

1

The big picture

“When people talked about ‘Sales Strategy’ I used to laugh. As an oxymoron, even ‘Military Intelligence’ paled in comparison. In those days, ‘Sales Strategy’ was nothing more than simple tactics ruthlessly executed. But that was then. Today the wrong sales strategy sinks companies.”

Neil Rackham in *Sales and Marketing Management*, Spring 2000
Reproduced with kind permission from Professor Neil Rackham

The place of sales in business strategy

The role of marketing has been hotly debated over the years, whether it is strategic, tactical, or not even necessary. The role of sales is rarely questioned. Ever since Stone Age tribes traded pots for shells, selling has been necessary. Of course, you cannot have a seller without a buyer, but more of that later.

The evolution of business in the 20th century favored those with professional qualifications such as accountants, who frequently made the switch from money management to general management at Board level. Marketers too, armed with MBAs and compelling concepts like branding and segmentation, became more strategic and also jostled for a place on the Board. Not so sales. Most Sales VPs got on with selling, consoling themselves that the monetary rewards of selling provided a more attractive prize than power. Nevertheless, company politics did not go away. As soon as a quarterly target was missed, the sales force became the reason for the failure of the business strategy.

Can sales continue to sit on the strategic sidelines? In this era of customer orientation, it is more important than ever that sales managers should be

involved in strategy-making, despite assertions from some business gurus that marketing is strategic and sales is operational. Who else but salespeople are close enough to understand the relevant decision-makers in the customer organization? If a company truly wants to align its strategy with customers' strategies, it is no longer appropriate for salespeople to be the tactical, operational doers, whose feedback is filtered through layers of management and skepticism.

Professor Nigel Piercy and Nikala Lane at Warwick Business School have identified ways in which the sales function contributes to strategy-making, and call it the five Is: – involvement, intelligence, integration, internal marketing and infrastructure development. We will discuss many of these functions in Part III, with a specific focus on infrastructure development in Chapter 12. At the moment, let's just look at the big picture.

Intelligence is the easiest to discuss. Professional salespeople should be closely scrutinizing the customer and their business environment and applying their skills to selective supplier–customer relationship development. Some companies may assume that marketing does all that research, and for some categories of relationship, an aggregation of information about customer needs may be all that is necessary. But in business-to-business, many customers are large and complex, and the account manager's understanding should be complete.

The account manager can identify opportunities for relationship development with certain customers, but operations have to deliver it. That's where internal marketing is essential, but it also leads on to involvement and integration. If sales is not involved in strategic decisions at the same level as operations, what does that say about the status of the organization's knowledge of the customer? Sales can only be integrated into the rest of the organization when it is represented at the highest decision-making level. Where else can sales explain what customers are doing, and how the organization can add value?

In this era of customer orientation, it is more important than ever that sales managers should be involved in strategy-making, despite assertions from some business gurus that marketing is strategic and sales is operational. Who else but salespeople are close enough to understand the relevant decision-makers in the customer organization?

Selling has always been a “boundary-spanning” role – representing the company to the customer and representing the customer within the company. Companies cannot call themselves “customer-focused” unless they have that “voice of the customer” in the Boardroom. Is it just wishful thinking that sales should have a place at the Boardroom table? Not at all.

Selling has always been a “boundary-spanning” role – representing the company to the customer and representing the customer within the company.

We live in an era where a company’s top five customers frequently generate more than half of an organization’s revenue. These key customers have a significant impact on all parts of the business: they influence, or even decide, R&D priorities; and they affect every element of the business chain, from systems design to distribution. Increasingly, it makes no sense to have a Board on which the voice of these key customers is not represented. Marketing can represent the voice of the many anonymous customers who, in aggregation, are called “the marketplace”, but only sales has the closeness and depth needed to speak for these key customers who have such a profound effect on a company’s strategy and future.

Selling with strategic focus has implications for the way sales activity is organized. It also has implications for the knowledge that salespeople, account managers and sales managers need. In order to operate at Board level, you need a certain language, and a historical and cultural background of strategy-making. This chapter gives an overview of business strategy models that sales managers and account managers need to present their case internally and to work with senior customer personnel on relationship development.

So what are the strategic roles of the sales function?

- Involvement – in strategy formulation
- Intelligence – industry and customer knowledge and analysis
- Integration – working across functions to develop value
- Internal marketing – of the customer to colleagues
- Infrastructure development

Source: Piercy and Lane (2005)

What is the “big picture” that drives strategic thinking?

No company operates in isolation. When business strategy is converted into sales targets without sufficient involvement of sales in the strategy formation, there’s often a serious disconnect. It sometimes seems that Chief Executive Officers and their strategy formulation teams assume that the company can drive itself anywhere, regardless of economic cycles, the activity of competition or customer behaviour.

It sometimes seems that Chief Executive Officers and their strategy formulation teams assume that the company can drive itself anywhere, regardless of economic cycles, the activity of competition or customer behaviour.

Real strategy is not like that. Strategic plans cover not only “where are we now?” and “where do we want to be?” but also the methods of getting there. Plans must be modified by consideration of the global and local business environment (see Figure 1.1).

Quite early in a strategic plan, there is usually a “PEST” analysis, of the political, economic, social and technological trends that impact on the company. Just keeping up to date with new laws affecting the operations of the company is a demanding activity. Economic conditions affect all players in the global economy, but some industries are more sensitive than others to economic swings. Food retail is a good place to be in a recession as we all need to eat, but the size of a knowledge services firm, such as systems integration, can change significantly depending on economic prosperity or recession.

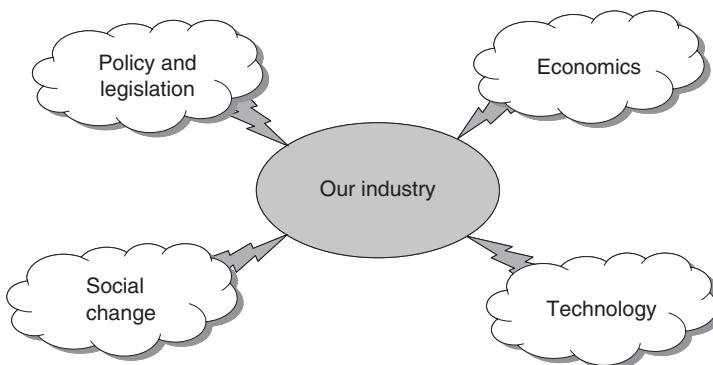


Figure 1.1 The business environment.

Social trends are very important, even for business-to-business companies. In retailing, it is vital to know the patterns of the catchment area of each store, by age, income, cultural origin and family size (demographics). This enables plans to be made to get the right stock to the right stores at the right time. All demand in a supply chain is derived from aggregated consumer needs and wants. If the rising generation of consumers is concerned about the environment and social responsibility, then raw materials extraction companies need to ensure that that is reflected in their activities.

Other external impacts, such as the weather, local sporting success or national tragedies, also have to be taken into account. This analysis is a means of identifying some genuine opportunities and threats for the business.

Political/legislative factors

- Corporate governance
- Health and safety at work
- Equal opportunities/diversity
- Employment law, governing individuals' rights at work
- Consumer protection
- Tax and duties on products/services
- Regulations governing use of land and property
- Environmental regulations
- Copyright law
- Privacy law, e.g. regulations covering spam e-mail and unsolicited telephone calls
- Prohibition/legalization of substances and activities.

Adapting to the external business environment

In 1989 in Argentina, inflation reached approximately 5,000%. The 1990s saw increased stability, but also deregulation, which opened up competition.

In a study of companies adapting to this dramatic economic change between 1989 and 1999, researchers found that flexible, adaptive companies had the following characteristics in the way they gathered information about their business environment:

- They had formal and informal ways of gathering information about the external business environment.
- They attempted to create an external orientation.
- They adopted new models for processing, analyzing and using external information.

“Every employee is aware of the importance of having an open mind and catching all they can from the sector, competitors and customers.”

Source: Hatum and Pettigrew (2006)

An important role of VP Sales is to contribute to an understanding of how PEST factors are affecting the company, and to take the lead on identifying how these factors are affecting certain customers in particular industries. Changes in external pressures can affect the way they want to buy, as we will see in Chapter 2.

You may ask how objective a PEST analysis can be. Some businesspeople can have their own fears or enthusiasms about any or all of the PEST factors, which is why other sources of opinion should be reviewed. Research institutes, industry watchers, government departments and consultants all produce analyses of trends and predictions. Since these analyses are based on reliable sources, businesspeople should take notice of them, at least for developing a Plan B in case Plan A, or “business-as-usual”, does not give the expected results.

Early in my career in the IT industry, I worked on a strategic plan that was heavily influenced by a technology trend. IT analysts’ reports were predicting that most companies would decentralize their IT installations from mainframe computers with dumb terminals to client/server networked technology. Client/server versions of mainframe software had to be developed in order to meet this trend. Subsequent reviews suggested that the mainframe software performance was still buoyant but the client/server software was not being accepted very rapidly. Global economic recession had arrested the customers’ desire for change.

The analysts’ predictions were not necessarily wrong. The rise of the Internet in the 1990s ensured that networked servers with their personal computer clients became the norm, so it was a good idea to have prepared new products for the new world. Mainframes did not disappear, they merely

changed into super-servers, so the plan could be seen in hindsight as pessimistic compared to the reality that emerged. Nevertheless, it would have been desperately wrong to ignore the analysts' predictions altogether and assume that a steady sales performance for a mainframe software product with over 20 years' heritage was going to continue forever.

Competitive pressure in our industry

Too many companies, not enough differentiation

Merging to survive

Sometimes, there are just too many companies competing to deliver similar value. In 2006, two Taiwanese companies merged to create a large-size display panel supplier that could rival the Korean market leaders. Demand for large-size TFT-LCD (Thin Film Transistor-Liquid Crystal Display) screens was weak and prices were declining, putting pressure on revenue and profitability in the industry. Scale and capacity were the keys to survival.

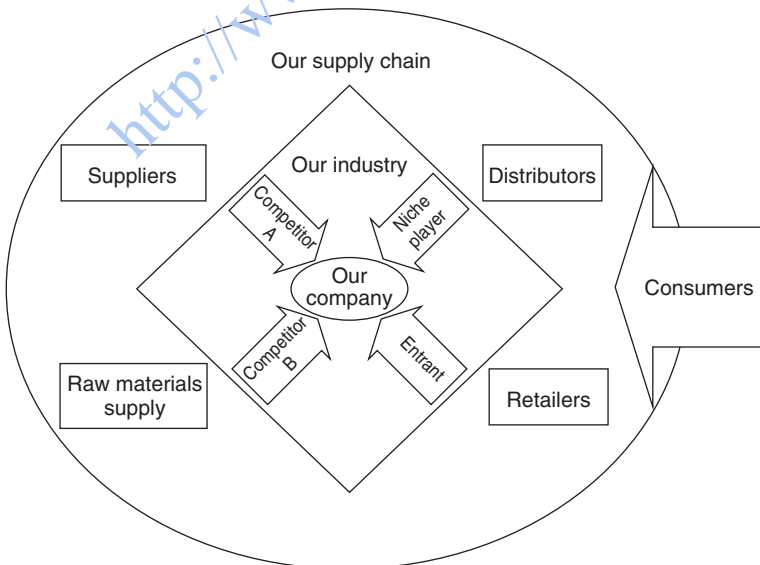


Figure 1.2 Industrial supply chain.

Decisions to deal with competitive pressure through merger are usually done collectively and at a high level. VP Sales should be able to contribute to them based on feedback from salespeople about particular competitors. Salespeople must know what their direct competitors are doing. Unfortunately, research report after research report suggests that salespeople have such faith in their own products and services that they do not pay enough attention to learning about competitors and why they might be more successful in

developing relationships with customers. A recent survey of 426 salespeople found that respondents were not confident that they had a good understanding of the competitive environment or industry benchmarks (The Communication Challenge Ltd, 2006). When salespeople understand “the big picture”, they are able to impress the customer with their knowledge, and demonstrate a clear framework of differentiating value to address their needs.

Besides understanding current competitors, salespeople also have to be constantly alert to the possibility of new entrants coming into the industry. Sometimes, the effect of an entrant can be dramatic. A distinctive European brand entered the US vacuum cleaner market in 2002, and gained more than 20% of market share within four years. Meanwhile, the parent company of the former market leader decided to sell it.

Working closely with other supply chain players in strategic relationships may help a company to cannibalize its own products or services before someone else does. As the long-term nature of a relationship reduces risk, innovation becomes more of an opportunity. A balanced portfolio of customer relationships can help to reduce risk if a particular strategic relationship is lost to a market entrant.

Meanwhile, the biggest competitor that any company should fear is “do nothing”. In the IT industry, a high proportion of proposals are lost to the

Salespeople must know what their direct competitors are doing.

Unfortunately, research report after research report suggests that salespeople have such faith in their own products and services that they do not pay enough attention to learning about competitors and why they might be more successful in developing relationships with customers.

customer's inertia and unwillingness to act, which can often be linked to uncertainty and risk in the business environment.

Supply chain influences: upstream suppliers

Recession prompts OEM competition with channel

With business hard to find in the dot.com bust after the dot-com boom, the direct sales teams of some of the major players in the IT industry appeared to be reaching deeper into the small and medium-sized business customers that were usually served by channel partners. Where it occurred, this conflict risked reducing margins for both the supplier and the reseller. It is worth noting that it was the front-line salespeople in the resellers who were the first to realize the situation.

If our immediate suppliers hold significant power in the supply chain, or if the companies extracting raw materials create bottlenecks as their ability to supply – and their prices – vary, our opportunity for profit is lower. Of course, the prices we pay for goods may be affected by the suppliers' bargaining power, but we may be able to partner with suppliers to ensure some long-term stability in prices. There might be different types of suppliers that a company could work with to ensure a better balance of mutuality. The worst we might fear from our suppliers is that they have enough power and brand value in the industry to by-pass whatever value we create and build relationships directly with our customers. We will look later at how value has to be justified in all aspects of the supply chain. There are also legal constraints on supplier power. When a company has more than 25% of the market share, they attract the interest of anti-trust legislators. This reduces to some degree their enthusiasm for wielding their power.

Derived demand: how consumers drive supply chains

If your company is extracting tin, it is because millions of people want to buy food in tins as that extends the food's shelf life. So, if all demand is "derived demand" from the consumer, why do we think that we can push

our value down the supply chain? Many strategists now talk about the “demand chain”. In fact, the idea of a demand chain was identified in the 18th century by the Scottish economist/philosopher, Adam Smith:

“Consumption is the sole end of all production; and the interest of the producer ought to be attended to, only so far as it may be necessary for promoting that of the consumer.”

Adam Smith, *The Wealth of Nations*, Book IV, Chapter VIII (1776)

Consumer power generally expresses itself as an insatiable hunger for more choice at lower prices. This contributes to the fearsome reputation of retailers in the supply chain. I once interviewed a purchasing manager in a medium-sized retailer who admitted pushing an account manager too hard on discount. The account manager walked away from the negotiations, and supply ceased. The next week the buyer had the hassle of explaining to his manager why an important brand was missing from the shelves in stores, and backed down. In a large retailer, this would have been high risk indeed.

Many retailers have progressive supplier development programs that can help small companies to grow and be profitable and successful. Power brings with it public expectations of responsibility. For example, retailers can be called upon to address power imbalances throughout the supply chain.

Customer power reaches up the supply chain

For four years, a group of agricultural workers in the USA conducted a campaign to gain public support for their demands for better wages and working conditions. Student groups, religious organizations and celebrities joined a boycott of fast food chains that were dealing with the workers' employers. To end the boycott of their brand, one chain implemented a “pass-through” to ensure that the workers got an increase in their piece rate.

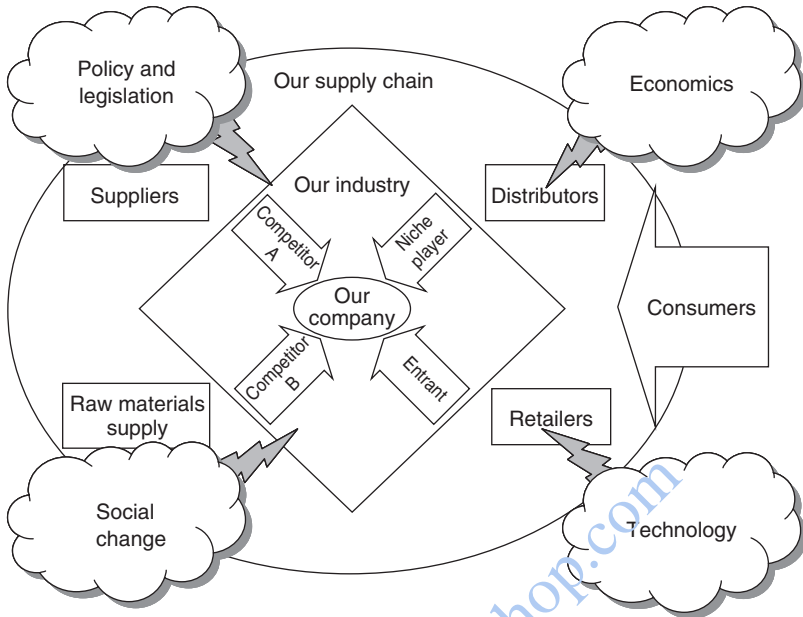


Figure 1.3 The big picture.

You may not be in an industry that deals with retailers, or even distributors. Perhaps your business involves working directly with industry customers. This has been my experience in the IT industry. This can be equally challenging as large companies who represent a significant proportion of their suppliers' revenues are bound to be tempted to use that power when necessary. If industry conditions allow it, reinvigorating your customer base to ensure a broad portfolio of relationships is essential to minimize the risks associated with large and powerful customers. We will discuss this more fully in Chapter 3.

The components of the whole business environment are shown in Figure 1.3.

Opportunities and threats

All the external factors in the business environment are sources of opportunities and threats, so when we talk about a SWOT analysis, the "O" and "T" sections should be derived from PEST and the demand chain. That is the big picture that company strategists have to address; and VP Sales has to contribute to an understanding of what this picture is. The way that

strategists use this information to change the company's position in a turbulent business environment is by changing investment in the company's relative strengths and weaknesses to enable it to perform more effectively.

Strengths and weaknesses

In 1985, strategy guru Michael Porter introduced a concept called the "Internal Value Chain" to track exactly where companies add value to immediate customers. From the different functions identified in the internal value chain, we could make a judgment on what we do well, and what we don't do well. This was an extremely helpful tool at the time.

Looking back from 2006, this "chain" model seems to have been rooted in the concept of a company having different functions that pass things on to another department (Figure 1.4). In modern organizations that concept can be seen as a weakness, as it is at the handover stage that things tend to go wrong. The lack of internal integration can result in inefficiencies and dissatisfied customers, and functions within the company should at least be interlocking cogs in a finely tuned machine. We can all think of many ways that companies differentiate their value, even in B2B organizations, that must be inherent in all functions. Perhaps a company could be a "green" leader, known for an excellent record on everything from controlling its factory emissions to recycling paper and print cartridges. "Green" value leadership can now be important in winning government business in some parts of Europe.

Two things are certain about a company's strengths. One is that it does not matter a hoot what we who work for the company think are our

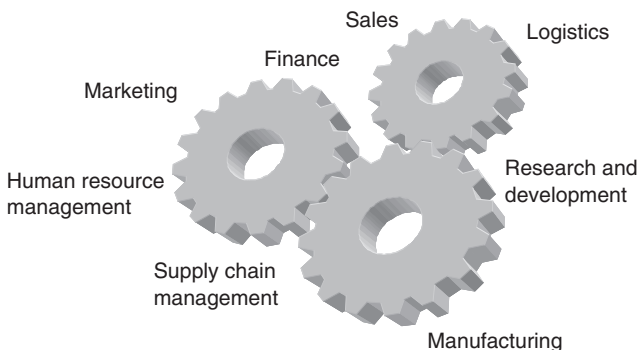


Figure 1.4 *The internal value chain.*

strengths, or even what the Chief Executive Officer tells industry analysts. A strength is only a strength if it is seen as a strength by customers, and if they think that it makes us different from our competitors. Let's

A strength is only a strength if it is seen as a strength by customers, and if they think that it makes us different from our competitors.

look at a value differentiator that almost every purchasing decision-maker will tell you is important: "Being easy to do business with." What does that mean? Customers who want it talk about simple processes – reliability, friendly service, speedy problem resolution, and much more. It is a powerful company-wide competence where it exists, and if customers tell you that you are easier to do business with than competitors in a particular way, then that is worth putting in a SWOT analysis.

On the basis of building on strengths, addressing weaknesses, exploiting opportunities and minimizing threats, companies can make strategies for themselves. But we have all seen many SWOT analyses that have simply been long lists of vague ideas or wishful thinking. As such, they can hardly inform strategy. A variation that is much more rigorous is a grid designed by key account strategist Diana Woodburn.

Her principles include the minimizing of the SWOT lists to a few key factors that are specific and relevant. These few things then need to be forced together to generate some truly strategic thinking. Do we have a strength that is neatly aligned with an opportunity? For example, what if a bureaucratic company has just taken over a nimble and flexible competitor, and one of our strengths is "ease of doing business with us"? We should be

	Strengths 1 2 3	Weaknesses 1 2 3
Opportunities 1 2 3	S/Os Strategic wins!	W/Os Investment?
Threats 1 2 3	S/Ts Risk management	T/Ws Danger area Contingency plan

Figure 1.5 A SWOT matrix. (Reproduced with kind permission from Diana Woodburn of Marketing Best Practice, www.marketingbp.com.)

able to leverage that all the more if our nearest rival gets restructured into its new owner's straitjacket or submerged in post-acquisition navel-gazing. If we are in a highly competitive industry such as printing, but are recognized for our expertise in using recycled paper and biodegradable inks, we should be swinging into action whenever new "green" legislation is passed.

The alignment of weaknesses with threats is also possible, and will require investment to avoid difficulty. Counteracting threats with strengths and addressing weaknesses that might cause opportunities to be lost is also important. Looking at SWOT this way tells us more about the strategy that is needed.

What's all this analysis for?

"Everybody's got a plan, until he gets hit", according to a heavyweight boxing world champion. But as Louis Pasteur (1822–1895), French microbiologist and inventor of pasteurization of milk pointed out, "chance favours only the prepared mind."

Analysis can lead to paralysis, decision-making that takes too long, and strategic plans that are inflexible and get ignored. An inside-out approach to analysis and planning can make a company internally focused with the possibility of being wrong in its view of the world. There are many variables that affect the future of any business, and contingency planning for all of them would be wasteful. Risks associated with any sort of investment seem to get constantly higher and more complex.

Portfolios reduce risk

The analogy of supply convoys in World War Two was used in a *McKinsey Quarterly* article to explain how companies need to operate in a complex and rapidly changing world. The weather was one problem – that could be difficult to manage despite meteorological forecasts and navigational equipment. Even more of a problem was enemy activity; attack by submarine, air or other ships was a constant risk, despite the best efforts of the intelligence services. Convoys were deployed, with supply ships

mixed with troop ships and destroyers, which improved the chances of each ship and the supplies crossing the ocean safely.

These convoys were the military equivalent of “portfolios” in business. In order to get your enterprise through the dangers of the business environment, you have to work with a variety of initiatives, in a collection, some of which will make it and some which will not. The key to success is a disciplined search for the right collection and a flexible approach to future change.

Source: Bryan (2002)

Readers might also reflect that many companies may make strategic plans, but manage themselves to quarterly objectives. This is ironic because expectations of future performance, not last quarter’s results, should theoretically drive share prices. But try telling that to a CEO who has just missed a sales forecast for the second consecutive quarter.

It is difficult to manage for the long term – anyone knows that from their own personal development – but consultants like McKinsey suggest that it is possible for companies to have a long-term value orientation yet deliver short-term performance. For example: some companies are known for having a long-term focus on innovation and managing progress in the short-term by measuring the proportion of sales coming from new products (Davis, 2005).

Some companies are known for having a long-term focus on innovation and managing progress in the short-term by measuring the proportion of sales coming from new products

Portfolio analysis

A portfolio is a collection of, for example, artwork, investment, property, products, skills or customers. Having a collection of things in a business sense is sometimes referred to as a combination or spread for the purpose of reducing risk and maximizing opportunity. Definitions of portfolio management describe a business process by which a company formulates strategy to

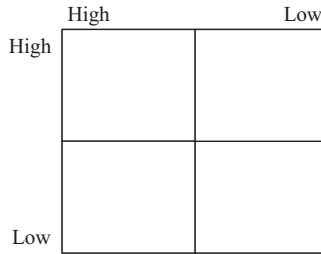


Figure 1.6 A 2 by 2 matrix.

achieve its overall objectives: how it decides on the mix within the collection in order to prioritize resource allocation, accepting a risk/reward trade-off.

To visualize the mix, strategists use a diagram and call it a matrix. The meanings of matrix include “the formative parts of an animal organ” and “mass of rock enclosing gems”, but in its most general sense, according to the *Oxford English Dictionary*, it means “the place in which things are developed”. Strategists and marketers have been working with matrices to categorize items within portfolios for decades.

These portfolios usually involve a 2×2 box, with axes marked high and low (Figure 1.6). The horizontal axis works from left to right. Once you get used to these universally useful boxes, the world of strategy is yours for the taking!

Product portfolio management

The Boston Consulting Group’s Growth-Share Matrix, designed in the product-led 1960s, is still probably the most well-used approach to analyzing a company’s product portfolio, and the earliest example of a strategic tool for professional marketers. The vertical axis measured the market growth rate and the product’s position on the horizontal axis shows the relative competitive position through market share. The Profit Impact of Marketing Strategy (PIMS) program, which has been managed by the Strategic Planning Institute since 1975, found that high return on investment was closely related to high market share. PIMS is still collecting and analyzing data from hundreds of companies (see www.pimsonline.com).

Some researchers have pointed out that the cost of acquiring market share varies considerably from market to market, and that correlation does not

prove causation, so we must treat generalizations carefully. Nevertheless, the BCG matrix has stood the test of time and gained popular appeal with its stereotypical product types of “Wildcats”, “stars”, “cash cows” and “dogs”.

Correlation does not prove causation

In my first statistics seminar as an undergraduate, the tutor handed out two lists of numbers by calendar month. One was the number of births in the country; the other was the number of storks in the country. More storks are present in the summer, when the birth rate is higher. On the basis of his lists, we could conclude that there was a statistical correlation between the number of storks in the country and the birth rate. His point was, of course, that the correlation does not prove that the storks brought the babies.

Business unit portfolio management

To accommodate more variables and shift the focus of matrix management to markets, McKinsey, working with General Electric, developed a nine-cell Attractiveness–Capabilities matrix. From General Electric’s point of view, something was needed to address the problem of its business unit managers planning too conservatively, which resulted in a weak plan at corporate level when the unit plans were aggregated (Lorange, 1975).

The vertical axis “industry attractiveness” addressed the industry sector in which the unit operated. A score for the business unit was derived from factors such as market size, market growth and profitability, weighted and scored to create a compound overall score. To score “business strengths” on the horizontal axis, the unit was judged on market share, growth, product quality, technology skills, economies of scales and experience, marketing capability and profitability relative to competitors. The importance of the business strength score was that it was deemed to be something that the unit could change with the right allocation of resources over time.

With a score on each axis, each GE business unit would land in one of the cells in the matrix. Each of the nine cells in the matrix was allocated a label indicating strategic direction. For example, high industry attractiveness and strong business strengths would result in investment for growth;

medium industry attractiveness and weak business strength would result in a strategy of “manage for cash”. Given the continuing success of GE, who can argue against the power of the tool to focus resources where growth could be maximized? So, the company got a balanced plan rather than a conservative plan, ambitious where success was achievable, tactical where market conditions were unfavourable.

So, the company got a balanced plan rather than a conservative plan, ambitious where success was achievable, tactical where market conditions were unfavourable.

This model is indeed sophisticated, but includes variables that are difficult to measure objectively. There may be independent benchmarks for market share and product quality, but how can we determine the relative strength of a company’s marketing capability?

The model attracted interest from other large corporations, but some wanted to adapt it. Shell wanted to incorporate more qualitative variables and called their amendment of the BAA the Directional Policy Matrix (DPM), a name that seems to be more widely used in strategy textbooks than the original (Figure 1.7).

All these matrices (Growth-share, BAA, DPM) used circles to indicate a product or business unit’s position, with the area of the circle being proportional to sales volume. Most companies who adopted strategic portfolio matrices found that they improved the skills of the managers involved in working with them and the quality of information used in strategy-making.

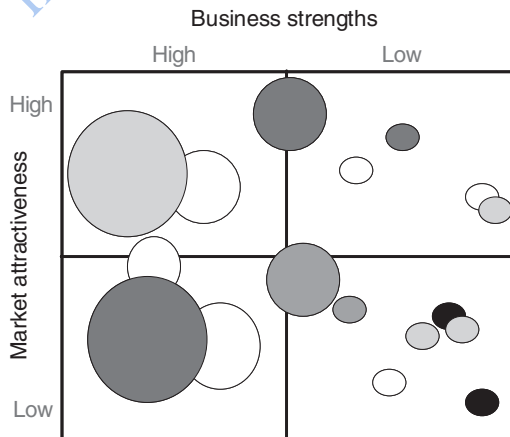


Figure 1.7 A variation on the directional policy matrix. (Adapted from Professor Malcolm McDonald with kind permission.)

They perceive the analysis as far more objective, and the process as far more efficient, than other approaches. At least all assumptions and sources of information are logged so that participants in the process can trace why decisions have been made. Of course, the matrix is only a “snapshot” of the portfolio at a point in time. The positioning of the circles should provoke questions, rather than being a definitive answer.

Of course, the matrix is only a “snapshot” of the portfolio at a point in time. The positioning of the circles should provoke questions, rather than being a definitive answer.

By the 1980s, the DPM was taught in business schools around the world. It was designed for a global conglomerate, and it worked very well at that level. It still needed more adaptation in order to work for smaller companies, or units within large corporations. This is where the customer portfolio became significant.

The development of customer portfolio analysis

Large customers are not necessarily profitable

The Supply Chain Executive Board, a division of the Corporate Executive Board, has analyzed 1.26 million order records from six companies in three industries in an ongoing study of supply chain “costs to serve”.

The least profitable 20% of customers represent only 11% of volume of orders. But these are **large** orders – over 20 times the revenue of the average order – and they generate **large** losses. For every dollar of revenue earned, they reduce profit by 87 cents. A large order from a customer seems attractive, but large orders still cost a lot to fulfill. The implication is that customers who order in large quantities are not necessarily strategic to their supplier.

This research, which is discussed more fully in Chapter 3, is referenced with kind permission of David Evans, Managing Director, Research, The Supply Chain Executive Board.

A division of the Corporate Executive Board.

A provider of business research and executive education based in Washington DC.

(www.sceb.executiveboard.com)

Customer portfolio management was designed to address this sort of problem – challenging the assumption that volume drove profitability. Volume might have been king in the 1950s, but by the 1980s the world economy was a different place, and achieving success was more complex.

In 1982, Renato Fiocca examined the use of portfolio matrices in what were then called “industrial markets”, but we know today as B2B (also incorporating B2G, business-to-government). He suggested that the core for strategic analysis should be the customer. He pointed out that in most industrial markets there are a limited number of important buyers. Buying processes are complex; supply chains have their own power structures and close relationships or partnerships between buyers and sellers are possible.

Fiocca intended that his matrix would help decision-makers in B2B markets to improve profitability because they could allocate resources to the most promising business relationships and withdraw them from others.

In B2B, we are familiar with large customers being referred to as “accounts”. Fiocca called his model the “account portfolio matrix”. The attractiveness of the customer’s business was scored on the vertical axis. The score on the horizontal axis was based on the strength of the relationship between the supplier and the customer.

Customer “attractiveness factors” were about the market in which they operated. Fiocca included market size, the customer’s market share and the customer’s strength compared to their competitors, covering financial strength and their technical skills and intellectual property. The “relative buyer–seller relationship” encapsulated the strength of “our” relationship as supplier to the customer versus the customer’s relationship with competitors. Fiocca included personal friendships and complementary culture as strengths as well as the “share of purse” versus competition, and the number of years that the supplier–customer relationship has been in place.

Since Fiocca created the model presented in Figure 1.8, there have been other modifications and simplifications. In the mid-1990s, I was a researcher in a team led by Professor Malcolm McDonald at Cranfield School of Management working on key account management. We identified Fiocca’s account portfolio analysis as an important tool for distinguishing key accounts from other accounts, but rather than use a nine-cell model we decided to use a four-cell model into which we hybridized some elements of the directional policy matrix.

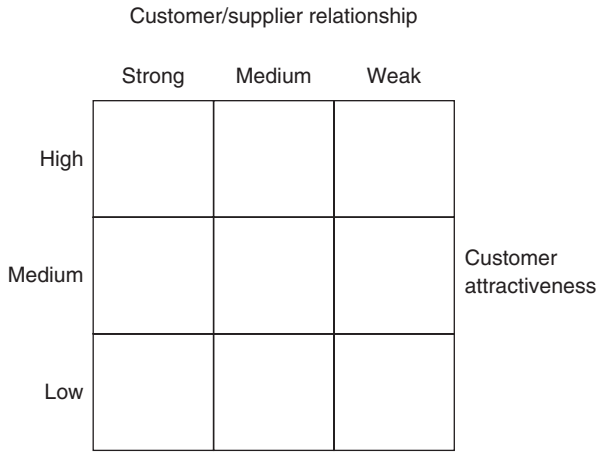


Figure 1.8 Account portfolio analysis. (Adapted from Fiocca, 1982.)

In practice, our model moved further on from Fiocca’s in trying to focus on the relationship between the buyer and the supplier. In my work with small companies and with companies from developing economies in recent years, I have tried to improve its usability even further (Figure 1.9).

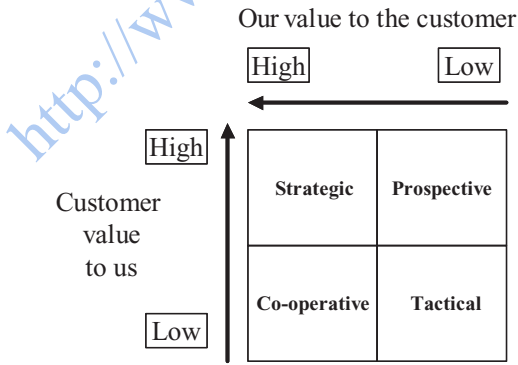


Figure 1.9 The B2B relationship development box.

My research into buyer–seller relationships has usually involved key personnel from the supplier and members of the customer’s buying decision-making unit. There are innumerable examples of senior managers in a

supplier thinking that they are doing very well with a customer when in fact the customer has a less rosy view of their achievements and the quality of the relationship. It is a phenomenon that was identified by Professor Malcolm McDonald as “supplier delusion”. So it is important that the horizontal axis should represent the customer’s point of view.

There are innumerable examples of senior managers in a supplier thinking that they are doing very well with a customer when in fact the customer has a less rosy view of their achievements and the quality of the relationship.

When account managers have asked purchasing managers about how they compare to competitors, it is clear that because all suppliers are expected to be able to meet core expectations of product quality and delivery accuracy for a reasonable price, it is “soft” factors such as accessibility of key staff and problem-solving that distinguish them. True perception of business strengths comes from a customer viewpoint.

Although the research and calculation involved in identifying appropriate factors, weighting and scoring systems can be difficult and time-consuming, there are two main strengths in portfolio approaches.

First, the steps involved in compiling the customer attractiveness scores are more likely to deliver a greater degree of objectivity than models with axes based on single, qualitative or judgmental factors. The requirement to consult the customer about their rating of “our business strengths” (versus competitors) can also be a contribution to objectivity, which should lead to better decisions about resource allocation.

After all, while suppliers are looking out to their customers from the inside, those same customer organizations have purchasing professionals looking out to their suppliers from the inside, analyzing them and making judgments about them. Chapter 2 examines their strategic perspective.

The labels for the quadrants of the relationship development box are designed to describe business relationships simply:

- *Strategic*: To describe a relationship as strategic is instantly understandable; it is one where both parties to it anticipate long-term gain.
- *Tactical*: A tactical relationship is instantly recognizable as one where both parties are not investing, but doing mutually advantageous business on a transaction-by-transaction basis, looking for mutual short-term gain.

Where there is a difference in either party's perceptions, more care is required.

- *Cooperative*: If a customer recognizes a supplier's business strengths but potential for business development is limited, the relationship can still be long-lived, but it will not attract significant investment from either side. The relationship is cooperative in that there is some mutual dependence, but it may not necessarily be comfortable or even friendly.
- *Prospective*: If a supplier is targeting a customer or potential customer, but the customer is not yet convinced of the supplier's strengths, the relationship can be described as prospective.

In describing the axes of this model in workshops and classes, I find myself repeating again and again that the vertical axis represents the strategic value of the customer to the supplier, and the horizontal axis represents the strategic value of the supplier to the customer. This way, we can marry the purchasing analysis with customer analysis and form a tool that both buyer and seller can use to describe their relationship at a point in time. It is supposed to be a relationship portfolio analysis rather than an inside-looking-out customer analysis.

In terms of strategy-making, investment focus is in the high/high box. But a healthy supplier needs to spread risk, and generate development activity in the other quadrants at low cost. We will return to the relationship box in Chapter 3, and examine each of the quadrants in Chapters 4 to 7. In the meantime, let's take a look at strategic purchasing: how customers analyze their suppliers.

<http://www.pbookshop.com>