$119.95

mdm premium

MDM Special Report:

2016 Distribution Remodel – Core Competencies

mdm.com Copyright © 2016 by Gale Media, Inc. All rights reserved. Modern Distribution Management® and mdm® are registered trademarks of Gale Media, Inc. Material may not be reproduced in whole or in part in any form whatsoever without permission from the publisher. To request permission to copy, republish, or quote material, please call 303-443-5060.

Table of Contents

MODERN DISTRIBUTION MANAGEMENT

Founded in 1967
by J. Van Ness Philip

Publisher
Thomas P. Gale
tom@mdm.com

Editor
Jenel Stelton-Holtmeier
jenel@mdm.com

Associate Publisher
Craig Riley
craig@mdm.com

Associate Editor
Eric Smith
eric@mdm.com

Editorial Advisory Board

Chester Collier, SVP & general manager, Bio-Circle North America, Walter Surface Technologies

Ted Cowie, Vice President Sales, Safety & Industrial Products, Motion Industries

Larry Davis, Chief Commercial Officer & EVP, Stellar Industrial Supply

Julia Klein, Chairwoman & CEO, C.H. Briggs Company

Doug Savage, President & CEO, Bearing Service Inc.

Burt Schraga, CEO, Bell Electrical Supply

Ted Stark, President, Dalco Enterprises

Contact Information
Questions, comments, article proposals, address changes or subscription service to:

Gale Media, Inc.
2569 Park Lane, Ste 200, Lafayette, CO 80026
Tel: 303-443-5060
Website: http://www.mdm.com

Subscription Rates
To subscribe to Modern Distribution Management, please call 303-443-5060, email tish@mdm.com or **http://www.mdm.com/subscribe.**

Published twice monthly; $395/yr., $415 U.S. funds other countries. Six-month and two-year terms are available. For group subscription rates and site licenses, please contact Tish Marti at 303-443-5060 or visit www.mdm.com/corporate.

Copyright © 2016 by Gale Media, Inc. All rights reserved. Modern Distribution Management® and mdm® are registered trademarks of Gale Media, Inc. Material may not be reproduced in whole or in part in any form whatsoever without permission from the publisher. To request permission to copy, republish, or quote material, please call 303-443-5060.

ISSN 0544-6538

mdm.com

Introduction: How to Build a Better Business

Market conditions favor the adaptive distributor

The distribution industry is due for a remodel. What has worked for decades still works, but it is far less effective now for businesses that want to grow. MDM's team has identified key areas to focus on in 2016 to build the adaptive model that changing market conditions require.

By Jenel Stelton-Holtmeier

Understanding economic cycles – and where we are in them – is an important part of doing business. And disruptive cycles are nothing new in distribution. So this current disruption – or "curve in the road," as Alan Beaulieu of ITR Economics called it at the 2016 NAW Executive Summit – should seem familiar.

The world is in an era of fundamental change. The impact of technology, the emergence of the digital globalization, demographics and many other factors have changed how business is conducted on both the buying and selling sides. But the fundamental issue is around how companies are changing their capabilities to create value for their customers in spite of what's taking place in local and global markets.

Bridging the cycle gap

The current market cycle has created a gap that keeps growing. On one side of the gap are companies that continue to operate using essentially the same business model that has "always worked" for them. In this model, businesses ride the cycle up in good times and they hang on as they ride it down in the bad times.

Adjustments are made along the way. Distributors focus process improvements around inventory, logistics and other transactional elements. But most of their competitors have also done that. The incremental optimization is getting smaller and smaller, particularly as the technology tools have gotten better and better.

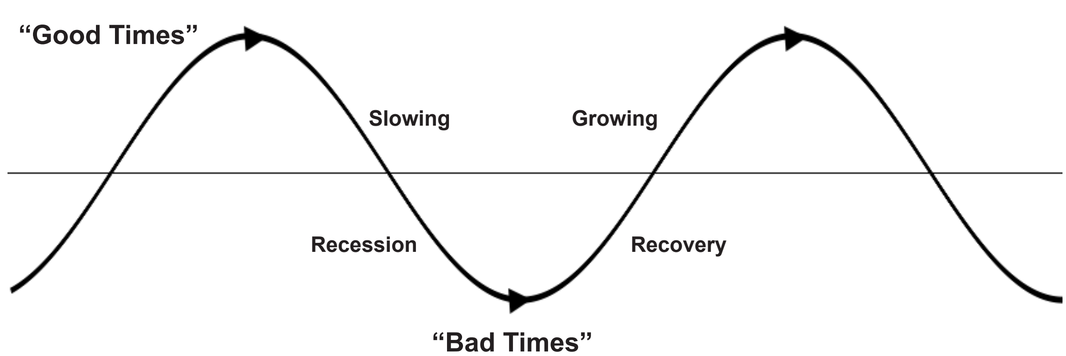
On the other side of that gap are companies that are asking different questions about what they have to do to make themselves successful going forward. These are the market leaders. Instead of asking "Who moved my model?" they're saying, "We've changed our model." These distributors focus on how to use the conditions on the way down to improve conditions on the ride up, rather than on just how to survive the drop.

The distribution model is due for a remodel. The foundational elements should not be abandoned – customer intimacy and operational excellence are still critical to long-term success. But serving customers requires a change of mindset. It's not just about being lean; it's about being adaptive.

The days of your customers buying from you because it is too difficult to compare what you offer to your competitors – online and offline – are quickly becoming history. This series on the 2016 Distribution Remodel will provide deeper insights into how distributors can upgrade their models to be more competitive.

Here is an overview of the elements we consider key to the 2016 Distribution Remodel, and the topics that we will cover more in-depth

Figure 1: Riding the Economic Cycle



in this and in upcoming issues.

Investing on the Down Side

The increased competition from new players, including big-box stores and online-only distributors, and more supply chain transparency have resulted in compressed margins and tighter budgets. This, in turn, inhibited the ability of distributors to invest in new product and service models because cash flow has been constrained.

But the new environment requires an upgrade. Current conditions have magnified the impact of lack of investment for many distributors, and many are struggling to figure out how to best use their limited resources. They need to invest in technology, in talent and in how they approach sales – among other aspects. And it is likely too much for any company of any size to address all at one time.

It is critical to strengthen the foundation core, then prioritize how to build a bridge to the future, more adaptive model for your company. Start by identifying your gaps and strengths and evaluate the role those aspects play in your company. Then assess what needs to be done to create a stronger, more agile company for the upside.

Taming the Talent Tide

Millennials now outnumber baby boomers in the workforce. And they have a very different idea of what an ideal workplace is.

And as digital natives, they bring a very different skillset to the table – one that you might not know is ideal for growing your company. For a long time, the focus for hiring has been on matching a person to a job description. Hiring managers want the "unicorn" employee, the one who has the perfect collection of skills, experience and education – easily assessable characteristics.

But that one-size-fits-all definition isn't working as well anymore. It excludes many good candidates who may have a degree or experience in a field that's not listed. And it fails to account for culture, which, in many ways, is the most important differentiator for distributors.

Don't let your search for the mythical unicorn employee keep you from finding the best employee. Skills can be taught; culture can't.

It's also important to look at how you develop skills within your own organization. The myth of the millennial is that they're willing to jump ship for a little bit more money. The reality is that they're really looking for some place where they don't just feel like any generic cog in the machine. You do still have to offer a competitive wage, but you can't just throw money at them and hope the other issues are forgotten. If you invest in developing them for the long term, they are more likely to repay that investment with loyalty.

Finding Balance & Focus

As with any remodel, having a strong foundation is important. Without a strong foundation, new additions will crumble before they've had a chance to be fully built. But if too much focus is placed on the foundation, your business will not grow.

How can you adapt to your customers' changing needs while staying focused on your core strengths at the same time? How will you continue to create value for your customers as their expectations change?

Companies that are proactive and strategic about how they adapt have more control over the process than those that are just reacting to whatever is thrown at them.

Data plays a big role in finding balance and focus, going back to identifying gaps and strengths. But instead of focusing on how to improve business operations, the focus needs to be turned outward to how markets are being served.

Where are the most profitable places to deploy your limited resources? How can your customer segments be most effectively and efficiently served?

'Invest or Die'

Distributor survival depends on strategic investment - even in downturn

Distributors that invest wisely on talent, technology or other areas of their business will gain competitive advantage – and market share – when economic conditions improve. This article explains why strategic investment is critical and provides tips on where and how to devote resources.

By Eric Smith

Remodeling a business model requires strategic planning, unwavering commitment and, most importantly, financial investment. A distributor can't reinforce the company's foundation or add new floors without devoting time and money to the process, but those that take the steps needed to compete in today's competitive landscape will be rewarded with additional market share and improvement to their bottom lines.

When should distributors invest? Distributors must prepare for the looming economic recovery – expected to arrive in the second half of 2016 – by investing in their businesses now. While cost-cutting seems to make more sense in today's challenging economy, distributors should commit to growing their business so they'll be ready when the climate improves and sales bounce back.

Where should distributors invest? That depends on a company's most glaring shortcomings. Even a successful distribution giant like Grainger, Chicago, IL, which has endured two straight quarters of sales declines, is finding areas to cut costs in order to build the company's infrastructure, e-commerce, supply chain and IT systems, according to CEO Jim Ryan.

"Those capital investments are really tough to make when you're looking for ways to get costs back out of your business when revenue is down," Ryan says. "Many companies, we found, will take a timeout on those more capital-intensive investments in down economies. But this is not only an opportunity to be different; it's an opportunity to move forward faster."

Reasons to remodel

Myriad factors underscore the need for distributors to remodel. Disruptions occur every day. The digital divide is growing. Positions throughout a company's organizational chart remain unfilled as HR directors lament high turnover and a lack of qualified candidates. Yet distributors – especially small to mid-sized ones – have historically remained resistant to change.

The main reason is financial. For a $10 million distributor that has annual profit of $200,000, a new e-commerce platform might seem like a luxury rather than a necessary tool to compete in today's digital world.

"If you're asking them to spend $100,000 on a new e-commerce system, and that is going to take out what their profit is for that year, that's obviously a really hard conversation," says Ranga Bodla, wholesale distribution industry lead for NetSuite.

Another reason is that many distributors are family-owned and multigenerational. Lifestyle businesses, in which the owner is also the chief executive, operate on a different playing field, according to Mike Marks, partner, Indian River Consulting Group.

"For them, it's more important to avoid a bad year than it is to take a risk, invest money and have a good year," Marks says. "That's hard-wired in their DNA. As soon as things get soft, they hunker down and wait for it to go away."

But professionally managed distribution businesses, such as ESOPs, private equity-owned entities or public companies, take a different tack. They covet revenue growth, geographic expansion and added market share – and the percentage of businesses pursuing measurable growth is encouraging.

A joint MDM-Baird survey showed that more than three-quarters (77 percent) of distributors plan to invest in their business in 2016. Of the 6 percent that said they won't invest in 2016 and the 17 percent that said they might, the fragile U.S. economy was the top reason for hesitating or balking altogether.

But, as Bodla points out, "the market, as always, is going to turn. If you wait until the market stabilizes, you're going to be too late. Now is the perfect opportunity to get ahead of the pack and put in place that competitive advantage before your competitors do."

The need to differentiate

Investing in a distribution business, especially during a down economy, helps differentiate it from enterprises focused only on short-term results.

"We try to practice an investment mindset instead of what I think a lot of larger, publicly held companies, in particular, tend to do," says Victor Jury Jr., CEO of Summit Electric Supply, Albuquerque, NM. "They view things like payroll or technology from a financial perspective, seeing them as expenses rather than investments. Any business is only as good as the people that it employs and the technology it uses to serve its customers."

That approach doesn't change when the economy softens or sales dip, Jury says. If anything, it provides a key opportunity for Summit to find new ways to excel. "When the industry is less active, we have our very talented people pursue improving our business and doing things that we can build on for the future," he says. "That's been our philosophy for the last 38 years."

Distributors with that ideal are more likely to evade the disruptions that arise constantly, according to Mike Sprague, director, eBusiness Development, Thomas Enterprise Solutions.

"Players like Amazon have changed the landscape forever," Sprague says. "These guys are coming into the B2B space with a bunch of tools, a bunch of talent, a bunch of tried-and-true commerce methodologies and they're changing the old paradigms of locations, logistics, and they're changing it forever. Customers who use Amazon by night come to work by day with that expectation."

Differentiating means honing in on a company's competitive advantage, according to Will Parsley, manager of new product development, Carswell Distributing Co., Winston-Salem, NC.

He says a company shouldn't focus on committing to a specific amount – such as a certain percentage of profit each quarter or year – but should instead constantly ask what needs to be done to remain competitive and enhance the value proposition to customers.

"If we want to emerge from an economic cycle or even sit in the depths of an economic cycle and succeed, we're going to have to have a compelling value proposition," Parsley says. "We have to invest or we die."

Invest in technology

From e-commerce to IT to data and analytics, distributors have fallen behind other industries when it comes to investing in technology, especially as customers expect a more compelling experience, like something they'd find on a B2C website.

"Looking at the different kinds of investments you can make, technology is the No. 1 investment to improve productivity and your competitiveness as a business," says Andy Vabulas, CEO, I.B.I.S. Inc. "I don't understand the hesitancy to invest in technology, but I understand that the question, 'Do I buy a new boat or lake house or do I buy a new ERP system?' comes into play more than I'd want to believe."

Others, like IRCG's Marks, agree that technology is where distributors lag, yet it often takes a backseat to other business considerations. "Given that most industrial channels are way behind the digital process, the smart play is investing in making it easier for customers to deal with (the distributor) electronically. It's about selling. It's about being sticky."

Carswell Distributing upgraded its 20-year-old business systems, which Parsley likened to trading in a flip phone for an iPhone, skipping the Blackberry phase altogether. "We made some clear strategic initiatives for the things we needed to do to evolve our business," he says. "We looked at the technology that we had and said we can't do it with this, so we have to invest to get to where we know our business can be."

Large distributors with massive amounts of capital to spare on new technologies aren't the only ones making that commitment. Smaller companies such as Carswell or health care packaging distributor Action Health, Bensenville, IL, repeatedly dedicate resources to upgrading their technology.

"Now is always going to be the best time to get yourself away from that traditional model of maintaining and supporting your own hardware and getting into an operating expense that's more manageable, easier to forecast and gives you the ongoing business capabilities you need," says Action Health CFO Phil Negri.

And while a basic website or e-commerce platform are now considered table stakes in the industry, many distributors are realizing the need to enhance their capabilities quickly – or risk obsolescence.

"We need to be the absolute best in our space," Negri says. "If we're running technology that's even a year or two old, someone's going to be passing us up. We always need to be current, we always need to be pushing the envelope in new optimizations to make us more efficient, better at what we do. If we're not, someone else is."

Right now, money is cheap to borrow, but companies also should view today's slow economy as the ideal time to optimize their systems because the downtime gives employees ample opportunity to learn at a leisurely pace, all with the idea that they'll be up to speed when things pick up.

"You have the time to put your best people on it and take a fresh look at your business so that when the business comes back, you're hitting it and you can take advantage of (the recovery)," says Vabulas of I.B.I.S. "The worst time to take advantage of technology change-out is when you're blowing and going and you don't have time to pay attention and you just do enough to get it done instead of rethinking your business and taking advantage of all the new best practices and technologies available today."

Invest elsewhere

Technology isn't the only area where distributors should consider investing. Respondents in the MDM-Baird survey indicated they will spend money in 2016 on sales (18 percent), training (14 percent) and other investment areas.

For Grainger, investing in inventory during a down economy is mission critical. Keeping order fulfillment rates high will help drive new inquiries and new business, Ryan says. "Customers are facing the same economic headwinds as we are, and they're looking for ways to get cost out of their business. So if they can rely on our inventory and we can help them manage their inventory, those are two great ways to help customers get costs out of their business and ways for us to invest," he says.

Another area to invest is marketing. Alan Beaulieu, an economist with ITR Economics, has been reminding distributors at various association conferences during the past year to invest in their businesses – most notably in human resources and marketing. "If you don't have a chief marketing officer, rent one," he said at the National Association of Wholesaler-Distributors Executive Summit in Washington, DC, last month.

Plenty of companies heed that advice. Summit, for example, places a strong emphasis on marketing, viewing it as an area where the company can brand itself, promote its competitive advantage and even find ways to more easily acquire talent while further developing customer and supplier relationships, according to Jury.

"We've invested in marketing since our founding and have been blessed to have the same person leading our marketing group for almost 30 years," Jury says. "At the end of the day, marketing is about telling a story. Whether you're telling it to a potential recruit, a customer or a supplier, it's important for that story to be well-told and for it to be communicated in a way that is compelling so it gives your audience an opportunity to respond."

Pitfalls to avoid

Challenges exist when investing in a company, especially amid stagnate sales, a shaky economy. and tenuous cash flow. Distributors must be mindful of the biggest mistake they can make, which is deciding to spend money once – on technology, talent, a marketing campaign or something else – and then not committing to it.

"You can't position it like you used to do as a one-time investment with bricks-and-mortar and say, 'I built a building, I don't have to worry about it for 15 years at least,'" says Dave Bandi, director, AEC/BIM Solutions, Thomas Enterprise Solutions. "These are investments that need to be aligned with an overall strategy, and they will become part of a significant ongoing plan. And it needs to be around a complete change of business. Some companies get it, some don't."

Grainger has spent heavily on its e-commerce capabilities during every economic cycle – up or down – in the past two decades, and in 2016 e-commerce will compose half of its revenue, or about $5 billion.

"That would not have been possible if we were episodic in our e-commerce investments," Ryan says. "Having the discipline to continue to invest in e-commerce, continue to invest in our supply chain and continue to invest in our systems infrastructure – which can be a little painful – has helped us create a competitive advantage."

The message to distributors is clear. Though the economy is down, it is short-term, and this is the point when you have the time to invest in one or more projects to make your business competitive long-term and capable of handling the disruptions that are sure to surface.

A company that invests in its technology and talent, in its inventory and its sales force, will bolster relationships with employees and supply chain partners, become more profitable and position itself for future success.

"This is not something that is a one-time project," says Sprague of Thomas Enterprise Solutions. "This is a journey that you're going to go on. And it's going to make you viable not only this year but into the future and will protect your business from B2C players like Amazon as well as the nipping at your heels from small, startup companies."

Refocus on the Core

Foundational strength imperative during uncertainty

For distributors to successfully navigate a challenging landscape they must reinforce their core strengths. This facet of the 2016 Distribution Remodel could entail a number of solutions, from deepening customer engagement to dropping unprofitable customer segments to divesting noncore assets.

By Eric Smith

Remodeling a distribution company requires a sturdy foundation before additions can be made, yet too many companies try to build new floors without first reinforcing the infrastructure.

Distributors in recent years have focused on broadening their offerings, adding product lines and expanding geographic reach. More than anything, however, today's climate requires a strong foundation to withstand lingering frustrations such as decreased end-user demand and mounting disruptions such as Amazon.

As the economy staggers through the first quarter of 2016, it is critical for companies to adapt to changing market conditions by strengthening their core. A wide range of options may be considered to achieve this, including investing in talent, enhancing technological capabilities, acquiring complementary businesses, shedding noncore assets or axing unprofitable customer segments.

"For a number of players, a 'focus on the core' will be the mantra that you hear in 2016," says Reed Anderson, head of Houlihan Lokey's industrial distribution practice. "Anytime a business faces a challenge, particularly a distributor, there is a tendency to pull back to core markets and practices, as opposed to diversifying, which is easier to do when all the numbers are going up and to the right."

Reasons to remodel

Sagging oil prices, China's continued economic woes and even El Nino have helped downgrade most economic forecasts, according to Alan Beaulieu of ITR Economics. At the National Association of Wholesaler-Distributors Executive Summit in Washington, DC, last month, he said that the "economy is in a lull. It's scary but it's temporary, and it will improve in second half of 2016."

An "unusual confluence of events right now" – pain that stems from the unfavorable oil & gas, commodity pricing and foreign currency exchange situations – is how Jim Miller, a principal and founder at Supply Chain Equity Partners, describes the climate that has affected particular distributors significantly worse than the recession. Year-end and fourth-quarter earnings reports that fell short of expectations bear that out.

"What you're getting hit with right now is the energy sector is getting beat up pretty bad," Miller says. "Not just on the Gulf Coast, but with the price of oil where it is, all the alternative energies have gotten eaten up."

The effects can be seen across distribution, especially in sectors with exposure to oil & gas end markets. But savvy companies are responding. In light of the oil and gas collapse, pipes, valves and fittings distributor MRC Global Inc., Houston, TX, agreed to sell its oil country tubular goods (OCTG) business to Sooner Pipe LLC, a subsidiary of Marubeni-Itochu Tubulars America Inc., for $48 million.

As Andrew Lane, MRC Global's president and CEO, pointed out, "The divestiture of our OCTG product line is the culmination of our strategy to reduce our exposure to upstream drilling volatility and to focus on growing our higher margin product lines, particularly our valve, valve automation and instrumentation business."

Devising a blueprint

The longer these headwinds persist, the more distributors will suffer because they have very liquid balance sheets of receivables in inventory, Miller says. "Short downturns, even if they're very dramatic like we saw in '08 and '09, you can sustain those if you liquidate your balance sheet," he says. But if the recovery keeps getting pushed back, many distributors will reach an inflection point.

"All you're left with at the end of the day is, 'I used to sell $100 widgets at a 20-30 percent markup and I'm now selling $40 widgets at a 20-30 percent markup,'" Miller says. "That math blows through the financial statements and the distributors have to react to it."

Those who don't react, those who maintain the status quo by "just pulling the blanket over your head and waiting for things to change," Miller says, will get left behind.

"You have two options," Miller says. "You have to scale down significantly or, like we see with some of the bigger distributors, divest noncore businesses and reinvest in the core. Or you have to continue to invest to diversify into sectors that aren't facing such headwinds."

As distributors look to prosper or at least stay afloat in today's slow- or no-growth markets while waiting for headwinds to ease, many are examining their key customer segments and the product portfolios that serve them. Analytics is driving model changes in distribution, from multisegment to the more focused strategy of targeted segments served profitably in the "sweet spot" of the distributor's service and product offering.

"Distributors are looking for ways to differentiate themselves versus the competition," Anderson says. "They are looking for a way to provide more value to their customers. That could be through a broader product offering, through having more services, through having different technical expertise. There are any number of ways that you can go about it."

One way includes a shift from being "all things to all types of customers" to focusing resources on providing the most profitable cost-to-serve equation. Overall the goal of these remodeling efforts is to become a more customer-centric company.

Embedding more deeply in customer business processes is another remodel blueprint. By creating deeper engagement in the core customers rather than the smaller, less profitable segments, distributors can differentiate from competition. Investing in technology is the surest way to achieve this, says Ranga Bodla, wholesale distribution industry lead for NetSuite.

"The question that distributors have to ask is how are they not just going to survive and improve their business, but how are they going to thrive?" Bodla says. "The ones that survive and thrive are the ones that create a competitive advantage for themselves."

Remodeling's role in M&A

While an upbeat economy drives more companies to grow through acquisition in complementary areas or expand what they're already doing, today's climate has a different effect on the industry as companies shift resources to their core business.

"When the economy is more challenging, more uncertain, it's more difficult to do something that is bolder or different," Anderson says. "The tendency, and the right thing to do in most cases, is to protect the 'golden goose.'" That's the time to focus on what you do best and "get back to your roots," he says.

The list of distributors shedding noncore divisions to focus on their core businesses is growing longer each month, and it should accelerate M&A in 2016. In each case, the CEOs of those companies are using familiar phrases to describe their mindset for these deals, using terms like "strategic" and "core" and "focus" and "shareholder value."

When Anixter International Inc. divested its fasteners segment last year, selling it to American Industrial Partners for $380 million, President and CEO Bob Eck said: "Following the transaction, Anixter will have a sharper strategic focus on our core enterprise cabling & security solutions and electrical and electronic wire & cable segments and additional financial flexibility to build on these strong global platforms through organic investments, as well as strategic acquisitions, allowing us to continue to deliver long-term value to shareholders."

Anixter later played the role of acquirer, buying HD Supply's Power Solutions division for $825 million. The deal helped Anixter sharpen its focus on wire & cable and allowed HD Supply to simplify and save money by in turn focusing on its three remaining divisions.

"If you look at the strategic rationale for the transaction for HD Supply, at the highest level it allows us to enhance our business mix, and it will accelerate our capital structure strategy," President and CEO Joe DeAngelo told MDM shortly after the deal. "This is a transformational transaction for us. It positions us to get faster and better."

Air Products is another recent example. When it announced late last summer it would spin off its materials technologies business to shareholders, President and CEO Seifi Ghasemi called it a "strategic move." And he said, "This separation will provide shareholders ownership in two leading and focused companies while providing the opportunity to value our industrial gases and materials technologies businesses independently. We believe a tax-free spin-off of the materials technologies business will create significant shareholder value."

Differentiate to win market share

Focusing on the core means getting "aggressive in other areas of the business," Grainger President and CEO Jim Ryan told MDM recently. As the company works to cut costs in light of slowing sales, it avoids touching anything that might impact service and, therefore, alienate customers.

"Investing in big distribution centers, investing in e-commerce infrastructure and investing in ERP systems, those things can be tough to do during a down economy, but fundamental to our strategy is being the best in the industry in service," Ryan says. "We know that the big enablers to our service offering are our systems, our supply chain and our e-commerce. There's a direct link to our strategy, and not continuing to make those investments would be backing off of our strategic imperative."

Honing in on customer needs as well as market conditions drove United Stationers to refocus on its core. As the company grew organically and through acquisition, expanding capabilities with each purchase, it realized that its ordering systems across all of its businesses weren't integrated. Company leaders devised a way to unite them all into one platform to enhance and streamline the customer experience, concurrently rebranding as Essendant.

"In 2015 we took a series of actions to position the company for success, including renewing the focus on our core office product and jansan businesses, lowering our cost structure and rebranding to Essendant," said Robert B. Aiken Jr., president and CEO. "As we look ahead, we are well-positioned to continue implementing our strategic initiatives and deliver revenue and earnings growth in 2016 … ."

Distributors that want to drive revenue and earnings growth this year will be the ones who constantly disrupt themselves. Those that have waited must begin the process now to ensure they have a rock-solid foundation for the rest of this year and beyond.

"Those companies that are pursuing the right business strategy – whether it's a good economy or an uncertain economy, and it takes a lot of discipline to pursue those strategies in an uncertain economy – are going to differentiate themselves from others moving forward," Anderson says.

And that holds true across sectors and geographies, for the small- and mid-sized distributors working the market's niches as well as the multimillion-dollar national and global distributors.

Deepen Talent Development

Demographics, competition for top talent drive development programs

As the labor pool tightens, developing and retaining existing employees becomes more attractive and critical for business success. This article examines how distributors are thinking differently about development and provides tips to overcome barriers and create an action plan that strengthens operational and financial results.

By Jenel Stelton-Holtmeier

Even when unemployment was high in the U.S., competition was fierce in distribution for top talent already imbued with the right set of skills. Now that more pressure is being placed on the labor pool, managers and executives are turning a keener eye on how to retain and strengthen the employees they already have.

In the fourth quarter MDM-Baird Distribution Survey, respondents were asked about where they intended to invest in their companies in 2016. Training was the third most popular response, behind sales and e-commerce.

For North Coast Electric Company, Seattle, WA, associate training and development was recently elevated to "high priority," says Christina Ide, director of human resources. "Associate development is so important to us that leadership has made it the fifth key company initiative for 2016. It ranks right up there with our sales and operations excellence initiatives."

Think differently about development

Changing customer expectations is one of the reasons North Coast elevated its focus on training, Ide says. Customers expect more, and the company can provide additional expertise through specialized training programs.

In addition, North Coast recognized the role that training could play in achieving other initiatives, such as improving operational efficiency. "Having well-trained employees contributes to profits," Ide says.

But talent development extends beyond training on products and processes; it's an investment in the culture and future of the organization.

Recruiting the right people is still critical to long-term success, says Rebecca Ray, human capital practice lead for The Conference Board. "If you don't cast the right people in the right parts, it doesn't matter how well you direct them." But many employees are no longer satisfied with doing the same thing day in and day out for their entire career. And they know that they don't have to be.

"One of the most important levers that a company has to retain talent is to continually offer opportunities to grow and learn," she says. "If organizations fail to do that, people are going to go elsewhere."

It's not about promoting new hires to C-level positions in six months; it's about making them an integral part of the organization.

It's also not all about the newer hires. Demographics demand a change in how managers and executives think about leadership and succession. There simply aren't enough Gen Xers in the workforce to replace the baby boomers in those management positions, which means managers may need to look at grooming younger employees for those roles more quickly.

"It will mean there is a different way that we start to look at leaders," Ray says. There are some indications that shift has already begun.

Each year, The Conference Board conducts a survey to uncover the top concerns of CEOs and their strategies to mitigate them. "The CEO Challenge" includes questions on strategies for innovation, which many executives view as a critical element for growing sales.

In the past, investing in technology was viewed as the top strategy for driving innovation in companies; in the latest versions of the survey – which began in 1999 – the top strategies revolve around developing innovation skills in employees. This includes a focus on scenario planning or exploring strategies from outside the company's specific industry or niche.

"Companies, particularly CEOs, are starting to recognize that innovation comes from people," says Ray, who has coauthored some editions of the report. "It's not incremental innovation from new technology, but rather smart people who leverage the technology to get to that innovation."

Dismantle development barriers

For many distributors, one of the barriers to implementing talent development strategies arises from resources. Smaller organizations often have a less developed human resources department – or they may not have one at all. And much of that office's attention may be focused on other operational elements, such as benefits and payroll.

Last fall, buying and marketing group Affiliated Distributors launched a program for its members to help address this challenge. AD created the HR Services program "at the members' request," says Neil Cohen, vice president of organizational development and human resources. "Collectively, they said they needed help with certain areas of HR, either because they didn't have a full-fledged HR department or they did but they needed some other resources to rely on."

Before launching the program, Cohen reached out to members to determine their top concerns. Unsurprisingly, recruiting was No. 1, followed by compensation. Training and development came in a strong third, he said, "particularly around management and leadership development."

Many associations, including the National Association of Electrical Distributors and the Industrial Supply Association, have created learning centers for their members that cover a broad range of topics from Microsoft basics to professional certifications.

But look internally, as well. Create diverse teams that will naturally bring different viewpoints to the table, Ray says. Younger leaders may be able to identify new ways to use existing technology to improve processes, while employees with more tenure may be more in tune with existing and ongoing pain points.

A mentoring program that pairs veteran leaders with up-and-coming stars can also go a long way toward accelerating development and increasing engagement. It allows for more personal transfer of institutional knowledge that might otherwise disappear when the veteran retires. It can also help identify areas for improvement even among veterans.

Lack of awareness of organizational needs can hamper and even derail a company's growth plans.

"Developing a business strategy without understanding your capability to execute is a fool's errand," Ray says. "What's the future state? Where are you now in terms of your organizational talent? And what's the plan to close that gap?"

More AD members are considering top-to-bottom talent reviews to help them proactively assess the skills and potential within the organization, Cohen says. And it should allow them to identify weaker performers and "deal with some of those tough issues head on, as well as create development plans for individuals with different performance and potential levels throughout their organization."

Clear and accountable roles are among the most important drivers of organizational health, according to McKinsey's Organizational Health Index, and they provide a blueprint for creating or adapting talent management and development programs.

"We are in the process of developing job descriptions which will allow us to better determine training needs," Ide says. "Once we identify the needs, we are going to compare them to the training we already have, verify that it's up-to-date and identify who needs it. We are going to roll out training to the area(s) where we have the most turnover to facilitate retention."

Assessing development initiatives

Having HR programs in place is only the first step, however; assessing the effectiveness of those programs is also critical. For AD members Cohen spoke with, this was the fourth and final piece that needed to be included in the HR Services program.

They wanted to know if their HR programs were effective and how they benchmarked against other organizations, Cohen says. They wanted to "identify opportunities to make their HR processes better, especially where those could be tied to improved business results."

Numerous studies have highlighted the effect of employee engagement on performance and productivity. If employees are invested in what they're doing, they're more likely to put more effort into doing that job well.

But measuring engagement is more nuanced than assessing if hiring goals have been met, Ray says. "Are you getting the level of productivity and the discretionary effort that you had hoped from those hires? It isn't just bodies in the chair."

There are hundreds of different survey providers to help evaluate the level of engagement, but ultimately what matters most is what is done with the information provided, regardless of the tool.

"What does that number really mean for your organization? If you moved from 72 percent engagement last year to 74 percent this year, is that really significantly better?" Ray says. "More important than that number is what you do about the issues that are uncovered.

"If you ask your employees for feedback and don't do anything about it, they'll probably disengage from the process."

Develop an action plan

It's easy to think of this at the individual level, Ray says, but it's more difficult – and in many ways more important – to tackle it at the organizational level. Often managers are charged with developing their own action plans based on the results from their departments.

"You can have thousands of plans floating around the organization that nobody does anything about until the week before they are supposed to be done," she says. And then everyone scrambles to pull together training sessions at the last minute just so they can "check off the box to say that they've done something."

As a result, the programs probably aren't well thought out, are less effective and can overwhelm employees with too much useless information.

"What an absolute waste," Ray says.

Instead, create a team that includes the CEO – "One of the most critical pieces to having a highly engaged workforce is having a very active CEO," Ray says – and other leaders throughout the organization. That team should identify one or two areas for the company to fix over the next year.

These areas will be different for every company, but make sure they're focused on the entire company. This could be improving communication to make it more frequent, transparent and honest or providing managers with the skills and training to be better coaches that help identify and encourage development of younger leaders.

"If you do talent development well, your retention is going to be far better, and, in the long run, you'll have a stronger organization," Cohen says. "But the only way to do that is to have it baked into your culture. One of the biggest hurdles is managers and leaders making time to keep talent development in front of them."

Thank you for your purchase. Interested in more special reports?

MDM Premium subscriptions include full access to all MDM Special Reports at no additional cost.

Learn more about subscribing to MDM Premium at www.mdm.com/subscribe. Use SR10 to save 10%.