

Ensuring Segmentation Has Bottom-Line Impact

Practice #4

Customer Intimacy Protocols



- **Company Profiled:** Air Products and Chemicals, Inc.
- **2003 Revenue:** \$6.3 billion
- **2003 Employees:** 18,500

Situation

Air Products and Chemicals Electronics Businesses is faced with an extreme form of customer consolidation, as only 2% of its clients (20 customers) drive 80% of its revenues. Furthermore, the top 20 customers use a broad and diverse portfolio of Air Products' products, rendering product portfolio prioritization difficult as the most important customers often purchase a broad range of products, including low-margin products. The severity of customer consolidation and the breadth of its product offering create two primary difficulties for the firm: first, they complicate the Electronics Business's efforts to rationalize its product portfolio, and second, the rapidly changing nature of the electronics industry means even large customers change their technology and investment plans quickly, rendering it difficult for Air Products to place technology bets of its own that will position it for the long run.

Action

Air Products' Electronics Business segments its top 20 customers by profitability, innovation potential, and share of wallet to ensure that, even within its most strategic customers, it is allocating its resources efficiently. Upon identifying a handful (three to five) of its most strategic customers that are truly innovative within their respective industries, Air Products embeds staff across multiple touch points and in many cases forges co-development projects to design innovative products. Using feedback from these key customers, Air Products analyzes its product portfolio and migrates unprofitable and lower-value products out of its portfolio or toward better profitability and adds innovative products that customers value more highly.

Result

Through its customer intimacy strategy, Air Products gains market share with one-fourth of its most strategic customers while increasing revenue from 90% of them. Additionally, by using its key customers to drive its product portfolio review, the firm eliminates numerous unprofitable products while fixing the economics on previously unprofitable products that its top customers value highly.

Segmenting an Already Concentrated Group

With 80% of its revenue coming from only 20 of its 1,000 customers, Air Products and Chemicals' Electronics Businesses recognizes a need to serve its top 20 customers with special care. That said, the firm also realizes that even within this tremendously concentrated customer segment, the top 20 customers have varying levels of strategic importance. The firm plots all 20 customers against one another based on profitability, innovation and growth potential, and Air Products' share of wallet. Through this analysis, Air Products identifies various sub-segments of customers within its top 20 that warrant different engagement strategies.

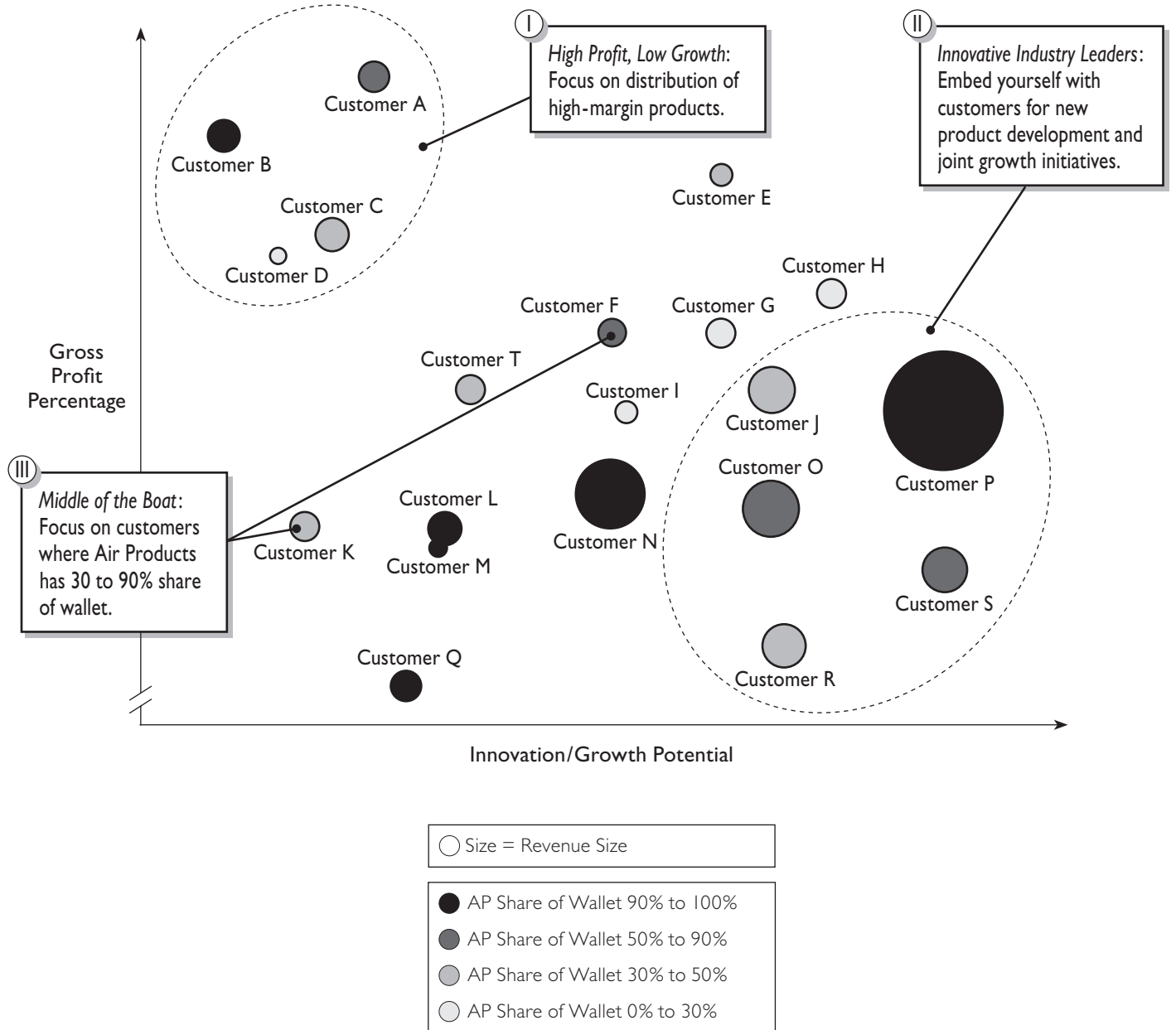
- I. *High Profit, Low Growth*: Despite being the most profitable customers to Air Products, Air Products believes that this group of customers may not be reinvesting to maintain market position. As a result, Air Products focuses efforts on maintaining position with high-margin products to these customers.
- II. *Innovative Industry Leaders*: Even though many of these customers are not as profitable as others in the top 20, Air Products believes that they are leaders in their end markets and will increase their position over time. Air Products believes the key to serving this group is to embed themselves with these customers to learn about which technology bets to place and how to best build products or solutions that will position them as key suppliers in the future. Essentially, Air Products is willing to expend additional effort in joint development and be flexible with key new products to grow with these customers. Growth enables Air Products to improve its cost and infrastructure positions.
- III. *Middle of the Boat*: Rather than focusing on increasing share of wallet with all remaining top customers, Air Products again focuses its resources more precisely. While many firms dedicate their resources toward the customers buying less than 30% of their goods from them (expecting this group to have the most potential for growth), Air Products finds that this effort could be a waste of resources. The firm believes that this group actually has little room for growth due to a buying philosophy that requires them to use multiple suppliers. Rather, Air Products primarily focuses its resources on customers who currently purchase between 30 and 90% of their goods from Air Products. The firm also dedicates necessary resources to keeping the customers that purchase more than 90% of their materials from Air Products satisfied.

A THREE-PRONGED ANALYSIS OF KEY CUSTOMERS

Analysis Suggests Differing Strategy for Various Customer Groups

Air Products and Chemicals' Top 20 Electronics Customers

By Profit, Size, and Share of Wallet



Gaining Intimacy

Upon identifying its most innovative customers, Air Products dedicates a cross-functional, full-time, global account team to serving each of them. Each team is organized around the customer's structure to ensure that Air Products is interacting with the customer across multiple touch points and locations. The teams are managed by a senior team leader who has risen through the ranks of sales, operations, and general management and has the sole responsibility of managing the specific customer account. Team size differs per customer and specifically the number of locations and touch points within each customer organization—larger customers have a team of seven to eight full-time staff, while smaller ones have about three to four.

The basis of all team activities is an agreed upon set of customer opportunities. The opportunities include detailed lists of new products to develop for that customer, product bundles that offer specific customer-defined solutions, and pricing changes for new or existing services that can enhance revenue. All team members are compensated on specific targets linking to the customer opportunity plan and overall account success and growth.

The Team in Action

Two examples of the global account team in action are presented on the opposing page.

- *Embedded R&D Manager:* An Air Products engineer who works full-time on site at customer facilities. The engineer's responsibilities include understanding the technology and product bets the customer is making and identifying potential innovations that Air Products can make to support the customer's product investments.
- *Efficiency SWAT Team:* "SWAT" teams that teach customers how to use Air Products' products more effectively and efficiently. Although increased effectiveness leads to short term revenue losses, the relationship-building effect promotes long-term economic gains from the account.

REACHING OUT TO THE CUSTOMER

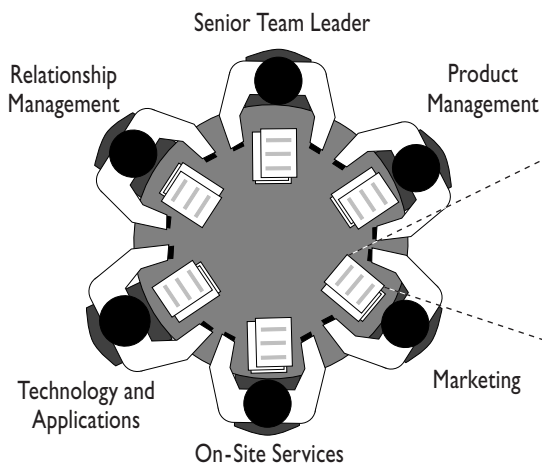
Cross-functional, full-time team devoted to key customers...

Air Products and Chemicals' Focused Account Team

Hypothetical

Focused Account Team

- Full-time cross-functional staff (with additional part-time support) dedicated solely to one customer
- Team organized to touch customer at multiple points and locations across the organization
- Team coordinates all activities against a defined set of customer opportunities (e.g., new product identification, price and service management, solutions opportunities)



Customer Opportunities

New Product Opportunities

Pricing and Service Opportunities

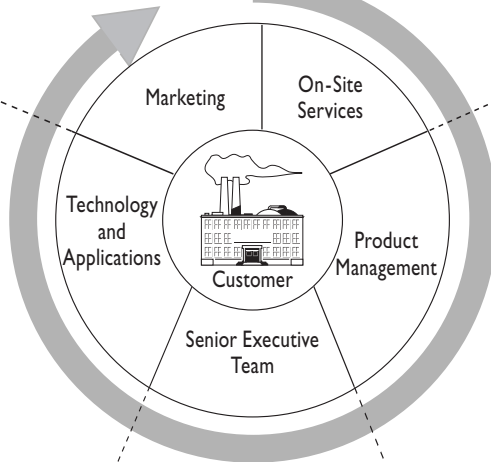
...provides service and collects information across multiple customer "touch points"

Embedded R&D Manager

Air Products embeds a senior R&D manager at customer development site to work on joint projects

KEY QUESTIONS

1. Where is the customer headed?
2. What can Air Products do to help the customer get there?
3. Can Air Products help the customer get where they are headed and apply the solution more broadly to the customer base?



Efficiency SWAT Teams

Customer Operations Team

Air Products' applications teams enhance customers to improve their use of its products and services, thus creating cost savings for the customer

Short-term consumption declines from increased efficiency are off-set by long-term account growth.

Category	Change from Current
Current	0%
Short-Term Effect of Applications Teams	(10%)
Long-Term Effect of Applications Teams	25%

An Innovation Focus

A critical aspect of Air Products' customer-intimacy program is the opportunity to co-develop pioneering products with its most innovative customers. By locating its employees on site at customer locations, Air Products maintains unusual access to innovations and technology bets that its industry-leading customers are making.

Working with innovative customers, Air Products creates technology road maps that outline both current and future product needs and technology trends in its customers' industries. The road maps allow Air Products to predict customer needs in advance of the actual need and develop products to meet them in advance of other suppliers.

Often times, Air Products cannot develop the products internally. Likewise, many of its customers do not maintain the capabilities to do so. As a result, Air Products often joins together with its innovative customers in joint development projects. Through these partnerships the two firms leverage each other's technical capabilities to develop groundbreaking products.

Leveraging the Opportunity

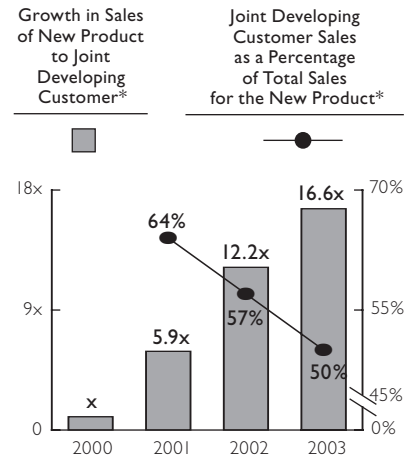
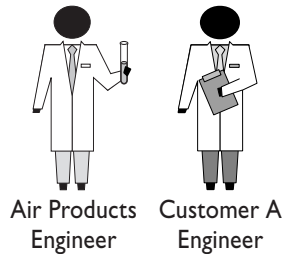
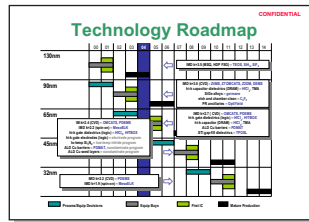
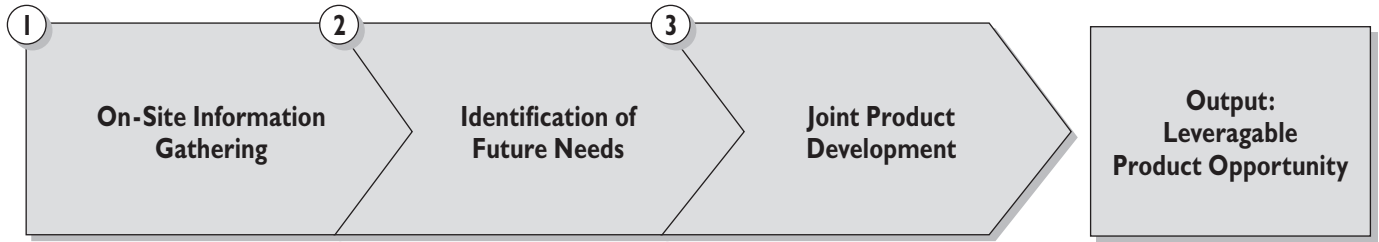
While joint development with a specific customer initially leads to large sales to that customer, Air Products is also successful at leveraging these innovative products to a broader group of customers. For example, while sales of a product the firm co-developed with an industry-leading customer in 2000 have grown by more than 16 times, sales of that product to that customer now represent less than 50% of total sales.

In summary, Air Products uses customer intimacy to embed itself with its most innovative customers, resulting in breakthrough technological development that is ultimately distributed to the broader Air Products customer base.

SPREADING THE WEALTH

Embedding with Innovative Customers Informs Broader Product Development Efforts

Air Products and Chemicals' Intimacy-Led Joint Development Process



- Air Products embeds a network of employees across 80 global customer sites
- Air Products employees at customer sites handle supply of gas and chemicals up to point of use
- Air Products employees attend customer's operational meetings and identify customer problems and needs
- Air Products works closely with thought-leading customers to create road maps of future product needs and technology trends
- Air Products also leverages relationships with customer suppliers (e.g., manufacturing firms) to identify future needs and innovation opportunities
- Leveraging each other's innovation and technical capabilities, Air Products and engineering customers jointly develop new products (often with joint product rights)
- At any given time, Air Products typically has 50 new products in the pipeline for its top 20 customers
- While initial sales to co-developing customers result in large individual account growth, creation of an innovative product often results in significant revenue from other customers

* Numbers portrayed in graphic represent sales to one customer.

Source: Air Products and Chemicals.

A Broad Spectrum of Products

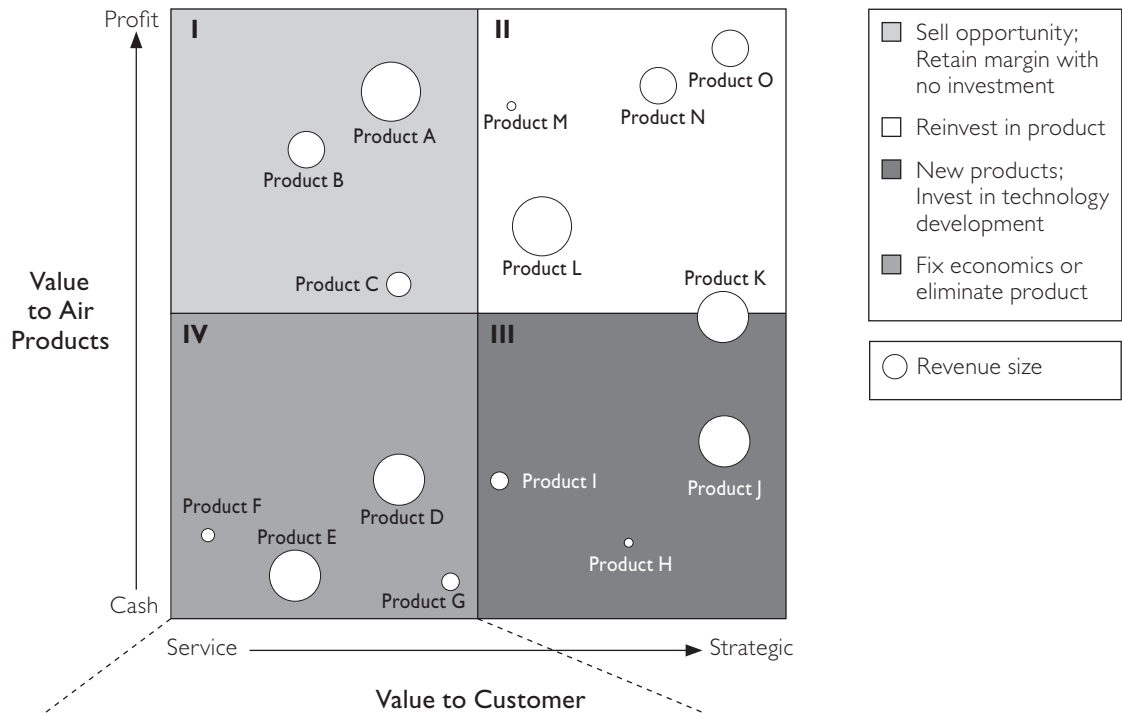
Air Products' top 20 customers use more than products that are spread across the value spectrum, from commodity products to premium products. While Air Products would clearly prefer to focus on premium products, it recognizes that providing a full suite of products to its key customers is too important to simply eliminate commodity products. Rather than simply segmenting products across the value spectrum, the firm segments all products by profit delivered to Air Products and value delivered to the customer. Upon plotting all of its offerings onto a matrix, Air Products determines specific strategies for each quadrant.

- Quadrant I:* These products are very profitable but have little growth potential. Air Products strategy is to continue distribution without making additional investments in them.
- Quadrant II:* These are the “win–win” products that are both profitable and valuable to the customer base. Air Products continues to reinvest in these products given their potential for continued growth.
- Quadrant III:* These are primarily new products or products that have recently received significant investment. Although not yet profitable, these offerings are valuable enough to the customer that Air Products continues to invest while focusing on improving the economics over time.
- Quadrant IV:* These are the products that need to be fixed or eliminated, as they are not valuable to the customer or profitable to Air Products. Air Products' goal for these products is to improve product economics through price increases and new efficiencies. In many cases though, improved economics are not achievable. Rather than simply eliminating such “doomed” products, Air Products uses an additional “impact on the key customer” screen. Air Products finds that in many cases it is important to keep some of these quadrant IV products, as they help fill out a suite of products that is critical to key customers. If this is the case, however, Air Products often attempts to move the products to quadrant I through price increases.

CUSTOMER-FOCUSED PRODUCT PORTFOLIO ANALYSIS

A Holistic Approach to Investigation Sheds Light on Products for Reinvestment and Repositioning

Air Products and Chemicals' Product Portfolio Prioritization Matrix



CONSIDERATIONS BEFORE PRODUCT ELIMINATION

1. Are customers willing to pay more for this product/solution?
2. Can we cut enough costs out of production to enhance product profitability?
3. How does altering or eliminating the product affect our ability to deliver customer solutions?
4. How does altering or eliminating the product affect shared development platforms?
5. Can we price for product-related services (e.g., delivery or containers) to increase margin?

Strong and Growing

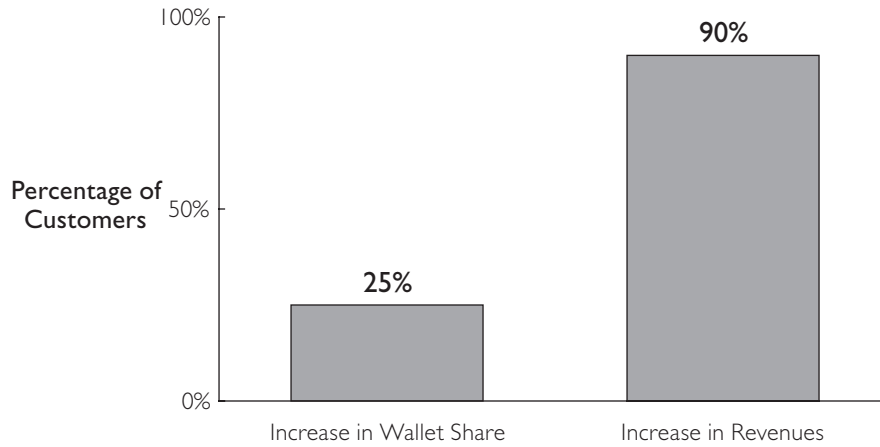
Air Products' segmented approach to its top 20 customers has paid tremendous dividends. The firm has not only increased its price premium with 90% of its key customers, it has also increased wallet share with a quarter of them while maintaining its wallet share with the rest. Customer intimacy helps define real value customers recognize and pay for.

Additionally, Air Products has experienced early successes with its product portfolio prioritization process. To date, the firm has analyzed four products in quadrant IV—two of which had little importance to key customers and were thus eliminated and two of which were kept in the portfolio with improved economics through price increases and supply chain improvements.

GETTING PAID FOR VALUE DELIVERED

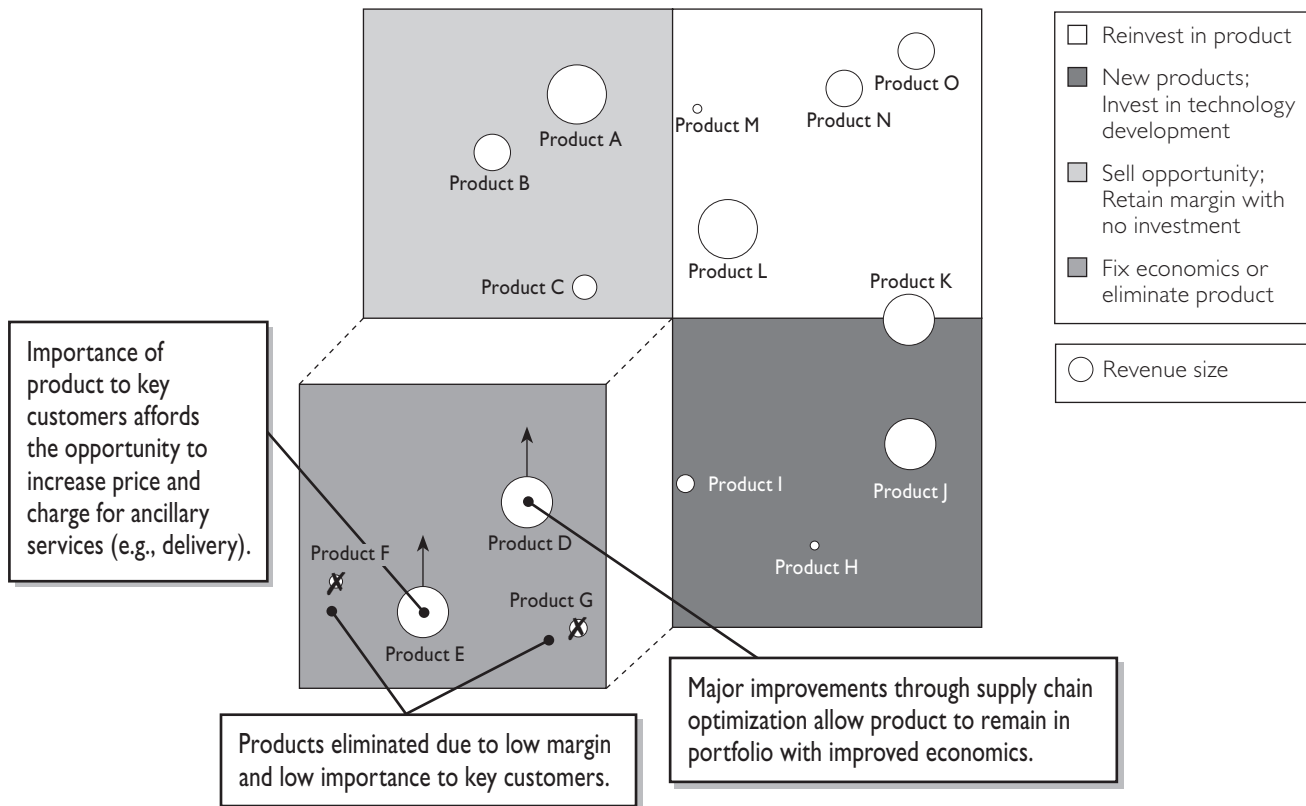
The segment approach to top customers has driven increases in premiums...

Changes in Wallet Share and Revenues of Top 20 Customers*



...while the product analysis has resulted in improved performance of specific products

Product Portfolio Prioritization Matrix Revisited



* Results are for a specific product in the Air Products portfolio.

Source: Air Products and Chemicals.