Customer-base concentration: Implications for firm performance and capital markets: 2011 American Accounting Association Competitive Manuscript Award Winner

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**ABSTRACT**

This study investigates whether and how customer-base concentration affects supplier firm fundamentals and stock market valuation. I compile a comprehensive sample of supply chain relationships and develop a measure ($CC$) to capture the extent to which a supplier's customer base is concentrated. In contrast to the conventional view of customer-base concentration as an impediment to supplier firm performance, I document a positive contemporaneous association between $CC$ and accounting rates of return, suggesting that efficiencies accrue to suppliers with concentrated customer bases. Consistent with a cause-and-effect link between customer-base concentration and supplier firm performance, analysis of intertemporal changes demonstrates that $CC$ increases predict efficiency gains in the form of reduced operating expenses per dollar of sales and enhanced asset utilization. Using stock returns tests, I find that investors underreact to the implications of changes in customer-base concentration for future firm fundamentals when setting stock prices. A trading strategy that exploits investors' underreaction yields abnormal stock returns over the 30-year period studied.

**JEL Classifications:** M41; L25; G14.

**Data Availability:** Data are available from the sources indicated in the text.

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