THE TYRANNY OF KEY ACCOUNTS: WHY THEY'RE NOT ALWAYS A GOOD THING

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In this article, Gerry Katz discusses one of the most common traps in all of New Product Development: the conflict between responsiveness to your biggest and most important customers versus the need to address the wider needs of the market-at-large. Katz observes that, in too many cases, companies' product development pipelines are clogged with projects to develop custom products for key accounts, and that this diverts time, attention, and resources from longer term projects that might result in far more innovative and profitable products. At the conclusion, he offers a sobering set of recommendations to avoid this trap.

There is a long-standing joke in our office that goes something like this: *"What is the opposite of the Voice of the Customer? It's the Voice of the Loudest Sales Rep!"*

Whenever I tell this joke to clients, the reaction is always a knowing glance and nervous laughter, because they recognize the situation immediately: a sales representative with a large, important account who bangs their fist on the table and insists, "Well, MY customer says we need to do such-and-such, and if we do, they'll buy a gazillion units."

This phenomenon is perfectly logical. Any sales rep with a large, important account knows that it's the rep's job to advocate for that account, to represent their interests, and to keep them happy. Much is at stake for all concerned.

Companies pride themselves on these customers: the key accounts, the A-listers, the gold-level customers. I refer to them as the "usual suspects." These are your company's largest, most important customers—the ones who are singled out for special treatment and handled with kid gloves. They will almost always be assigned to one of the company's best and most experienced sales reps, and the relationships often include multiple higher-ups—even the CEO. They will demand and receive favorable pricing and favorable terms. They will get great service. And most significantly, they will be blessed with the ability to demand and receive customized products and services.

We use a special vocabulary to describe these relationships. We talk about partnerships, joint ventures, and co-development projects. Deep in our psyches, we tend to think of these relationships in the same way we describe committed personal relationships: as marriages.

There are good reasons to do so.

- These customers purchase a large volume of products and services, thus covering a large portion of fixed costs, e.g., plant capacity, people resources, etc.
- Most key accounts are willing to—and in fact, want to—sign multiyear contracts, to lock in high volumes and favorable pricing for several years.
- These relationships carry prestige, offering a significant public-relations opportunity that can help gain other accounts.
- And don't forget about the money: juicy commissions, bonuses, or even stock options for all those involved.

Along with these obvious benefits, however, are some significant downsides.

- A higher level of service means a higher cost to service.
- Favorable pricing means smaller margins, sometimes razor-thin.
- Greater management attention means diverting attention from other accounts that may have far greater upside potential.
- If the customer pulls back from or terminates the relationship, companies may be left with expensive, unused plant capacity and other fixed costs to absorb.

Rajesh Chandy of the London Business School refers to this phenomenon as "the tyranny of powerful customers."

In my experience, the most critical problem with key accounts is their impact on new product development. In more than half the companies I deal with, almost every new development project is a custom product for just one key account. There is always hope that the product will be appealing to others as well, but it rarely works out that way. This can be a huge trap, keeping companies from giving enough attention to other products, especially general-use and major next-generation products. In essence, the key accounts suck all the air out of the room.

> *"...key account relationships are not a marriage: companies don't sign on "for better or for worse."*

This same phenomenon is at work in Clayton Christensen's theory of disruptive innovation. In both his original paper on the subject and his groundbreaking book, *The Innovator's Dilemma*[1], Christensen describes a chronology that goes something like this (paraphrased):

> *Gargantuan Corporation, a major OEM, has several key accounts that purchase large volumes of their products, primarily because they are superior on attributes A, B, and C, which these accounts highly value. But Upstart Corporation, a potential supplier to Gargantuan, creates a product with a new technology that makes it superior on attribute D, to which no one else has paid much attention. Upstart's product is actually quite inferior on attributes A, B, and C, but they have chosen a different dimension on which to compete.*
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> *Upstart visits Gargantuan to discuss licensing or incorporating their new product into Gargantuan's product. But Gargantuan either rejects Upstart's product, or perhaps, takes it to several key accounts for input, and they summarily reject it. They are not interested in a product that emphasizes attribute D; Gargantuan's key accounts are perfectly happy with their current products that are superior on attributes A, B, and C.*
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> *Eventually, Upstart gains a toehold when they find a few customers who value attribute D. They continue improving their product's performance on attributes A, B, and C, ultimately achieving parity with Gargantuan. Now they can compete for Gargantuan's customers. Meanwhile, because Gargantuan devoted most of its resources to servicing key accounts, it is caught flat-footed on attribute D. But now it's too late to join the party. Upstart has disrupted the market.*

Not every new technology disrupts the market. Some simply improve performance on one or more of the existing key attributes (A, B, and C). Others may be designed to address a different need (say, E), but a significant-enough niche that values that attribute is never found.

If you are lucky and smart enough to identify your "attribute D," you might be in a position to disrupt the market. But it's unlikely you discovered that attribute from any of your key accounts. After all, the reason they are your key accounts is that you already address their most important needs better than your competition.

PUTTING AN END TO THE TYRANNY

Escaping the tyranny of key accounts may feel like bad news initially, but there is a silver lining: the freedom to develop next-generation products. The following example is a case in point.

> *In the late 1990s, GE Lighting was the dominant supplier of standard light bulbs at Home Depot. Then almost overnight, they lost the account, at enormous cost. But with 15 years of hindsight, losing the Home Depot account might have been a blessing in disguise. GE focused its attention on emerging lighting technologies—technologies that the market now embraces, for both their greater energy efficiency and longer life. The market has transitioned from incandescent bulbs to compact fluorescents to LEDs, where the margins are several times those of the old incandescent bulbs. GE's initial loss, therefore, turned into a tremendous gain.*

So how do we end the tyranny of key accounts?

1. Carefully review your key accounts. When all the associated costs are loaded in—the thin margins, the cost to service, and especially, the impact on other needed activities—chances are you'll find that some are worth it, but many are not.

2. When you conduct your Voice of the Customer research, don't just talk to the usual suspects. You talk to these people every day, and the odds are, you're already addressing their needs quite well. Instead, talk to a broad cross-section of customers in the market: large and small, yours and your competitors', current and ex-customers, etc. According to Edward

McQuarrie in his book, Customer Visits, "Your most rapid expansion of sales might come from visiting and learning from customers who aren't buying very much from you today."[2]

3. Consider separating your new product development organization into two separate units: one that deals with custom products for key accounts, and one that deals with more general-purpose, next-generation products. Don't let key accounts hijack your entire product development process.

4. Learn to say no. You are not married to your key accounts, and they are not married to you. These are businesses. If they are not willing to help you be successful, why should you fall all over yourself to help them?

CONCLUSION

Despite the easy comparisons, key account relationships are not a marriage: companies don't sign on "for better or for worse." But key accounts do represent strong mutual commitments—cohabitation, if you will. The only way living together works is if both parties share the shopping, the housekeeping responsibilities, and the expenses—and if it's not good for both of you, it's not good for either of you. For many key accounts, it may be time to move out!

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[1] Christensen, Clayton M. (1997). *The Innovator's Dilemma: When New Technologies Cause Great Firms to Fail.* Boston, Massachusetts: Harvard Business School Press.

[2] McQuarrie, Edward F. (1993). *Customer Visits: Building a Better Market Focus.* Newbury Park, CA: Sage Publications.

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ABOUT APPLIED MARKETING SCIENCE

Applied Marketing Science (AMS) helps companies apply the Voice of the Customer and other techniques to create innovative products and distinctive customer experiences. From early-stage exploratory research to pre-launch pricing and positioning we deliver actionable Voice of the Customer insights that lead to increased innovation success rates and measurable improvements in customer service and satisfaction. Founded in 1989 with roots in the MIT Sloan School of Management, AMS offers an array of services to help clients uncover customer insights to guide important business decisions.