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Strategic Account Management

Segmenting for Growth in Business-to-Business Markets

Strategic Account Management—Segmenting for Growth in Business-to-Business Markets

Profitable growth is an elusive goal for many executives, but particularly in business-to-business (B2B) markets. Companies in these markets, such as industrial companies, experience a plateau in organic revenue growth, leaving many to believe that they can only grow through acquisition. The leaders of these companies often find themselves focusing sales efforts on capturing enough new business just to offset lost revenue. The reality, though, is that these companies can grow—and grow profitably—by allocating critical sales resources to the right customers.

Profitable growth requires that a B2B company continually strengthen its ability to serve its customers effectively and efficiently. It must assess its customers, considering key factors such as opportunity, volume, profitability, share of wallet, and duration of the relationship. It must formally recognize that, although all customers are important, some are more important than others. In fact, for most companies it is impractical—if not impossible—to serve all customers at the same level. This concept is central to Strategic Account Management (SAM). Companies employ SAM to preserve and grow those customer relationships that are critical to their firm's future financial success.

The sales organizations of B2B companies typically try to manage their customers based on customer size, customer industry, product line, or geography. This approach generally promotes the belief that there exists an equal opportunity for success with any customer. As a result, B2B companies, particularly industrial companies, often employ a simple customer segmentation methodology like the one provided in Figure 1. This example illustrates how a manufacturer distributes product through independent agents ("Reps") as well as a company as owned sales force.

Example Segmentation

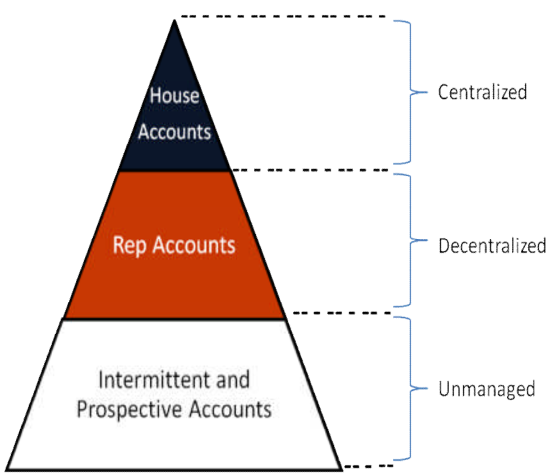


Figure 1: Customer Segmentation for Industrial Manufacturer

In this typical example, customers are segmented to fit the sales force. Unfortunately, this structure often fails to account for the value of each account. The fact that all customers offer varying levels of profit and growth opportunity must be incorporated into a company's sales strategy. Segmenting companies based on value provides the focus necessary to properly deploy SAM.

Customer Segmentation

The process of customer segmentation involves dividing a market into discrete customer groups that share similar qualities. Through segmentation, companies learn the key needs and behaviors of their customers and can respond accordingly. More importantly, they are able to identify underserved customer segments that can be exploited for growth.

Through segmentation, companies can tailor their offerings to segments that are the most profitable and serve them in a way that provides a distinct advantage over competitors. This prioritization is often used to develop marketing campaigns and pricing strategies. A company can also use customer segmentation as the principal basis for allocating product development, marketing, sales, and service resources.

Customer segmentation is often performed along one or more of the following behavioral-related dimensions: demographics, buying behavior, decision-making patterns, and end use of the product/service. These dimensions provide insights into customer buying behavior to increase account penetration and improve account profitability.

Behavioral segmentation, though, may provide limited insight for some B2B markets. Customer buying patterns in these markets are often dominated by two factors: price and service. In other words, all customers share common buying behaviors. Therefore companies in these markets are better served to segment customers along additional dimensions.

If buying behaviors are similar across customers for a B2B company, it may be more appropriate to segment customers based on financial dimensions. Specifically, customers may be segmented based on multiple dimensions that indicate their current and potential value to the company.

These dimensions can include:

- revenue realized (current an potential) from the account,
- profit contribution (current and potential) of the account
- volume and seasonality,
- fit with distribution network,
- fit with the company's long-term objectives and,
- interest in developing a long term business relationship

It is important to note that current revenue should not be the sole dimension for segmentation. By expanding this segmentation to other factors, companies can identify the largest, most profitable customers that hold the key to future growth.

Consider the example of a mid-sized industrial company with a sales force organized by geography. Within its primary market, the company has 350 sales executives aligned by geography. The first segment includes 150 "Corporate" accounts. These accounts are managed centrally by the company's main office because they cross multiple sales territories. Another 4,000 "Field" accounts are managed by regional sales executives. The responsibility for Field accounts is defined by the geography of the customer. Finally, there is a third segment comprised of 29,350 "Unmanaged" accounts. The sales activity on Unmanaged accounts is sporadic and infrequent. No sales executive has been assigned to serve these accounts, either because they are deemed too small or they purchase too infrequently. This segmentation is outlined in Figure 2.

At first glance, this geographic segmentation and the related sales staffing appear fairly balanced. Each Corporate sales executive is responsible for 10 accounts while a Field sales executive is responsible for a comparable 12 accounts. An imbalance becomes evident, though, when examining the revenue realized within each segment. The 15 Corporate sales executives are responsible for $920MM of the company's sales. The 335 Field sales managers, on the other hand account for only $735MM of revenue. A small fraction of revenue, $20MM, is generated from Unmanaged accounts. It is clear that Corporate sales executives, although responsible for slightly fewer accounts, have a much greater revenue responsibility. Although the two sales groups have the same tools and means to serve their accounts, the current segmentation has created a significant imbalance in sales coverage between the two groups.

Cleary, Corporate accounts provide the greatest source of revenue and, potentially, the greatest profit potential. On the other hand, Field accounts tend to be much smaller in nature, yet they receive the same level of attention as the Corporate accounts. Although the geographic segmentation in this example has merit, there exists an opportunity to segment by an additional dimension—value. It appears that this industrial company can achieve much greater leverage from its sales force by revisiting the existing segmentation and realigning the sales force accordingly. Higher value accounts warrant greater sales coverage than lower value accounts.

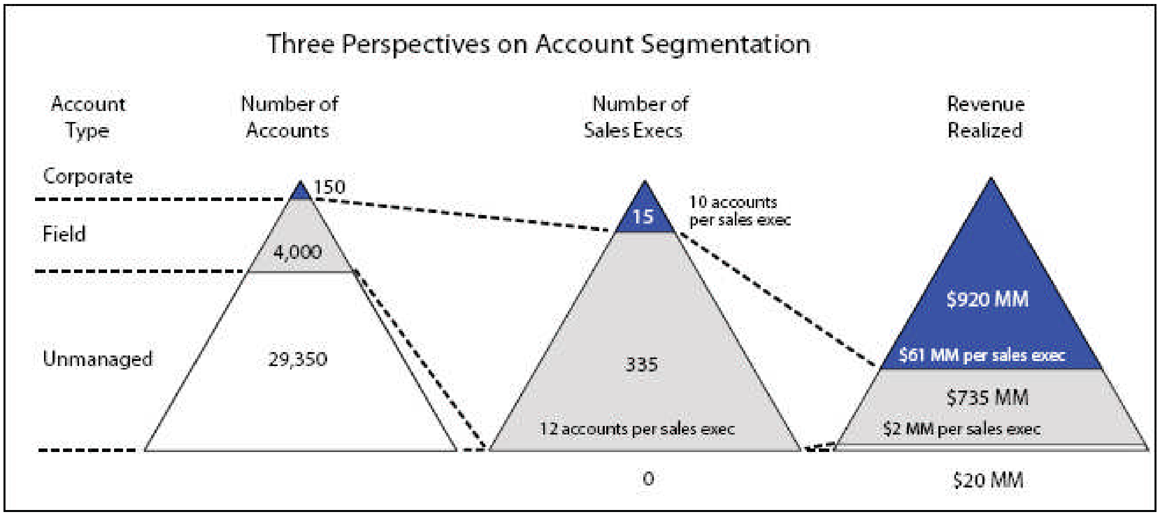


Figure 2: Example Segmentation of Customer Portfolio for Industrial Company

Meeting the needs of the largest, most important customers requires a new customer interface and account management paradigm—Strategic Account Management (SAM). Strategic accounts are those customers which provide significant revenue and/or profit and hold the potential for substantial levels of revenue and profit in the future. These customers are key to the future growth and prosperity of a company because of the volume and stability of their purchases, the size of their revenue stream, their profitability and fit within the company's operating model, and their potential for growth.

Additionally, strategic accounts are those accounts that desire long term business relationships with the supplying company and value the quality of service provided. Strategic accounts do not select providers based solely on price. They recognize the importance of the capabilities of the people, the dependability of the products and services, and the ethics and culture that underpin relationships to be built with the supplying company. Such accounts will respond to a company's product and service offering by increasing their share of spending, expanding their business relationships and loyalty, and providing a basis for more profitable business. A SAM program must be more than a re-segmenting of customer accounts. It must be designed around customer needs to maximize the interface with the strategic customers. The following are a few of the most significant imperatives of the SAM business model:

- Proactively work to ensure delivery of quality products and services that strategic accounts expect and that will position the supplying com pany as their preferred provider.

- Provide outstanding support for customer ser vice, pricing, contract negotiation, issue resolution, performance reporting, and other customer-facing functions through a central, easily accessible, point of contact.

- Hold sales executives accountable for achiev ing revenue, profit, and customer satisfaction objectives for all strategic accounts.

In Figure 3, the customer segments of the original example are redrawn based on value. In this example, margins are assumed constant across segments. Therefore, the value of each account can be attributed to the revenue realized from that customer. This revised segmentation seeks to create greater sales leverage. The five segments, or tiers, for this example are explained below:

Tier I – These accounts provide a significant portion of a company's total revenue and business volume and hold great potential for growth and increased profit contribution. This segment consists of the largest and/or highest potential accounts for the company and occupy the very top of the customer segmentation pyramid.

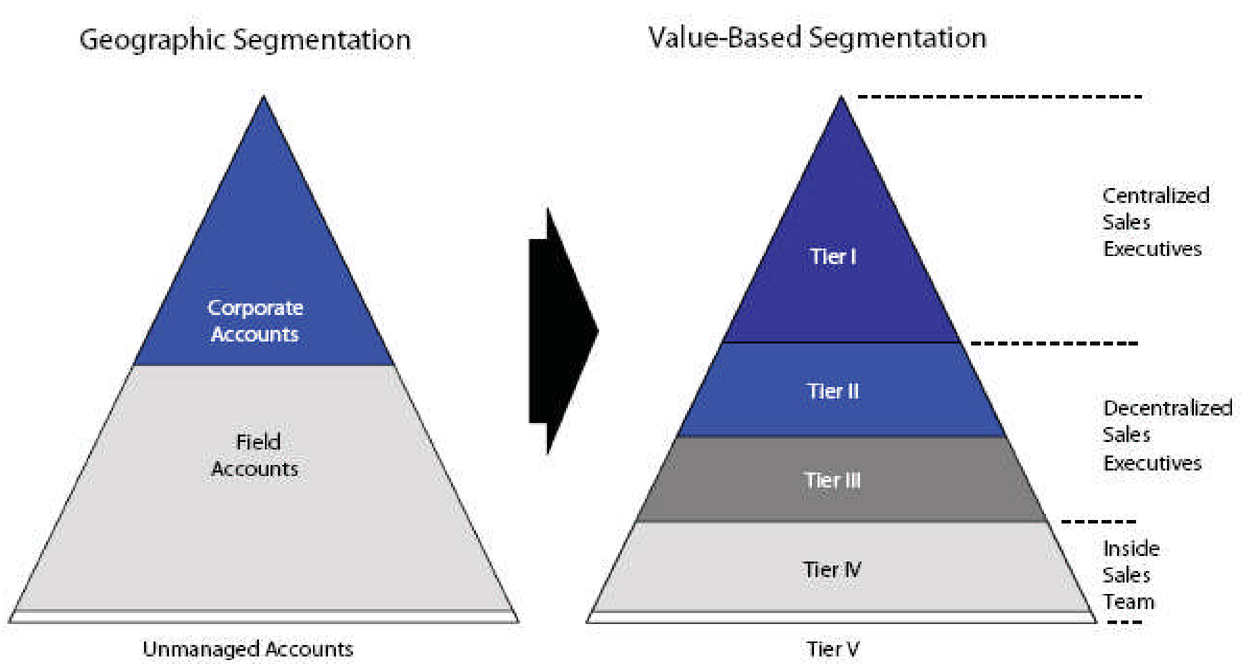


Figure 3: Re-segmenting Customers Based on Value

Tier II – The next largest and/or highest potential accounts for the company are included in this segment. In the example provided, the existing Corporate accounts would be considered for selection as a Tier II account. Similarly, some Local accounts may be promoted to Tier II based on their value.

Tier III – This segment includes the largest Field accounts, as well as any former Corporate accounts that did not fall into Tiers I or II. These accounts require personal service, but are small enough to warrant a higher accounts/sale executive ratio.

Tier IV – Managing the smallest accounts with dedicated sales executives proves to be too costly. Therefore, the accounts in Tier IV can be managed more cost effectively by phone. For these customers, a new Inside Sales group should be formed. Inside Sales executives work as outbound telemarketers to increase contact with the smallest (by revenue realized) accounts. Inside sales executives can contact many more accounts than could a sales executive in the original geographic structure.

Tier V – Unmanaged accounts will continue to provide some level of revenue. These customers will call the company on an as-needed basis for its products and services. Inside Sales executives will serve these customers, in addition to their Tier IV customers. Tier IV accounts are proactive in nature (Inside Sales executives call on a scheduled basis), whereas Tier V accounts are reactive in nature (Inside Sales executives respond to customer inquiries and sales requests).

It is important to note that although revenue is used to approximate value in the initial segmentation exercise, it is not the sole attribute for segmentation. Attributes such as account potential, profitability, product line, cultural fit, and others noted previously are also important to the selection process. In fact, some accounts may be targeted as Tier I accounts that do little or no business with the company today.

Account progression is another important factor to consider. Over time, accounts that grow in revenue and profit should be promoted into the next tier. Similarly, customers whose value diminishes, either by shrinking or failing to keep up with the growth of other accounts in the segment, should be demoted to the next lowest segment. Account segmentation is dynamic, and customer accounts should move up and down in the pyramid over time.

Benefits of Strategic Account Management

Strategic Account Management provides a means for companies in B2B markets to grow profitably. This is accomplished by strengthening relationships with the largest, most profitable customers to win a larger share of their share of wallet. Share of wallet represents the percentage of a customer's requirements that were filled by the supplying company. Similarly, these same B2B companies must earn the business of other high potential customers to continue to fuel growth. SAM addresses these imperatives by providing greater leverage of the sales force for the most valuable accounts. B2B customers are continually managing their supplier base to concentrate their spend with a few, select vendors. The purpose of this strategic sourcing activity is to achieve preferred pricing as well as to simplify vendor interaction. SAM helps companies respond to this by ensuring that sales executives are managing the profitability of strategic accounts. Sales executives should have a complete view of each customer's business, and the associated costs to serve, to develop appropriate pricing levels. Further, this provides an excellent opportunity to become the preferred provider with a sustainable competitive advantage with the potential for greater levels of account penetration and profitability.

Customers in B2B markets also want to ensure they have responsive suppliers who can provide a simple service interface and access to decision makers. SAM provides for a higher level of sales executive contact to service top-tier accounts, making it easier for the customer to do business with the supplying company. Similarly, smaller accounts have centralized support via the inside sales organization. In this way, they have immediate access to a sales executive as needed.

Because of the increased level of contact for top tier accounts, SAM promotes greater customer loyalty through more personalized service. This customer loyalty can pay dividends through significant year-over- year growth potential and increased account penetration. Increased contact also drives a much greater understanding of the customer's goals and requirements. This knowledge is critical not only to day-to-day management of top customers, but also to defining future products and services.

Finally, SAM improves the sales executive's ability to manage account profitability on and account-by-account basis. By providing greater coverage to larger accounts, sales executives have the wherewithal to focus on profitability as well as revenue. Enabling this focus strengthens a company's ability to manage its most complex accounts and improve the profits realized from those accounts.

Conclusion

Profitable growth is difficult in B2B markets, but it is very achievable. Key to this growth is the assurance that critical resources are dedicated to strategic accounts. By recognizing that some customers are more valuable than others, B2B companies can design a program for growth around the highest value, highest potential customers. Through Strategic Account Management, B2B companies can segment their customers by value, and realign their sales force accordingly.

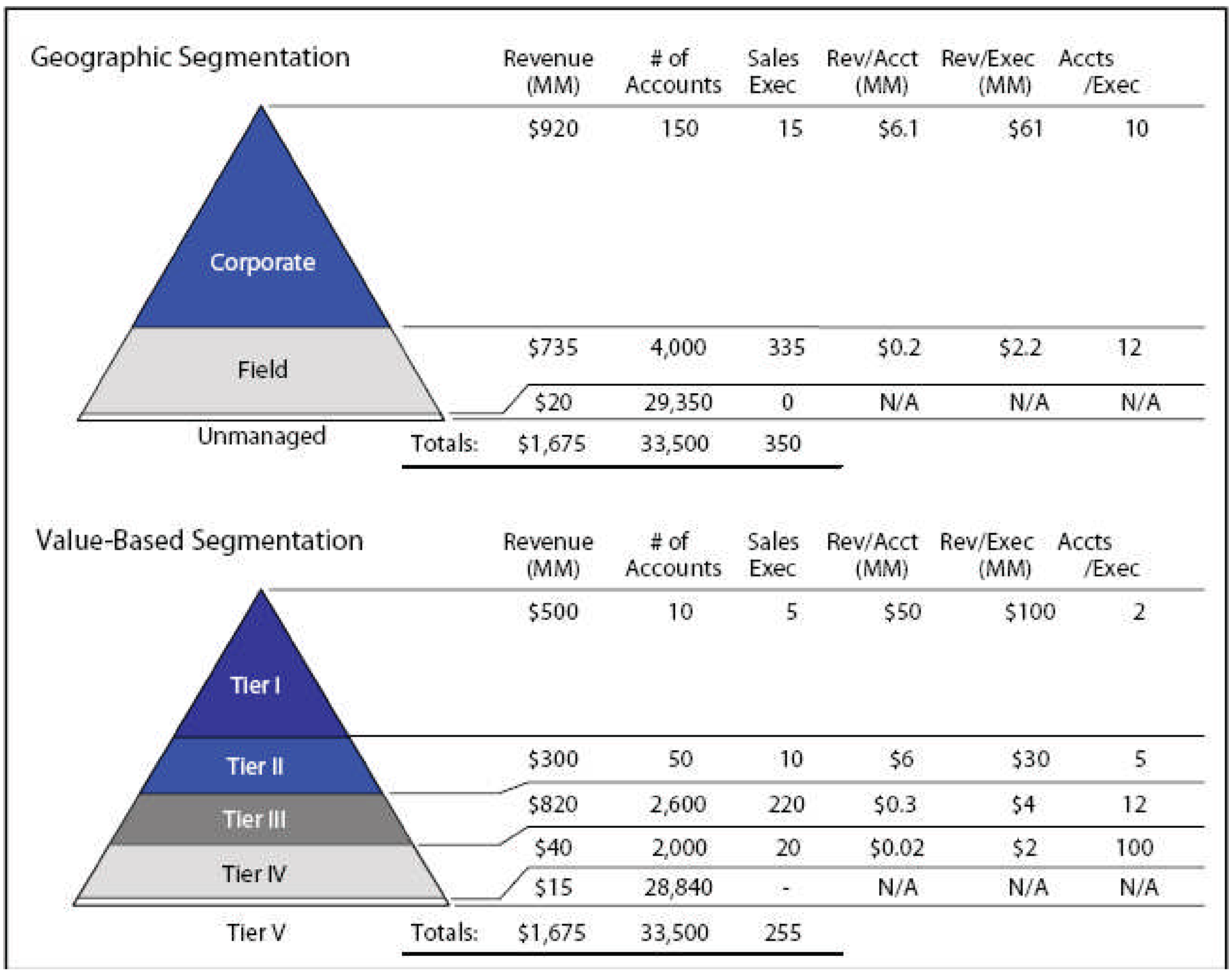
Benefit Summary

Category	Anticipated Impact
Revenue Growth	$ 10.0 MM
Margin Improvement	$ 5.0 MM
Cost Reduction	$ 7.1 MM
Total	$ 22.1 MM

Table 1: Applying SAM to the Example Company

Case Study

The implementation of SAM at a mid-sized industrial company has been discussed through-out this document. The SAM concept was introduced in an effort to realign the sales force to address its issues with profitability and revenue growth. The financial impact of this realignment is quantified here. A summary of these results can be viewed in Table 1. The example company discussed earlier suffered from marginal profitability and experienced virtually no growth for four consecutive years. The company's legacy sales strategy and organization had existed for years with little refinement. As illustrated originally in Figure 1, the sales force was largely aligned by geography. Sales territories were defined in such a way that the sales force was staffed equally in each territory. Sales executives were man



Geographic Segmentation	Revenue (MM)	# of Accounts	Sales Exec	Rev/Acct (MM)	Rev/Exec (MM)	Accts /Exec
Corporate	$920	150	15	$6.1	$61	10
Field	$735	4,000	335	$0.2	$2.2	12
Unmanaged	$20	29,350	0	N/A	N/A	N/A
Totals:	$1,675	33,500	350			

Value-Based Segmentation	Revenue (MM)	# of Accounts	Sales Exec	Rev/Acct (MM)	Rev/Exec (MM)	Accts /Exec
Tier I	$500	10	5	$50	$100	2
Tier II	$300	50	10	$6	$30	5
Tier III	$820	2,600	220	$0.3	$4	12
Tier IV	$40	2,000	20	$0.02	$2	100
Tier V	$15	28,840	-	N/A	N/A	N/A
Totals:	$1,675	33,500	255			

Figure 4: Applying SAM to the Example Company

aged against sales plans and targets, knew actual sales volumes, and generally knew their customers well. However, they had little information concerning customer profitability or share of wallet and were not focused on any particular market, customer group, or segment. Within the selling company's primary market, the customer portfolio was re-segmented based on value. This segmentation provided the means to realign the sales force around customer value. This realignment is summarized in Figure 4.

A number of financial benefits were expected from this realignment. They are quantified below.

Revenue Growth

One of the drivers for instituting SAM was the expectation of increased revenue. This growth was expected within each segment due to improved sales executive leverage. However, to ensure a conservative business case, only growth within Tier I was quantified. By surveying the executives within the strategic accounts, it became evident that the SAM model would drive revenue growth of 100% for Tier I accounts. Most of the revenue growth was anticipated from improved share of wallet for strategic accounts. For many strategic accounts in this example, the supplying company had just a fraction of their customers' total business, indicating that share of wallet improvement could exceed expectations. In some instances, share of wallet could increase ten-fold or more.

Assuming 100% revenue growth on strategic accounts, an incremental $500MM revenue would be realized over time. The existing Tier I accounts provide a 2% profit margin. If the margin on these accounts is held constant during this growth, the incremental revenue would contribute $10MM annually in incremental profit.

Margin Improvement

Implementation of SAM also improves strategic account margin. Dedicating more resources to a customer allows the supplying company to gain insights into each customer's needs. In turn, they can respond more quickly and efficiently to customer concerns, capture the customer's most profitable business, achieve better pricing and reduce concessions, and gain knowledge of where and how to improve the mix.

The opportunity to improve profit contribution was anticipated to be 25% or greater for strategic accounts. This would increase the contribution margin on these accounts by 0.5 points. This incremental contribution, applied to $1B of Tier I revenue, results in an incremental $5MM annually in incremental profit.

Cost Reduction

Realignment of the sales force around SAM created greater sales coverage at each tier. In fact, it became evident during the realignment that the Field sales executives were spending a disproportionate amount of time on lower value accounts. Creating an inside sales organization to manage the large number of low-value accounts reduced the workload on the original Field sales force. The total number of accounts served by this group was reduced from 4,000 to 2,600. Importantly, the value of these accounts increased from $735MM to $820MM.

Holding each Tier III sales executive responsible for the same number of accounts as in the original model, 12 per executive, reduced the number of sales executives required. The sales force could be reduced by 115 sales executives - from 335 Field sales executives to 220 Tier III sales executives. 20 of these sales executives would be redeployed to Inside Sales, for a total net reduction of 95 sales executives. Assuming an average salary and benefits cost of $75,000 per year per executive, a reduction of 95 executives creates a savings of $7.1MM annually.

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