- JAMES HASHEM
- DIAGNOSTIC INSTRUMENT
- ROB RODIN
- MARSHALL INDUSTRIES

Customer Intimacy

Pick Your Partners, Shape Your Culture, Win Together

Fred Wiersema

THE NEW YORK TIMES Bestselling Coauthor of The Discipline of Market Leaders confidence as they grow, the lines of distinction between them grow blurry, as if the two were different aspects of a single organization, jointly pursuing mutual success.

Look, for example, at the relationship between Marshall Industries, the giant electronics distributor, and contract manufacturer Diagnostic Instrument, one of Marshall's larger accounts. An outsider would be hard-pressed to tell where one company ends and the other begins. The two companies sell together. They forecast together. They've abolished separate purchase orders, bills, invoices, and accounting. They use software that links the two of them, allowing them to run their consigned material system jointly. The Marshall's account rep even sits in on Diagnostic's purchasing meetings. "We kid him all the time that we're going to give him a Diagnostic Instrument time card," Diagnostic's CEO James Hashem says. "We've already given him a desk, a chair, and a telephone, and he's on our E-mail as well as Marshall's. It certainly cuts communication time, and time is money for both of us."

COMMIT, COMMIT, COMMIT

By now it should be clear to you that customer intimacy is not a discipline for the faint of heart. It's less traditional than operational excellence or product leadership. It's more relationship driven, and it focuses uniquely on mutual results with each customer. Conventional-minded managers may find the customer-intimate approach alien—a strange land with radical assumptions and a barely understandable language.

skills let them pursue entirely new ways of doing business together. I could equally well call this third model of partnering "vertical integration without equity." The companies, in practical terms, eliminate the already blurry demarcations between supplier and customer. Each continues to contribute from its strength and expertise, but the form and shape their combined enterprise takes depends on how the newly integrated team best improves the elements of the collaboration. The goal of the partners is to create new value for both of them.

Win Together

Which kind of processes can partners jointly reengineer as they integrate their businesses?

Sales? Forecasting? Purchasing?

Pricing? Inventory? Billing?

Hiring? Training? Cash management?

The answer—for electronics distributor Marshall Industries and contract manufacturer Diagnostic Instrument Corporation—is all of them. When results are all that matter, the only limits to the forms and possibilities of business integration are the limits of the imagination.

Marshall Industries, the nation's fourth largest distributor of electronic components in the U.S., has become customer intimate by necessity. It doesn't sell a unique product; its 10,000 mostly small customers could buy the same supplies from hundreds of other distributors. And it can't compete on price; with so much competition, there is always one who will offer a lower quote. Instead, Marshall sells results: It has led its industry with such innovations as 24-hour service, on-line Internet ordering, and a robotic warehouse that can guarantee 24-hour shipping service.

"We know everybody can sell components," Marshall president and CEO Robert Rodin tells potential customers. "We want to be a virtual distributor allowing customers customized access to our products, services, and information. Any time of the day, from any place on the planet, by any method they choose."

Diagnostic Instrument Corporation, a small player in an equally competitive industry, has become customer intimate, also by necessity. As a high-tech contract manufacturer, it becomes its customer's manufacturing department: Diagnostic takes the designs and specs; it sources, costs, procures, buys, and tests the materials; and finally, it assembles and tests the customer's final product, usually a printed circuit board. With hundreds of contract manufacturers who deliver quality, Diagnostic's ability to compete on speed is a key driver of its success.

"As you try to get closer to your customers you have to get closer to your vendors, aiming for seamless integration among the three of you," Diagnostic's CEO James Hashem says. "The problem is that the typical distributor operates at arm's length, trying to sell each individual product for the most it can, then moving on to the next product and sale."

But Marshall and Diagnostic found a better way that produced dramatically better results for both of them. Three years of integration have helped Diagnostic grow by more than 500 percent, from annual sales of $6 million in 1992 to more than $33 million today. And it has made Diagnostic one of Marshall's significant customers: an $11 million account.

The seed of their integration was planted at a 1992 dinner honoring Marshall as Diagnostic's "Vendor of the Year." A half dozen or so employees from each company sat together into the evening, talking about how far their relationship had progressed during their three years together and where their respective businesses might be going next. For both companies, the problem—and the opportunity—lay in the explosion of subcontracted electronics manufacturing. The potential business for Diagnostic was huge, but with a sales force of only three people, the company was too small to find and capture customers in that growing market. Marshall, in turn, had hundreds of salespeople—25 covering New England alone. Still, subcontracting was creating challenges for Marshall, too. A Marshall salesperson could spend weeks with a prospect's engineering team, specifying parts and assembling information, only to lose the sale when the prospect decided to outsource the work to a contract manufacturer who would choose its own distributor for supply.

That night, the Marshall and Diagnostic people hit on a simple solution. Since Marshall was selling components to customers who often needed assembly work, why not pitch potential customers on the combined capability of their two companies?

But the actual implementation of the joint sales effort was more complicated. Although management at both companies embraced the concept, meeting regularly to push for implementation, the sales teams were slower to sign on. Salespeople, after all, thrive on competition. Learning to collaborate meant a radical change in style as well as a change in commission structure (as we shall see in Chapter 13). As the salespeople talked and trained together—and started to win new business together—they too were eventually convinced that the partnering strategy was the right approach.

The successful joint sales effort brought good feelings to both companies, but it brought a new problem, too. Growing volume at Diagnostic stretched its ability to meet customers' demands. "Our customers demanded very short cycle times from us. Speed to marketplace was their key competitive issue," Hashem explains. "We couldn't do it with traditional purchasing. Sending out for quotes meant it sometimes took us six to eight weeks to answer a customer's questions about availability and cost. But customers need to get their products out quickly, and that means we need to build their prototype quickly.

"Cost is the other major issue," Hashem adds. "Most of the customers we do business with need to lower their costs every six months. So we have to work in a continuous cost-reduction mode, too."

Once again, they met the challenge in partnership, radically reengineering Marshall's way of selling and Diagnostic's materials purchasing.

Diagnostic had always worked with its suppliers in the traditional "pick, pack, and ship" mode: source the inventory, solicit and compare quotes, write the purchase order, sign it, send it, and confirm it. When supplies arrive, log them in. That traditional purchasing system was too slow, too cumbersome, and too costly to meet competitive demands. Delay was inevitable, and overhead was high.

Together the two companies changed their purchasing process. Since most of Diagnostic's orders were already going to Marshall, the partners decided to develop a consigned materials program, making Marshall the Diagnostic vendor of choice.

No longer would they waste time negotiating prices part by part. Instead the two agreed on a uniform pricing formula, which they based on cost and a mutually satisfactory markup.

Management from both companies was eager to try the idea. Both companies first had to persuade the purchasing and sales teams to adopt the new strategy. "The normal buyer is used to going out and getting three prices to make sure to get the lowest," Lori Lucy, Diagnostic's materials manager says. "My argument was that since Marshall was bringing us the customer, Marshall would have every interest in making sure that we are competitive. If we don't win the business, they don't win the business. So it doesn't make sense to spend time and money calling around for better prices."

With prices set, the partners developed a single forecasting system to further speed the process. Each new end customer's monthly forecasts became part of Diagnostic's forecasts, and Diagnostic, in turn, shared its monthly forecasts with Marshall.

With forecasts in place, the two companies established the most visible element of the process redesign: Marshall moved, rent free, into a small space in a Diagnostic building and stocked it with the materials forecasted for use during the coming weeks. They call it the store. Linked to Diagnostic's computer system as a warehouse location and linked to Marshall's main computer in El Monte, California, the store, staffed by a Marshall employee, operates as if it were in a Marshall facility. When Diagnostic employees need parts, the Marshall employee takes care of them.

Operational improvements were immediately impressive. No more FedEx charges for rush shipments. No more delay in answering an end customer's question about, say, delivery dates for extra parts. And, as the partners pushed their redesign, they continued to find new opportunities to improve speed and cut costs.

Purchase orders were the first administrative procedure to go; the partners couldn't justify the overhead costs. Diagnostic had to write them and Marshall had to log them in. They abolished bills for the same reason. Both partners have found it cheaper and faster if Diagnostic runs a list of everything it has taken from the store and forwards it to the accountant for payment.

"Administrative work is where you start saving some money," says Hashem, "and it comes from reducing costs for us both. That means we can reduce costs for our customers and offer better service. It's an absolutely win-win-win situation all the way around."

The partnership even solved Diagnostic's working capital needs. Shut out from additional credit by his bankers, Hashem took his growth plan to Marshall, and the two developed a solution. Marshall extended Diagnostic a line of credit, with payment due in 60 days. Diagnostic, in turn, persuaded its customers to accept a discount in exchange for 10-day payment terms. Having cut the manufacturing cycle time to 4 days and their payment time to 10 days, Diagnostic still had use of the cash for 46 days.

The final change concerned how Marshall's sales staff handles Diagnostic's business. Under the old system, six people had to service the account. With the new consigned materials system in place, one person could easily handle that work. And rather than selling, the salesperson's job now requires sitting with the Diagnostic purchasing group and working to help Diagnostic win the business of its end customer.

"It's a huge dollar savings for them, and it certainly helped us, too," Lori Lucy says. "When we start quoting on jobs and working with customers, Marshall's salesperson is right there. By the time we're actually ready to buy and build the product, we've shaken out the materials problems. We don't have to get on the phone to find something out; somebody lives right here, in plain view. We can go and get anything we need, right on the spot."

Hashem adds, "It cuts overhead for both companies, and gives Marshall a competitive advantage with their other business. Marshall's salesman not only gets to quote every piece of business we do, he gets firsthand information about how the larger market is moving."

This change, too, demanded a major adjustment, Lucy says. "People here worried about putting their salesman inside our purchasing group, where he could see and hear all the details about our business. But I said it didn't matter—we can walk over to his terminal and see everything about his business, too. Who has the time for that? We both have a vested interest in making this work: It's the lowest cost option for both of us. The old mentality—where customers and vendors don't tell each other anything—just doesn't work."

Today the two companies function as one virtual, vertically integrated business, with everyone focused on the same end: better results. Salespeople meet monthly for breakfast to share leads and plan campaigns. Employees from shipping and purchasing departments meet monthly to talk about logistics, looking for still other costs to cut; the MIS staffs meet monthly to improve communications. And senior management meets quarterly, to review the profitability of their thriving partnership and to look for ways to push it forward.

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"We need to understand how well we are doing and how we can continue to drive costs down for both of us," Hashem says. "But we have always been clear that neither of us wants to lower margins by taking it out of profits. They decide how much profit they would like to make. We decide how much we would like to make. Everything else is up for grabs. Maybe we are doing something that costs them overhead. How can we change it? Maybe there is something they can change. We're at the point now where we can ask them if they are making money off of us. I don't know of any other two companies where the customer and the vendor sit down to make sure the vendor is making money. If the business isn't profitable for them, in the long term it's not going to work for either of us."

That, right there, is the essence of partnering.

their connection. In every such meeting I've attended, I've noted the eye-opening frankness and empathy both the supplier and the customers demonstrate.

I recently attended one such session hosted by Staples National Advantage. About a dozen vocal customers created an atmosphere that reminded me of an elite club, with experts vying to share their experiences. I'm convinced everyone left feeling nourished.

Whether such exchanges occur routinely or during special council sessions, open communication at every level of the interface has the additional benefit of reinforcing the trust-building process. Robert Rodin, president and CEO of Marshall Industries, is very direct with his customers: If he's not already on the line, he picks up his own phone to answer incoming calls. Customers are startled the first time, but their surprise quickly gives way to delight. "It's a simple way to stay in touch with randomly chosen customers," says Rodin. "All my management does this as a matter of policy."

Northwestern Mutual Life Insurance takes a more complex approach to demonstrating its concern for customers. That company was among the first to adopt a mission statement—in 1888. Jim Ericson, president and CEO, describes its mission as follows: "Everything that we do—every decision we make—is based on what we think is good both for our customers and our owners." Northwestern is a mutual company, so customers are owners. The company's 7,200 sales agents learn to be skilled listeners, to be contemplative, and never to rush a sale. "I know most people think of insurance agents as people who talk a lot," says Ericson. "But at Northwestern, we focus on drawing customers out." The company stresses warmth, face-to-face communication, and the personal touch.

As Robert E. Carlson, executive vice president, marketing, explains: "A good insurance agent should know more about an individual and/or family than any other professional. A lawyer knows a piece of the story, medical people know a piece, the church materials manager, Diagnostic Instrument Corp., says she does nothing fancy to track success. "I can tell by how well I am able to service my customers. If the machines are always down, and we are always running out of parts, it's not going so well."

Put Customer Performance in Perspective

Customer-intimate companies try to get straight to the point—the other guy's point. Precisely how much did the customer's performance improve as a result of their association? How does that gain compare with its competitors' benchmarks? In many industrial businesses, you can monitor the clients' performances by examining their process performance, cost performance, etc. Nypro, for instance, can more readily quantify the effect it has had on Vistakon's or on Abbott's operations. It assesses those accounts in terms of their product development time: the time it takes to ramp up a production line to deal with, say, unanticipated, rapidly increasing demand.

For a customer-intimate company to determine its specific impact on a customer, and share that information with the customer, is valuable in more ways than one. Within the company, it keeps everyone focused on what is most important—results—while providing the customer with hard, tangible measurements of benefit. In fact, all regular monitoring of the client's business creates a scorecard of results that enhances the meaningfulness of the connection and spurs both parties to higher levels of performance.

For example, because of their intimate connection, Diagnostic Instrument and Marshall Industries collaborate on their forecasting and share information on overhead and cost drivers. Marshall's line of credit allowed Diagnostic to expand, creating greater opportunity for both companies. Such results flow from trust. James F. Hashem, president of Diagnostic, says, "We no longer give Marshall's people reservation system, was the first in the air freight business. "Because time is so important to our customers," he says, "we had to have a way to quote flights. Once the customer has presented us with the problem—the origin and destination cities—we had to find a way to quote a flight within seconds." System-1 provided the way. Without that technology, the company would have been unable to fulfill front-office promises; if it hadn't kept promises, it wouldn't have established trust; and without trust, it would never have established intimacy.

Another illustration: James F. Hashem, president of Diagnostic Instrument, tells us that customers phone to amend their orders. They might say, "I know you promised us 100 printed circuit boards next week, but I could use 125." In the past, he says, "that question used to take us weeks to answer because we would have to go out and see if we could get an extra 25 sets of parts. We would have to visit a bill of materials line by line and check every single part. Because we're keeping Marshall inventory in our Marshall store, we can punch a few keys, and within an hour, our shared computer system gives us an answer to the customers' questions."

Information systems can serve as a consensus builder to create alignment. Everybody has access to the same information; therefore, nobody wastes time reconciling information. Everybody sings from the same hymnal.

Open Up the Font of Learning

Within a customer-intimate company, information technology and systems empower the organization through the learning process. This is hardly front-page news, but in a customer-intimate enterprise, a learning organization par excellence, it's not trivial news, either. The promise, the value proposition, of customer intimacy is the delivery of best results. The better job the company has done

With closer cooperation, both can reduce the costs of maintaining excess, just-in-case, insurance-policy-style inventory.

James F. Hashem, president of Diagnostic Instrument Corporation enthusiastically extols the virtues of his company's relationship with Marshall Industries. "The trust factor is unbelievable. Customer and vendor sit down together to ensure the vendor is making money, a pretty rare and wonderful arrangement. They go into detail: 'What costs you money? What can we do to lower the overhead?'"

Hashem describes how Diagnostic rationalized Marshall's billing system. "Their standard way of operating was to cut an invoice every time a transaction came from their stockroom. They stuck the invoice in an envelope, stamped it, and mailed it to us. My people in accounting were slitting 300 envelopes a week, entering 300 pieces of data into our computer, and tracking all that accounts billable information. My materials manager said, 'This is crazy. Why don't we set up a weekly billing? We'll consolidate all the transactions, summarize them on a computer report, and generate one cover invoice.' Now there's one envelope we have to open, one piece of data we enter into the computer, and one piece of data we have to track. I've gone from $6 million in sales to $33 million in sales and I still have only two people in accounting. That's where you start to make money. It's not coming out of my profit margin or out of Marshall's: It's coming out of our costs. The partnership has been tremendous for our customers because we've been able to lower our cost and offer better service."

Cooperation also allows for improvements in work allocations. Shifting certain tasks from customer to supplier, as several of our tailoring examples illustrated, or from supplier to customer, as we saw in coaching, benefits both. In some situations, the pragmatic solution calls for sharing responsibility for tasks. Certain transactions don't need to meet rigid deadlines. Because of their cooperative relationship, the supplier and the customer are well-positioned to note here, however, is CIGNA's channeling the momentum from this initial maneuver.

Similarly, Samsung Electronics is creating a single point of contact in its Business Operations Center. According to manager Richard Choi, "We're changing the process first. In the beginning we don't even think about the system, we think about the vision: What's best for the customers? Our vision for the year 2000 is to answer any kind of question that a customer presents within two minutes and deliver within two days. Technology is only the tool. The relationships are the key."

Change Your Measurements and Rewards Systems

Whatever the merits of the maxim "Spare the rod and spoil the child," it's long been understood that people learn most effectively when they're given positive reinforcement and rewards. Incentive programs for employees, sales quotas, and performance-related bonuses can be invaluable tools for keeping a company jogging along at top speed. One way to get on the road to customer intimacy is to measure performance and hand out rewards in accordance with the goals of the discipline.

That's precisely the way Marshall Industries went from being customer friendly to being customer intimate. Robert Rodin, president and CEO, realized that Marshall's customer service was designed to make sales first and serve customers second. "Our people were shipping orders ahead of schedule so they could seal enough sales within a given period to win a prize. Customers want the order when they want it, not a week before. All of this 'We gotta score' attitude, this internal heat, was causing quality degradation, customer irritation, and, ultimately, increased costs. We knew the system had to be changed from the top. It would've been absurd to yell at someone for