation to the matter at hand, but also because its decision will be a statement to other suppliers.

Similarly, a selling company’s key customers may demand supplier exclusivity, preventing the supplier from broadening its customer base by serving the customers’ competitors. The practice of exerting such pressure has generally been accepted by advertising agencies, for example, while other sectors have resisted it. However, the growth in the number of customers of considerable size has meant that this practice is increasingly tolerated.

The range of functions and initiatives involved in the relationship may reach a point where significant company-level backing is required which cannot be satisfied simply by allocating more resources, people and time. At this level of relationship, there may not be any room for parallel relationships, even for the selling company. For example, if two competing companies were developing similar new products at the same time using a shared supplier, the supplier would find it exceedingly difficult to work with both customers in the same way. Confidentiality might be hard to guarantee, as might be the origins of a research breakthrough. If the supplier and each of the buying companies were to approach the marketplace together, the fact that the company is offering products together with two different partners might confuse consumers.

At this level of relationship, there may not be any room for parallel relationships, even for the selling company.

However, by choosing to work with a single business partner, both supplier and buyer are consciously excluding others and declaring that the decision is right for them. Both companies want a partner they can work with and benefit from. ‘Backing the right horse’ for a strategic-level relationship need not be as much of a gamble as backing a real horse if the pre-existing relationship is well understood and well managed.

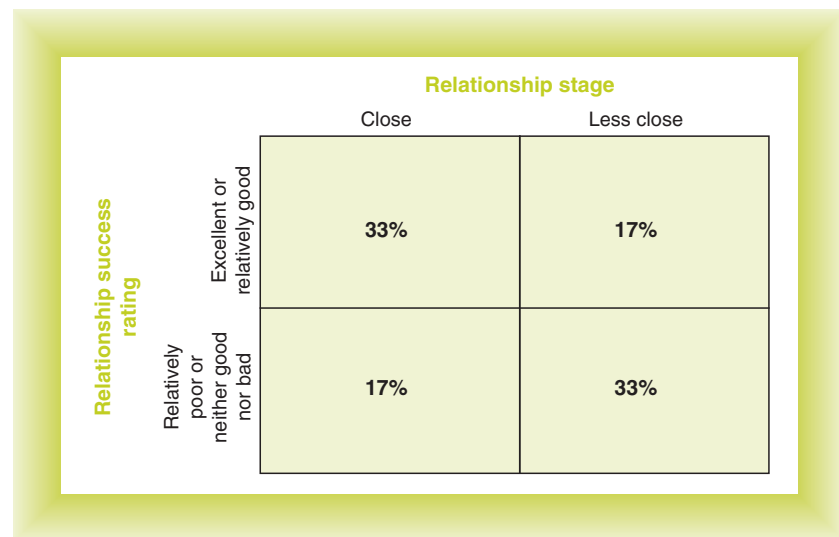
1.2.4 Misconception and disappointment

There is a common misconception that closer relationships will automatically bring greater profits. The reality is not so simple. The inability of companies to measure profitability accurately or realistically gives cause for confusion. However, it would appear that

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relationship stage, maturity and business success are linked: closer key relationships are widely considered more successful than relatively distant key relationships according to a range of accepted success and financial indicators (Figure 1.8). Nevertheless, a substantial minority of relationships do not conform to this 'rule' and it would be a mistake to assume that developing any relationship will automatically bring success or that relationships which are not developed to closer levels are failures. This was clearly demonstrated in the Cranfield/*Financial Times* research report (McDonald and Woodburn, 1999).

Figure 1.8
Relationship closeness
versus relationship
success.



From the supplier's perspective, an attempt at forced intimacy would be a mistake.

A number of these non-conformists represent successful relationships that are not particularly close for good reasons. For example, if the product or service purchased is not a core item and does not offer opportunities for deriving differential benefit, the customer may naturally decide that a simple purchase with minimal support is adequate. Any extra attention or additional services lavished on the customer might be accepted, but not necessarily valued. From the supplier's perspective, an attempt at forced intimacy would be a mistake in this case and the business should be serviced with efficiency and a positive attitude, but not much more.

Case study insight

'I do not think suppliers would benefit from getting any closer to us: quite the reverse. We are a very "taking" company and it would not do them any good.' (Retailer)

It is not uncommon for some key relationships to be close, but to be considered unsuccessful and/or unprofitable. They may be intransigent situations into which companies have been cornered, perhaps by a determined buyer, optimistic key account manager or poorly written contract.

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The fact that relationships can reach higher levels of intimacy and still prove unsuccessful should make companies wary of selecting the right relationships to develop in the first place as well as managing them extremely carefully (see Chapter 2). Part of that selection process should be an assessment of the relationship's current stage of development and the buyer's and supplier's respective degrees of commitment.

There is yet a further danger: that of sliding imperceptibly, by numerous smaller steps, into a relationship that the company has failed to anticipate, which has implications that they are unprepared for or cannot recognize. Logically, the development of key customer relationships should be a strategic process linked to the design and implementation of overall business strategy. Surprisingly, this critical connection is often overlooked. Customer relationships, whether key accounts or otherwise, should be examined objectively and developed deliberately in line with company aims and capabilities.

Customer relationships, whether key accounts or otherwise, should be examined objectively and developed deliberately in line with company aims and capabilities.

1.3 Increasing complexity of key account relationships

Relationships with key customers are not only complex, but increasingly so. For top customers, the simple model of 'I, salesperson, sell; you, buyer, get' only applies in certain circumstances. Few, if any, major business initiatives are now developed on this axiom. So why have things changed and how has this made key account relationships more complex?

1.3.1 The consolidation of customers

Key customer relationships often involve major corporations as both suppliers and customers. Because an amorphous mass is impossible to motivate and measure, most large companies introduce subdivisions into their businesses and the larger these companies become, the more entities they will contain. In many cases, a supplier will do business with more than one entity within the client company. While such a multiple interface offers potential benefits in terms of developing an inside track to new business with other parts of the organization, it may also incur undesirable costs. For example, there may be an obligation to service uneconomical parts of the business, involvement in internal competition, downward price levelling and additional communication costs.

1.3.2 Dual roles: the customer may be 'competitor' as well as 'client'

As companies consolidate, the situation in which a customer is both a competitor and sometimes a supplier arises more frequently. Obviously, this intertwining of relationships and roles complicates behaviour. Takeovers that juxtapose competitors inappropriately are a common cause of terminated key account relationships. However,

The situation in which a customer is both a competitor and sometimes a supplier arises more frequently.

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some companies struggle on and learn to live with ambivalence, perhaps because industry consolidation leaves them with very little choice of customer or supplier. The potential for internal and external conflict is heightened and management of the relationship becomes evidently more strained.

1.3.3 *The development of global businesses that demand global supply*

Global customers requiring global supply and service add additional complexity to the task of managing relationships effectively. Problems which are easily identified but not easily resolved originate from differences in terms of language, culture, zone and geography, making the servicing of pan-global operations a tough challenge for even the fittest of suppliers. The prevalence of knowledgeable and powerful country managers helps somewhat, but the scope and size of the task remains formidable. In addition, a new infrastructure may be required to service markets previously outside the supplier's sphere of activity which now fall within its global contract, meaning more new partners, languages and cultures to assimilate into the relationship.

1.3.4 *The accelerating pace of change, particularly as new IT reshapes markets*

It is already evident that many companies will have to make huge adjustments very quickly as customers adapt to electronic commerce.

Information technology, in particular electronic commerce, is forcing huge changes in the way companies work and how their markets operate. As always, there is a lag between the availability of the new technology which is possessed by the enlightened few and mass uptake with full-scale revision of the basic practices and processes. While it is not yet clear what the ultimate impact of IT development will be for business, it is already evident that many companies will have to make huge adjustments very quickly as customers adapt to electronic commerce and demand similar immediacy and intimacy from their existing suppliers.

1.3.5 *The emphasis on strategic alliances*

New needs may be satisfied on both sides of the relationship by the creation of a strategic alliance with another company, which has strength in a specific area rather than through the development of existing internal expertise and physical assets. Selling companies may find themselves supplying third-party associates of their customers instead of their customers directly. They may also be supplying customers alongside other suppliers who may have been selected by them or by the customer. As supply chain management reaches further up- and downstream, more complex relationships are being formed involving more participants. Communication is likewise complicated and, because strategic alliances are often forged as a fast and flexible response to market change, opportunities for misunderstanding and confusion abound.

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Case study insight

Customer perspective

'We deal with our suppliers on product development, marketing and ordering, but our warehouse is managed for us by Tibbett & Britten, so suppliers deal with them on inbound logistics.'

With today's flattened management structures, cross-functional teams are encouraged to take part in the activities traditionally allocated to lower levels of responsibility, including direct customer contact and decision making. Key customer relationships put more people and more functions in direct contact with the customers or supplier than ever before.

While the internal interactions required to drive the machine which actually delivers the customer promise are discussed later in Chapters 3 and 4, it is already abundantly clear that relationships and, in particular, key account relationships are undoubtedly complicated by the increased quantity and variety of contact with the customer.

Summary

The external context in which buyer–seller relationships exist is becoming increasingly extensive and complex. Change drivers include the rapid pace of change, the refinement of processes, market maturity, heightened customer power and the globalization of business. At the same time, the internal, organizational context is also changing, removing traditional delineations of remit and responsibility. Conditions are more conducive to 'partnering' between suppliers and customers and, hence, the nature of marketing has altered. Marketers are moving away from a traditional transaction focus towards a customer focus. Thus, there is a pressing need for finding ways of describing relationships as a basis from which to understand them better and build them stronger – and this has led to the ascendancy of KAM.

