Fighting Disintermediation: How Distributors Develop, Deliver and Measure Value

An MDM Webcast transcript, featuring:
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Michael Capone, audit partner & leader of Grant Thornton's distribution practice

This is the full transcript of the MDM Webcast "Fighting Disintermediation: How Distributors Develop, Deliver and Measure Value" from September 2014.

The Webcast presentation slides are included at the end of this transcript.

Jenel Stelton-Holtmeier: Welcome and thank you for joining us for today's MDM Webcast: Fighting Disintermediation: How Distributors Develop, Deliver and Measure Value. My name is Jenel Stelton-Holtmeier, editor of Modern Distribution Management and mdm.com, and I have the pleasure of moderating and participating in today's program.

Disintermediation is defined as manufacturers going direct to the end user rather than incorporating distributors to their sales channels. The idea is that by cutting out the middleman, manufacturers will be able to increase profit margins because they won't be sharing that final payment with a distributor, and it gives them more control over the relationship with the end customer.

But for distributors, there's a problem with this way of thinking beyond just the potential loss of business. They know that they do more than move product; they provide service and support both up and down the chain. The challenge is demonstrating that value to both the end user and the manufacturer.

In this Webcast, we will share with you the results from the survey Grant Thornton and MDM conducted in June and July about the threat of disintermediation. We will examine how distributors are combating this threat and provide examples of best practices for proving and measuring the value distributors provide.

I'm delighted today to introduce my co-presenter Michael Capone. Michael Capone is an audit partner and leader of Grant Thornton's distribution practice. Prior to his current position he served as the Midwest Region Consumer and Industrial Products Industry Leader. Michael has served a wide spectrum of public and private companies, predominantly in the manufacturing, retail and distribution industries.

Prior to joining Grant Thornton, he was with an international accounting firm in Chicago. Included in his experience is a four-year secondment in Mexico serving U.S.-based multinational companies. Capone is also fluent in Spanish, and he has extensive experience with public debt offerings and auditing portfolio investments of private equity groups. Michael also has two years of experience working within a specialty

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audit practice that dealt exclusively with private equity firms performing roll-up transactions. Welcome Michael.

Michael Capone: Well thank you, Jenel. It's my pleasure to be here and welcome to all the participants that are on the Webcast.

Grant Thornton partnered with MDM to prepare the survey that was fielded in the spring of 2014; it includes responses from 232 distribution executives. The purpose of this Webcast is to share those results and to provide some insight and examples as to best practices for protecting against this threat that we're all looking at.

Disintermediation is a significant concern for the wholesale distribution industry. More than three-quarters of the survey respondents indicated that they were very concerned or somewhat concerned. A common reason for the concern was the ease of online sales platforms making direct selling an easier and more appealing way of conducting business.

For some of the unconcerned or less concerned respondents, the threat didn't quite materialize the way folks were expecting. And one respondent even noted, "Been tried and failed at least once every decade, it only threatens the largest of accounts."

So what's different now? Certainly we see a lot of new competition, and we'll go into some detail as to what those are, but certainly there'll be some very familiar names. Amazon jumps to mind.

Technology has truly leap-frogged in the decades since the early 90s. And I think another big difference is generational. People graduating college now have never lived in the world without the Internet. There are those like myself who know what it's like to conduct business without using online resources, but this newer generation is accustomed to it. As more and more of them enter the marketplace I think we will see a continued shift toward that mode of business.

Stelton-Holtmeier: As Michael mentioned, the disintermediation discussion has been going on for a very long time. And one of the things that is different is how the Internet has made price visibility more of a challenge for distributors who traditionally rely on a lot of specialized price contracts, or who just don't want to have that changing price visible at all times because of the fluctuations within the market.

But as you can see on slide 5, one of the first catalogs that Sears Roebuck & Company put out in 1900 tells "just what your storekeeper at home pays for everything he buys and how that will prevent him from overcharging you on anything you buy from him."

The conflict is not new; price visibility has been a challenge over time and it's something that will continue to be a challenge, particularly with the Internet. The increased ease of implementing online platforms has definitely increased the fear of adoption by manufacturers, or of manufacturers using different types of intermediaries such as AmazonSupply to go to the market.

Alternate channels have also been around for hundreds of years, as people have looked for more effective and more efficient ways to buy the products they need, whether it's a business or a consumer. And some of these competitors are new, but some of them are the same ones that independent distributors have been watching for years, as Michael, you can tell us about on the next slide.

Capone: Thank you, Jenel. According to the survey, online-only competitors appear to be the number one concern. The Digital Age has created more transparency for price and availability. Amazon has been in the news a lot lately, we've seen *60 Minutes,* and we've seen talk of flying drones delivering packages.

It seems pie-in-the-sky, but a lot of these technologies really are coming to the forefront, and they're doing so very quickly.

AmazonSupply has gone from zero to more than a million SKUs in less than two years. The competition is moving fast, and it's something that we all need to be concerned about. And then there's some of the unknown or emerging online threats. Google is getting more into this, some of the foreign competitors, Alibaba, and there's continued pressure from the online channel.

Second to that is national distributors, and consolidation continues to be a strong force in the industry. As we all know they have more resources, tend to have greater spending power, increased multichannel capabilities, a larger distribution footprint, and oftentimes they're implementing a lot of the solutions such as their own online stores and then competing directly with Amazon.

So for the rest of us, consolidation as a whole is something that we need to take into consideration. But for some of the smaller, closely held, family businesses, it becomes more about generational issues. Who's going to take over the business when the current generation moves on? Does the second, third or fourth generation want to be involved in those businesses? If not, who can they merge with?

If you're a distributor looking for acquisition targets, where do we find the financing to complete those? How do we integrate? There's clearly risk any time acquisitions take place, and that's something that companies are concerned with on both ends of the spectrum.

Nearly 11 percent of our survey respondents indicated they're concerned about manufacturers selling directly online, competition from international companies, distributors focused only on price and integrated suppliers. And I think you'll see that as a bit of a common thread throughout this, price and number of SKUs, so we're going to delve a little bit deeper into that.

Before we do so, Jenel's going to talk a little bit more about Amazon and AmazonSupply.

Stelton-Holtmeier: Thank you, Michael. Before we move on to talking about the details of the competitive threat that Amazon and AmazonSupply bring, we have to make a distinction between Amazon.com and AmazonSupply.com.

AmazonSupply is the part of Amazon that is directly targeting the wholesale distribution market, and it actually started more than two years ago as smallparts.com. And this is the part that Amazon is investing heavily in, in order to try to gain a share of that wholesale distribution addressable market.

The problem is that with the blurring of the line between business-to-consumer and business-to-business sales, it's often confused with the Amazon Marketplace, which is not necessarily a direct competitor to most distributors – although nearly anyone can sell there, and you can definitely do business-to-business sales through that.

Both of these platforms have had a big impact on the industry by changing how buyers perceive the process of buying, which is something we'll get into in a little bit more detail later.

The one thing that a lot of people miss is that AmazonSupply is definitely trying to provide more of the services that people think of being provided by traditional distributors, including the technical support. They've spent a lot of time over the last few years trying to build up a bank of technical support specialists for the product lines that they provide, but what they do not provide still is that face-to-face, one-on-one contact.

The challenge is, is that what today's customer wants? Is that how you're going to prove the value, by providing that relationship piece?

The relationship is definitely still important, and it's something that distributors will have to continue to prove and provide for their customers throughout.

In addition, as Michael addressed, one of the big challenges is this perception of the national distributors and the market consolidators. On slide 8 is from the MDM 2014 Wholesale Distribution Landscape Report. We did a comparison based on our top 40 industrial distributors based on revenue. The market is still very, very fragmented, and the national players continue to consolidate the market, but the top 40 industrial distributors combined still only have an estimated 38 percent of that market. The remaining distributors and other channels have 62 percent of that addressable wholesale market.

The level of consolidation varies from sector to sector, but the underlying message is still the same: How do we stand out from this increased competition and this changing competition?

The other thing to keep in mind is that not all national players are consolidators. Electrical and datacomm distributor Graybar, for example, one of our top electrical distributors, prefers to open new locations but still has that broader reach and should remain a concern for some of the independent distributors.

Consistency across geography is one reason why these larger distributors have so much strength and so much power in the market. How can you address that?

One response is to collaborate with other distributors, independently or through buying groups, to create a larger network to address that same kind of geography that some of these national distributors can provide. Another way is to just simply start expanding your products and differentiate the products that you provide for your customers, and as the survey results show, that is definitely one area that people are looking at.

Capone: Great, Jenel. I think we can all agree that the threat is real; 75 percent of us see it as a significant threat.

So then the question is: What can we do? What are other distributors thinking about doing?

As the graph on slide 9 indicates, it's kind of the standard "more-better-faster" and certainly that is going to be a big component to offset and compete with the threats.

Regardless of the approach, the predominant goal is to provide greater value to the customer. There is an urgency to expand offerings to compete in the marketplace.

E-commerce is providing a better runway for expanding product offerings, and I think that's reflective in the results here, with 49 percent of the respondents looking to deepen product selection in existing categories and another 55 percent looking to add new product categories.

Keep in mind, more and faster and better may not be as large a differentiator as it was in the past, where the traditional strategy was for many distributors to have more, to be the one-stop shop. Oftentimes it's really seen as the price of admission these days and with the online competitors able to offer such a large variety of products with quick turnaround times, again, it becomes something that's way more of a necessity as opposed to a key differentiator, but something that we all need to do nonetheless.

Finally, private label products and customized services are increasingly viewed as a way to compete with online. It's a trend that we keep seeing more and more of.

Stelton-Holtmeier: Earlier this year, MDM did a special report on private label to try to gauge how the market is going and how large that addressable market actually is.

One of the things that we uncovered is that private label is far more accessible today to many more distributors, for many more products than it was even in the recent past. More manufacturers are offering short-run manufacturing to put their label on. Often this is for a lot of the commoditized-type products, but it can also create a competitive advantage.

Some distributors talked about the benefit in competing against online and big-box competitors, and even the manufacturers with private label, is that that product can only be gotten from you. That product can only be bought from the person whose private label it is.

The question is, is that product any different? Since so many of these things are commoditized, such as jan-san products, cleaning materials, how are they different from what is available elsewhere? How is it different from what they can buy at Staples?

That's something that you have to set up. Many private label manufacturers are willing to work to create that differentiation with the distributors. The question is, how much liability do you want to take on by having your name on that label, and how much input do you want on the type of products that actually have your label on it? And that varies from distributor to distributor.

The thing that is most important when considering this private label strategy is that it requires a clearly defined strategy for how to position those products.

As you mentioned, Michael, more people are trying to reach out and say, "Hey, we're going to provide you everything in one stop."

But it's the companies like Amazon and the presence of AmazonSupply; it's really going to become hard to compete and stay on top of being that one-stop shop. Amazon has that capability to add more products more readily than many distributors; they can connect with other people.

We talked to some distributors and manufacturers in the past who have connected to be affiliates of the AmazonSupply program and help provide those pieces for them. The difference is that they get a smaller margin on those products, but they get volume that they'd never have in other ways.

So one of the key things that we really have to keep in mind is that if product isn't the way to differentiate, what is? And one of the answers, as you'll address on the next slide, is through service differentiation.

Capone: Yes, I agree completely. I see this as the key differentiator. If the number of products and speed and quality are the price of admission, this is the area where traditional distributors can differentiate themselves.

Within the survey, we asked a question: What are distributors doing as it relates to service plans?

The implementation of new purchasing channels, in particular e-commerce platforms, was one of the most cited services that distributors plan to increase. This is a significant shift from a few years ago when many distributors were still resisting some of this change in technology.

Many are focused on ongoing services as solutions to the issues facing distributors rather than as a sales transaction. I see this as harder, if not impossible, for some of the online competitors and larger national distributors to replicate and to compete on. The personal touch is still important. I know a lot of clients we work with would say first and foremost that the one-on-one customer service aspect is what they do best, and that is their competitive strength.

I would also add though, that statistics show that there can be a disconnect between the perception that a company has of a service and the level of service it's providing, as opposed to what its customers perceive as great service. And don't quote me on the statistic but I do believe it's somewhere around 80 percent of companies thought they provided outstanding service, yet when their customers were interviewed the statistic was closer to 10 or 20 percent.

The other thing to consider, while I personally believe that face-to-face and the customized approach still wins out in the end, we do need to be mindful of the new generation. When I think about service and being able to call up a distributor and getting a person on the phone or a technician out to my place of business, I see that as outstanding service. A lot of the newer generation is very comfortable going to YouTube, going online, watching a video.

My daughter the other day was doing algebra, and I clearly could not help her with some of the problems. She was able to Google a website and watch a 15-minute tutorial from a college professor and figure out the problem. That's what a lot of this new generation is accustomed to, so I think we need to keep that in mind as we think through what service really means.

Stelton-Holtmeier: Definitely. You mentioned the fact that this sales transaction is no longer the key focus for a lot of these purchasers. But that transactional piece, particularly in the era of Amazon and the other e-commerce providers, is becoming in many ways a differentiator, but not in a positive way. If it's not easy for someone to buy from you, chances are they're not going to buy from you. And even if they buy from you this time because they don't know where else to go, if you make that process difficult, it's going to differentiate you from the people who make it a very easy process.

For example, Amazon has made the transactions on AmazonSupply very similar to their B-to-C side. They offer one-click ordering, they offer free shipping, corporate credit lines, you can use gift and store cards there and there are no order minimums.

More and more, customers just want to transact online, even if that's not where they're getting the sales process or where they're getting the service from. They want to be able to make that purchase quickly and easily.

As the market adjusts to what initially looks like a more efficient transaction, distributors need to find innovative ways to differentiate and effectively communicate what they have to offer, and that's not always just providing the product.

We've talked to some people who have come up with ways to offer more customization on those e-commerce platforms, whether starting the transaction there or completing the transaction there, and then talk to the service provider or the distributor to make that product specific to you. Whether it's kitting or special bundles that can be provided, or cutting it to the right length, these are things that Amazon or other e-commerce providers might not be willing or able to provide.

As Michael mentioned, a lot of distributors see themselves as being better than everyone else, or as providing service in much more exceptional ways than their customers do. In a survey that we did with Real Results Marketing last year, most distributors believed that they already provided more value than their competitors. Ninety percent said they provided more value or much more value for the same price or for a higher price.

So the question is: Can they continue to demonstrate their value when everybody else thinks they're offering value at that much higher level as well? Small businesses don't always have the resources for huge operational changes, but doing what the larger companies do isn't always the answer anyway, as one respondent noted in the survey from June. They said: "Nearest competition is a national company with much deeper pockets than our small family-run business. We aren't going to win trying to do everything the same way they do."

You don't want to be an Amazon, you want to beat Amazon. You don't want to be a Grainger, you want to beat Grainger.

So the idea is not to become what they are, but to find out what makes you better and what is that additional value that you believe that you're providing to the competitors. And it can't simply be the standard line of, "We provide it when you want it, where you want it, how you want it." There has to be that additional element because everybody says that as their value proposition.

The key part of that is improving the transparency and communication along the supply chain with all of your partners. A clear line of communication between the manufacturer, the distributor and the customer is what will create a lasting, significant return on the investment for all of them.

An Avnet representative told me once that you have to make sure there are benefits for everyone in that supply chain; it can't just be about you. No one is going to want to work with you if it's all about you. You have to have that transparency of that value and how you plan to achieve it within the industry. One of the ways to do that is through technology, and as Michael mentioned, technology investment is increasing.

Michael, would you like to address the technology from the survey?

Capone: Yes, absolutely. If you haven't caught on already, technology and the Internet seem to be a large component to this discussion and was an important aspect within the survey.

We asked respondents about what their technological investment plans were. While online e-commerce is the largest competitive threat noted by respondents, distributors still view this platform as the best tactic to combat the threats, or in other words, fighting fire with fire.

Customers are demanding more detailed information, more transparency around the products and services that they're purchasing. Technology gives us the ability to do that, and we don't want to compete just on price to the extent that we can add the value and the insights.

Distributors are in the unique position within the supply chain to have these insights and to hopefully monetize some of that knowledge.

A distributor's website is tied to the company's brand presence and is their face to the online marketplace. Many insights into customer preferences and engagement can be revealed based on website metrics. Both advertising and marketing, they're oftentimes what the world sees and those become the perception of a company, but they also provide a great deal of information.

Looking at the actual results, it's no surprise that 64 percent of respondents indicated that website development was one of their technology plans.

A third of respondents are looking at new business systems and ERP. As we all know those are large undertakings and a third of respondents indicate that they are still considering these types of upgrades. I think this highlights the importance that technology does play and will continue to play in our business.

Another one here, CRM: I think this one is often overlooked. You know the old adage: The easiest sale is to a customer we already have. How do we mine the data within our systems to understand our current customers, and what more could we be selling to them or services or value providing to them? How do we increase conversion rates?

We all have sales forces that are out in the field. How do we take their collective knowledge and bring that in-house so that the knowledge of all of them is at our fingertips?

Another hot topic is analytics, and I think business intelligence also ties into the pricing technologies. Roughly a third of respondents are looking to make investments in those areas, and that's big data, we hear a lot about that in the press. But how do we make our systems more efficient? How do we squeeze more profit out of the customers we have?

If we are in a lower growth environment than in the past, this becomes all the more important. And back to the point, how do we extract data and monetize that and create value to sell both to our suppliers and to our customers?

Stelton-Holtmeier: If you look at the numbers on the survey, you can see that many businesses are planning to invest in several different areas. That's an essential piece to succeeding with the technology investments to differentiate and to improve your business processes.

You have to have a cohesive strategy that intertwines all of your technology systems together, whether that be incorporating mobile tools or just implementing pieces to the ERP that incorporate many of the e-commerce platform pieces. There are a lot of options out there and a lot of things that you can look at, and it can be overwhelming. But it's a process that you have to begin. You can't work from silos to really invest in these technology plans.

Data is still one of the biggest challenges, as you mentioned, Michael. Big data gets a lot of headlines and a lot of attention, but for many people, that big data is a goal that is great for the long term. Right now, a lot of people are challenged with just getting clean data in their systems. They need data that their ERP system can read from their CRM system, from the pricing technology that can be translated for that key transparency piece that the customers and the manufacturers want.

Distributors have the potential to create more value for their customers with these comprehensive interfaces, but you have to build one that works from both ends for everyone who needs to use it. You have to make it accessible to the customers, to your employees, and even providing data from those resources to the manufacturer.

MDM published a report about point-of-sale information and how there's still a hesitation between some distributors and manufacturers to share that information. That's one of the things that can really increase that transparency and increase that relationship, improve that relationship between your supply chain partners.

The key here is having that cohesive strategy and not looking at these technology investments in silos. They have to work together, and they have to work with your business.

Capone: And I know that that can be overwhelming, there's lots of data out there as you mentioned, not all of it clean or complete. How do we take advantage of it?

We understand now what some of the threats are, what some general strategies are that some respondents are going to take to combat that, whether it's products or services. I think we understand the technology investment, but all of that then feeds into the question: How do we identify those new opportunities? How do we create the new services or the new value that the marketplace is going to want to buy?

The next part of our survey talks about how companies evaluate new opportunities. There's recognition that the evaluation of opportunities requires multiple factors, with customer feedback as the most prominent, but there's also a focus to exercise caution while making major investment decisions. To make large investments we need to have some level of comfort and certainty that they're the right investments.

What respondents said is that their number one method of identifying new opportunities was simply to talk with customers, and I think this is an often-overlooked true differentiator. It's not something that you can do online per se, at least not very easily. I have an example a little bit later on of how that insight can create a little bit of stickiness with your current customers.

Not every new customer is necessarily a good customer, not every customer request is necessarily in our best interest. How do we map those out and assess what we're going to do?

One that you really touched on, Jenel, is partnering with suppliers. We are in that unique position to help them and vice versa. How can we identify new products, new markets, and utilize our suppliers to assist in that?

Another one of my favorites is the association resources. I sit in on a number of CEO, CIO, CFO round tables, and I'm always amazed at the candid conversations. Putting a group of executives together in a room to talk about their businesses and have them share insights and best practices, I think is a great way of evaluating the opportunities.

Finally, look at the wealth of transaction data that we all have. Analyzing trends and being able to look to the customer and provide value to them, whether it's trend analysis, stocking information, supplier information; there's value here that we can monetize.

So we've looked at the threats, we've identified the new opportunities, we've created new products and services. What do we do to measure our success?

We asked our respondents that question, and they chose the top two indicators that they use to measure success. We've included the Top 5 here on slide 15.

As always, the best measure of success is dependent on the strategy and the goals set forth by each distributor, always with the customer at the forefront of those decisions, and oftentimes depending on where in the company's life cycle that they are, whether it's growth or maintenance mode.

Thirty-eight percent of survey respondents indicated that revenue growth is a measure, 29 percent talked about gross profitability. I certainly think that those are relevant; everyone likes to see top-line growth.

To me, the most relevant aspect is to have that top line translate into bottom line. All too often we are seeing companies sell more and earn less. It's a single indicator that we need to use in concert with others.

Fifty-nine percent of respondents talk about net profitability, and I think that that is truly the most relevant indicator for most. That really is the crossroads of revenue growth and increased gross margin.

I do think a key component to that though is SG&A, and that's something that's left out of these other metrics. That's a continued area of focus. We've all looked to streamlining and cost reductions; I still think there are opportunities in talking with other distributors.

The more creative, the more granular that they get in looking at some of these costs, and particularly given that some of these costs are within our control, these are items they can directly impact our profitability.

There are threats out there though, I know for a lot of us inflationary pressures continue, wages are going up, freight, drivers, there are certain parts of the industry where it's hard to find skilled labor and those cost pressures are tremendous and oftentimes not readily passible to our end customers.

Stelton-Holtmeier: There's often a challenge in measuring the success of something because you have to make sure you're measuring something that actually matters.

As Michael said, if you're selling more, great, your revenues are going up, but if you're making less and your margin is shrinking, is that something really that should be celebrated?

You need to increase both that top line and bottom line in order to really grow your business and be able to invest more to continue growing.

The second thing to keep in mind when measuring success is, are you measuring what you really think you're measuring?

In social science circles, there's a phrase that "correlation does not equal causation." Just because something goes up when something else goes up does not mean that one is causing the other. There's a great example of this in social science. As the stork population went down in Denmark, so did the birth rate. The problem is that both of these were being caused by the same thing, which was urbanization rather than the stork population actually being the cause of the birth rate going down.

The same is true in business. Sometimes it is that SG&A expense that is actually decreasing and it is not the fact that you're selling more. You're finding other ways to identify waste and identify redundancies within your business so that you can improve that bottom line, even if your top line isn't growing as much as you'd like it to.

Capone: I couldn't agree more, and I think the overall point is really a holistic view of your business. You have to look at the top line and at cost of sales, and you have to focus on SG&A. If you do all three of those, along with I'm sure a host of other items, that's ultimately what's going to lead to success.

That was the main findings from the survey, and we'll give you some information at the end of this to where you can find the actual white paper.

Next, I want to summarize those findings, add some thoughts, add some real world examples to a few of the companies I've seen and what they've done to really stay competitive and to offset some of this threat. There are no easy answers. If there were, none of us would be on this Webcast; we'd all be out spending the money we were making.

Knowledge is power to the extent that we can at least start recognizing some of the threats and the opportunities; then we can start to do some things about it.

I think one of the themes is the traditional distribution model is changing. Pure distribution is still valuable, but going forward I think there are going to have to be some tweaks to that.

On slides 16-17, we talk about services beyond distributing products and what those services could be. It could be doing the restocking and the inventory management for our customers; it could be consulting on facing and product placement, and really teaching our customers how they can sell to their end users, providing innovative and additive products, bringing those to our customer's attention.

One of my most successful distributors sold very high margin but low individual value items to big box retailers. Their strategy was to handle restocking; they had their representatives go to these stores, monitor levels, and what I like to say is "walk the halls," talk to the store manager and get their input.

It created a very sticky relationship where the retailers depended upon our distributor to do all that, and it's not easy to replicate. That personal touch, that walking the halls and having the ability to ask people, "What is selling?" and "What are your customers asking for?" Taking that knowledge back to corporate and using that to hopefully identify innovative and additive products.

The end result was that this client started with one product class that fit that mold, the high margin/low value, and they identified other products that had high margin/low value, very different products, and ultimately expanded to five different product categories, all of which were very profitable and all of which created that additional stickiness. They became one of the key suppliers to a lot of these large retailers.

It's a combination of solutions that we've talked about, but a real life success story on how one can do that.

As I mentioned, the traditional distribution model is changing a bit. It's not just about providing more SKUs and faster delivery, and it certainly doesn't want to be competing on price and price alone. None of us want to be known as the lowest cost provider; I think all of us want to be known as adding the most amount of value to our clients.

Jenel, you touched on this and we talked about light manufacturing and assembly, kitting as you mentioned and again, moving away from that traditional model.

I think to one of my apparel distributors that moved into embroidery and screen printing and doing some things from a fashion perspective that increased the value of the product greatly. I think of an electronics distributor that started as basically a national distributor, part by necessity. Their suppliers were demanding that they have greater geographic reach, they wanted to grow overseas. But they were able to work with their suppliers and partner with them and receive financing breaks to help them grow.

Expanding globally was certainly part of that, more importantly though, they used their knowledge of these products to create bundles of products and, with that, the services and the integration that went into these. They really became much more of a service and an integration provider, and again, it was seen as higher value and it was part of the key to their success and growth.

And it wouldn't be a Webcast if I didn't at least mention a couple areas where Grant Thornton has some service offerings that can help. From performance improvement, looking at capital structure and financial data, to profit mapping, and being able to help assess certain products that are on the market, certain bolt-ons that you can add to an existing ERP system, integrating that with IT.

One that I do find very interesting is tax in general, and as we ask you to think outside the box, some of these expanded activities create new tax opportunities that maybe you haven't thought of before. Maybe this also goes back to the SG&A to the extent that you're doing product development or working with customers or creating new technology for racking. There might be some other opportunities to claim credits that traditionally distributors have not found yet. But with that said, we wanted to leave time at the end of the presentation to answer any questions that you might have and we do indeed have about five to ten minutes. So Jenel, I'm going to open it up to any questions that the group might have.

Stelton-Holtmeier: Great, thank you so much, Michael. And so let's start with this first topic: Where do you begin? Where can a distributor begin to really try to identify ways to differentiate their business model?

Capone: That is the $64,000 question. I always tell people: start with bite-size chunks. Let's focus on one area, move forward with that and then nibble away at other areas.

I do think one of the easier places is to leverage one of your strengths that you have, and that's the personalization and the interface you have with your customers. If you're not already, maybe bake that into your periodic communications or with your sales force to expand the communications, to ask customers what they're seeing, to look for trends.

The other one I think can be expensive, and it'd be great if we all had the resources to go out and implement all those new systems that we talked about, but using the data that you already have. A lot of us do have fairly sophisticated ERP systems. We've got lots of data; how do we start interpreting that? There are some solutions out there as it relates to profit mapping and cost to serve. They're not terribly expensive solutions, to leverage what you already have out there and maybe use that more effectively. Those are two of the areas I would suggest starting.

Stelton-Holtmeier: Another question that came in refers to what I was talking about, the point of sale information with manufacturers. Are distributors charging a fee for sharing that information?

Based on the research we have, there's very little consistency with sharing that point-of-sale information. That's one of the areas that there really has to be open communications between the manufacturer and the distributor to determine what the benefits are for every party and whether that be having a fee or discount tied to providing that information to the manufacturer. I think one of the most effective things that came out of the conversations that we've had previously about point-of-sale information is really using that information and sharing how that information is being used to guide the conversations that you have with your supply chain partners.

The next question, in follow up to the answer that you had just given about where to begin, you had said that none of us want to be viewed as the low-cost provider. Did you mean to say low-price provider there?

Capone: It might be splitting hairs. I think we all want to be seen as providing the most value. If we're competing purely on cost or price, however you look at it, ultimately that's driving down our profitability and it's going to be, I think, ever more difficult to compete on price alone.

Amazon is very price competitive, so to me it's that overall value and that's where the services factor in. It was a generalization, not to say that some of you certainly don't want to be known or seen as a low-cost provider, but I would prefer to compete on value and being seen as the best value for the money as opposed to the lowest price on the market.

Stelton-Holtmeier: You and I have both used "value" several times in this presentation. Would you say that technology has changed what we've traditionally thought of as value? Has it changed the meaning of the word?

Capone: That's a good question. Yes and no. At the end of the day, value is what your customers perceive and if they're happy with the product that they got, or the product and service for the price they paid, ultimately that's what value is.

Does technology help us refine what that might be? Does technology maybe help us articulate our value propositions? I think there's where the answer is yes, to the extent that we can quantify value that might not have been perceived in the past.

That's where cost-to-serve comes in, and get in front of our customers and say, "Hey you're asking me to lower prices, but have you considered all these other things that I have traditionally provided and how that factors into the overall value model?" I do think technology assists in quantifying some of those where we didn't in the past.

Stelton-Holtmeier: The economy has obviously been on a lot of people's minds over several years, but how do you think that the pace of the economy and market activity impacts customer disintermediation activity? Do you think it has an impact?

Capone: Yes, absolutely it does. Getting back to cost; there has been a greater focus on dollar cost as opposed to value over the last several years and the recession certainly led to a lot of that. I think many of us have seen our customers wanting price decreases, shopping around, using the transparency that currently exists with pricing to push on that. I sense that turned a little, I think that's become somewhat ingrained. I don't think anytime soon we're going to see there be less of a focus.

But I do see a little bit more value placed on services and some of the, call it intangible if you will. From an overall economic standpoint, we're not in high growth; at least overall, I think we need to adjust our business models to take that into account.

I think there's some cautious optimism for the remainder of the year. I'm not an economist but I just look within my client base, I do see more investments being made than I have in recent years. So yes, absolutely that has an impact. I think we're still seeing some favorable aspects to the current economy, but unfortunately price or cost tend to still be very high on most customer's lists.

Stelton-Holtmeier: One of the other things that we touched on a lot is the changing behaviors of the buyers as the millennial generation comes in. Do you think that because of this there needs to be a shift in the distribution business model itself?

Capone: I don't think the model is going away. I know distributors add great value within the supply chain, and we all serve a function that can't be easily served elsewhere. Some of the folks that go back to the '90s, we didn't see manufacturers going en masse direct to the end users. I don't see that as that great a threat. I think we add a lot of value; it's about articulating what that value is.

It's beyond just being low cost or low price, it's adding those additional services. And maybe that is where the model is changing a bit, where we're quantifying what that is, looking for ways to add value. It might be about doing some light manufacturing, some software type integration, certain services that in the past we didn't do. But overall, I do think the model will remain intact but will change for the times.

Stelton-Holtmeier: Michael, I'd like to thank you again. And we'd also like to thank Grant Thornton for its partnership in this program today. You can learn more about Grant Thornton at grantthornton.com. Thank you for joining us today and this concludes our program.

mdm webcasts

FIGHTING DISINTERMEDIATION:

HOW DISTRIBUTORS DEVELOP, DELIVER AND MEASURE VALUE

Featuring: Michael Capone and Jenel Stelton-Holtmeier

September 4, 2014

Produced by:

Modern Distribution Management®
Wholesale Distribution News, Expert Analysis & Market Research

Event Sponsor:

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Agenda

- Introduction
- Presentation: Fighting Disintermediation
  - Results from Grant-Thornton/MDM Survey
  - Best practices for differentiating
  - Measuring success
- Q&A

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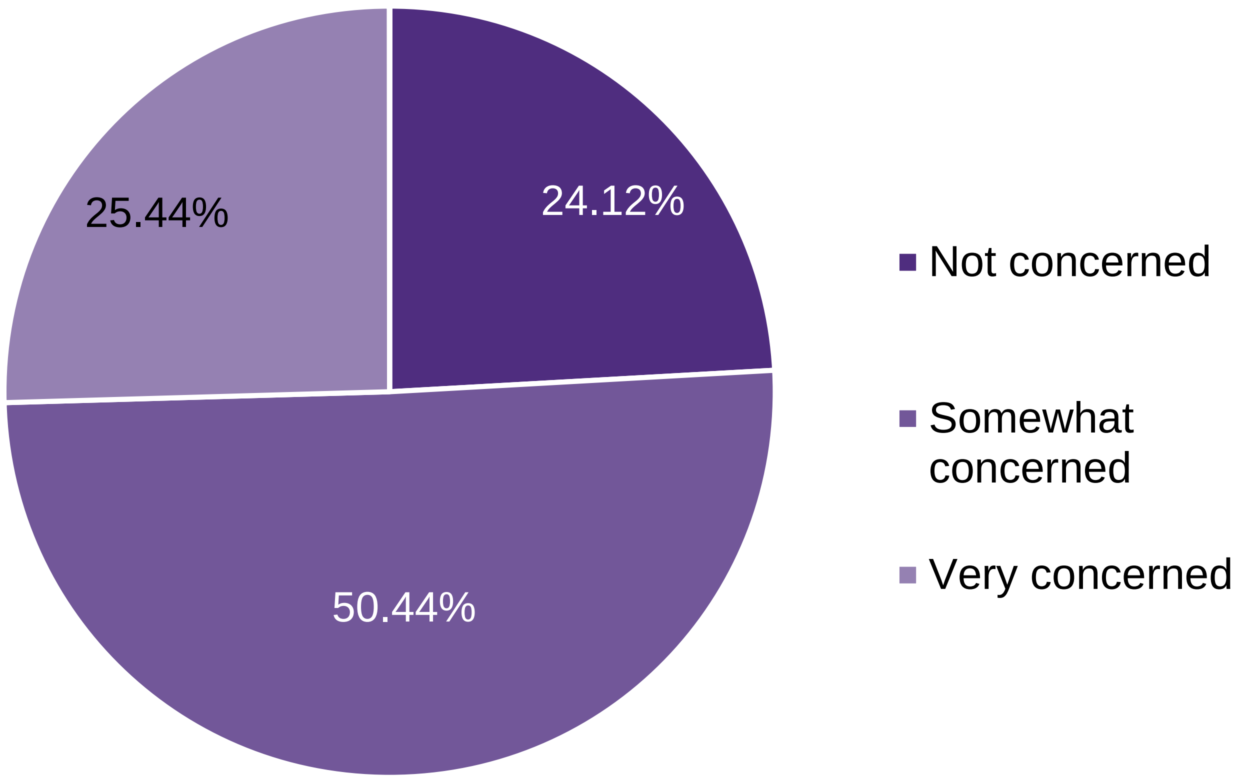
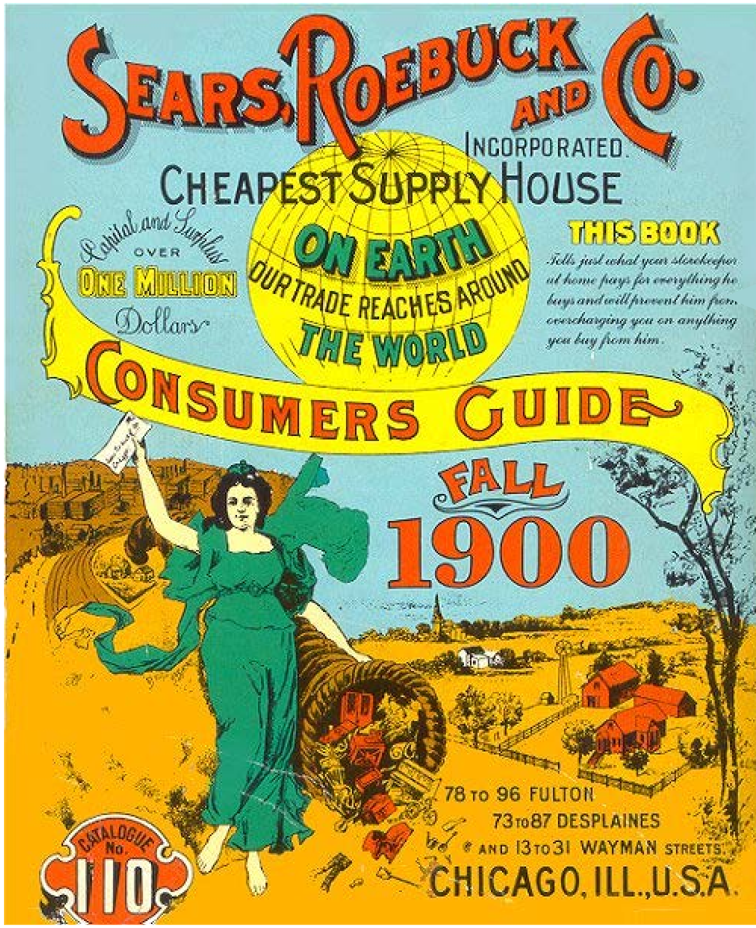
LEVEL OF CONCERN FROM DISINTERMEDIATION



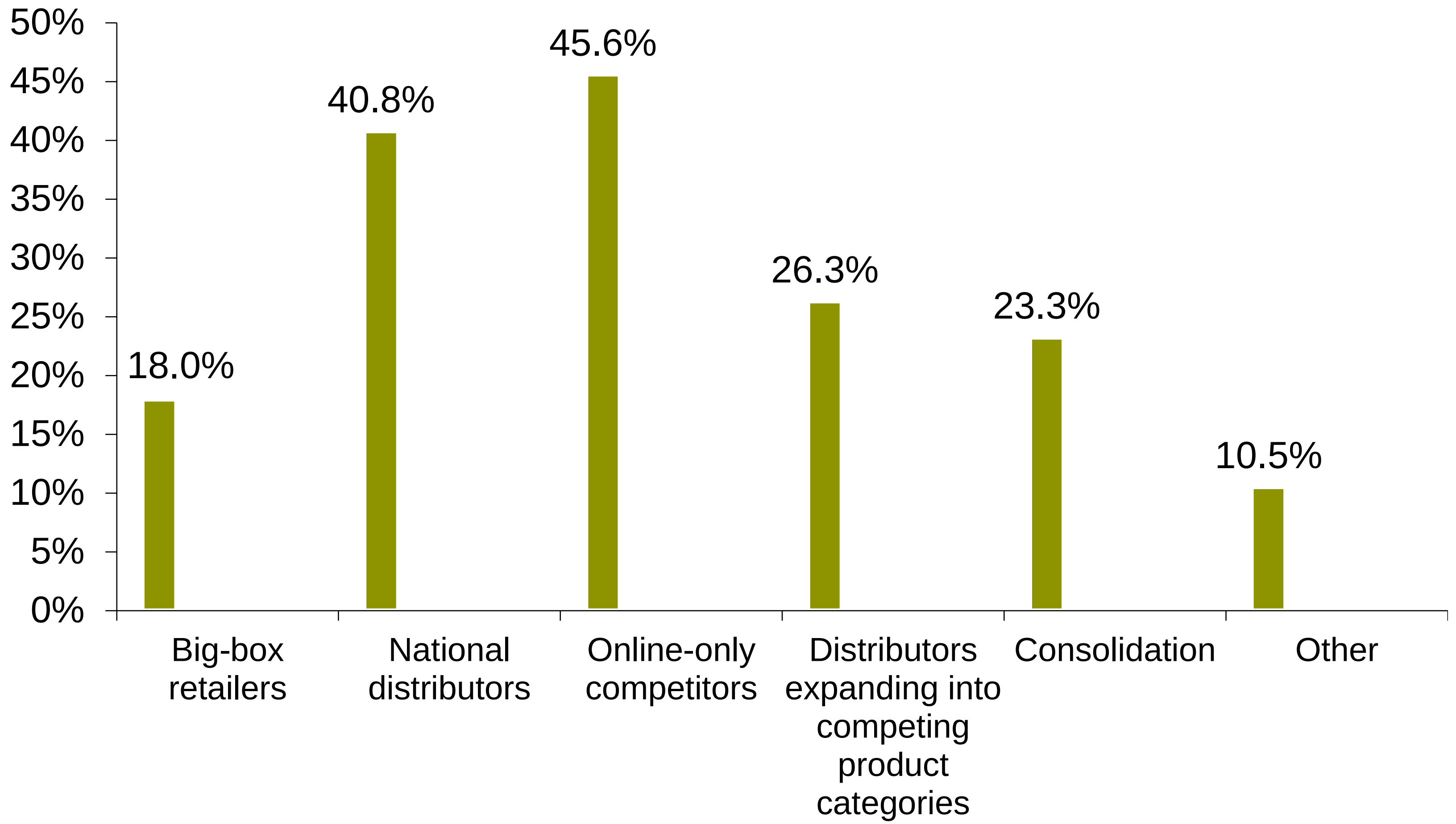
History of Competitive Changes



THIS BOOK

Tells just what your storekeeper at home pays for everything he buys and will prevent him from overcharging you on anything you buy from him.

MOST PRESSING COMPETITIVE CONCERNS



COMPETITIVE CONCERNS

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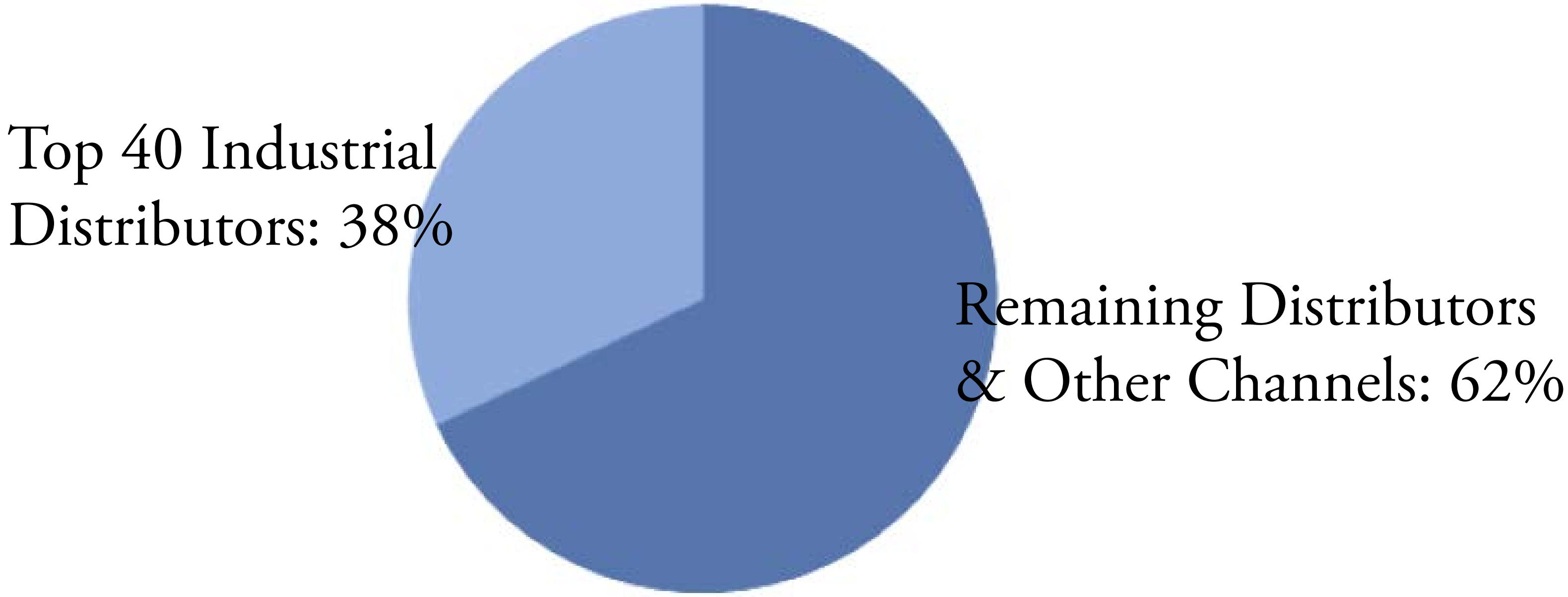
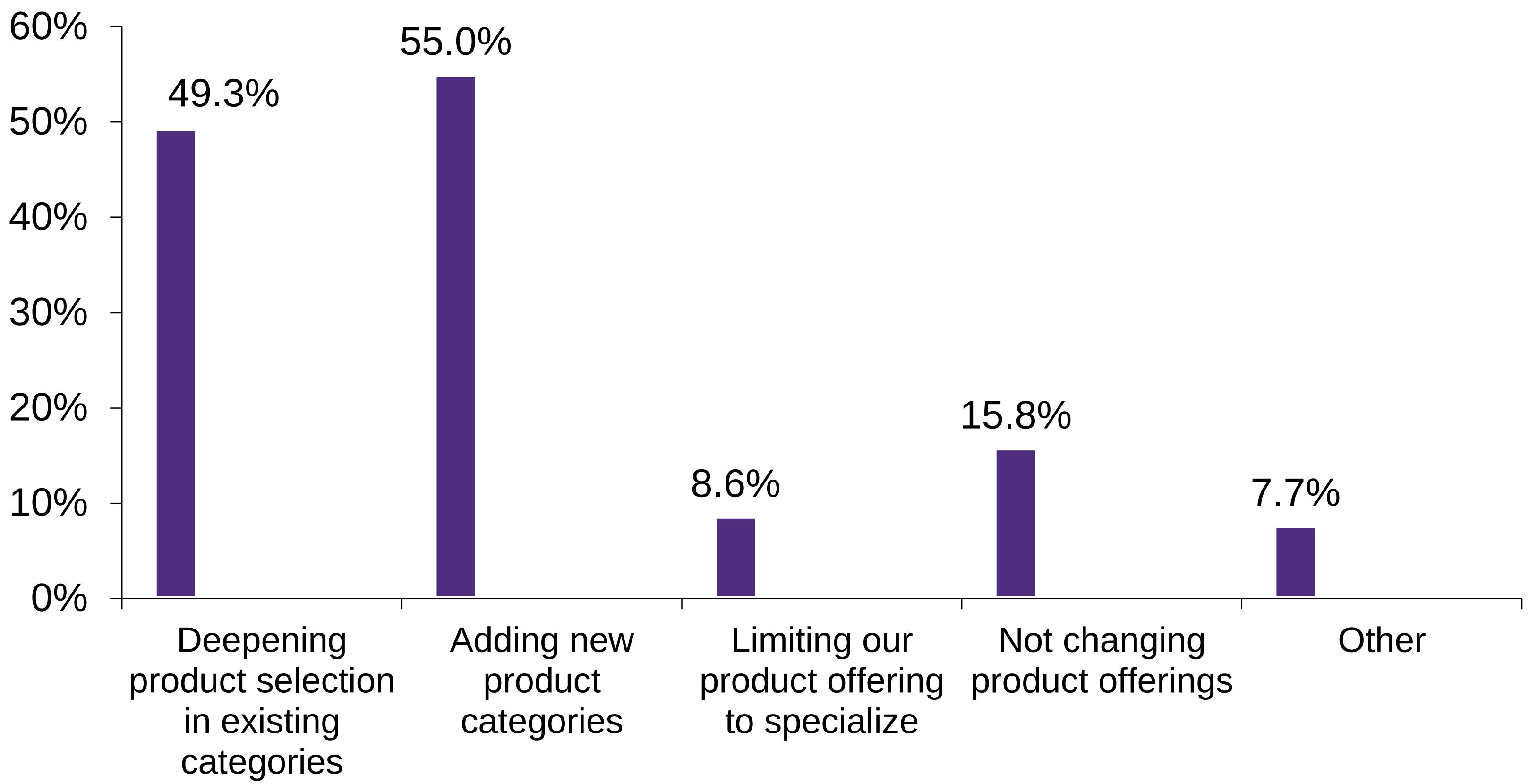
COMPETITIVE CONCERNS

National Distributors/Market Consolidators

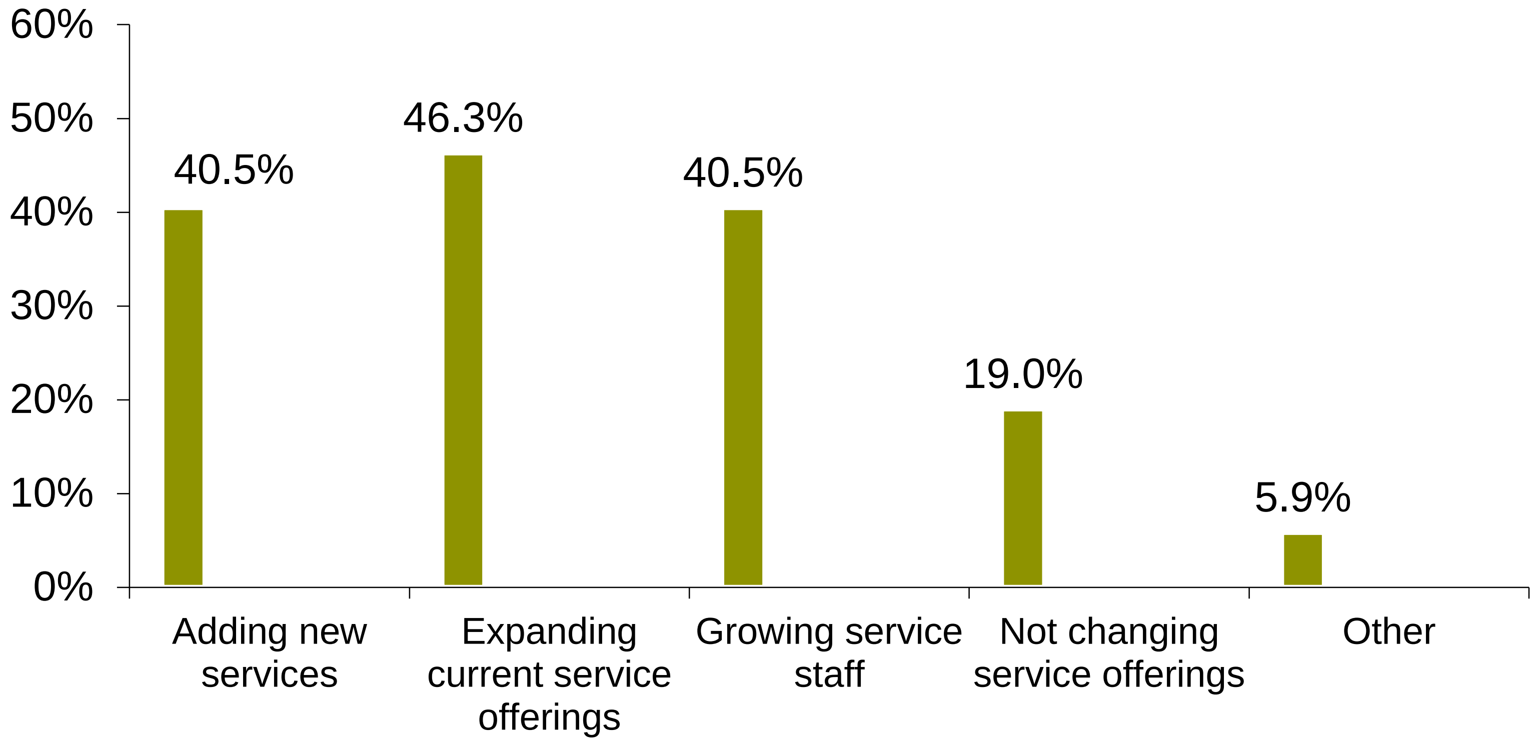


Source: MDM 2014 Wholesale Distribution Landscape Report

PRODUCT DIFFERENTIATION PLANS



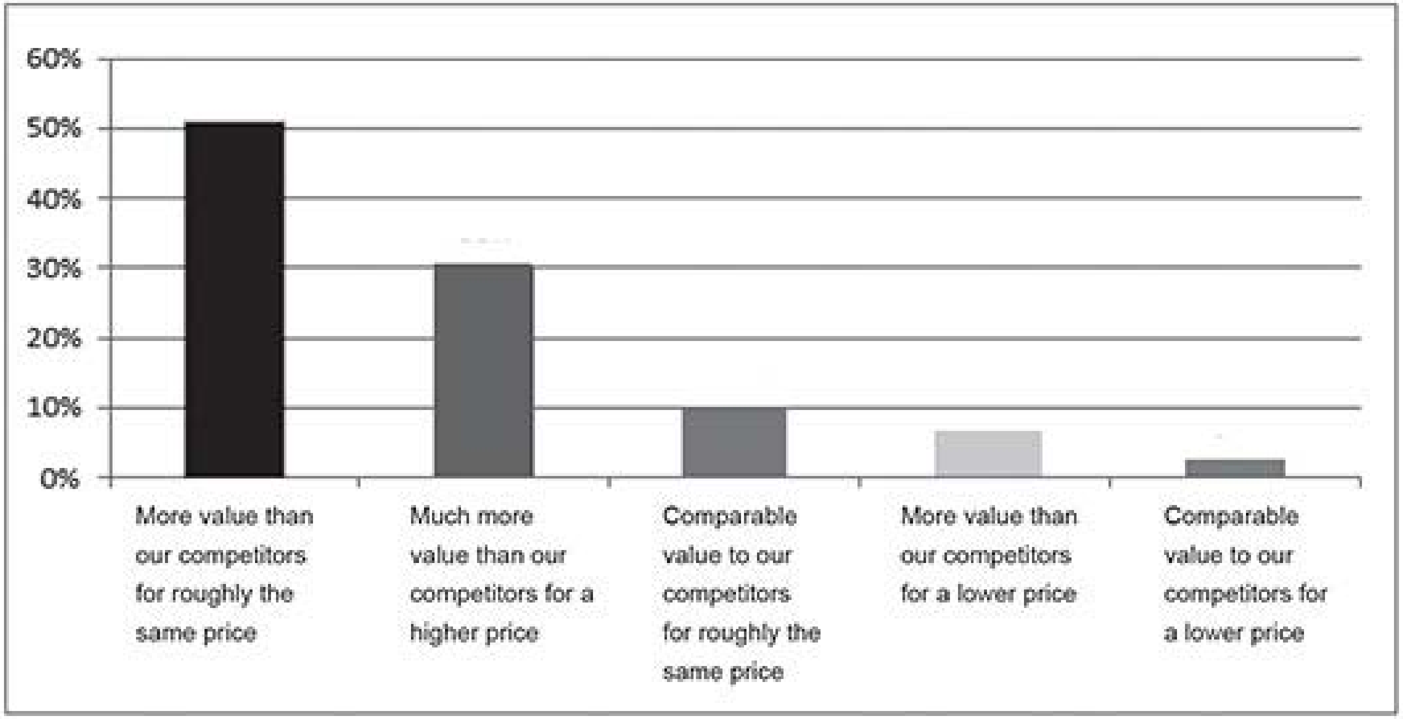
SERVICE DIFFERENTIATION PLANS



SERVICE DIFFERENTIATION

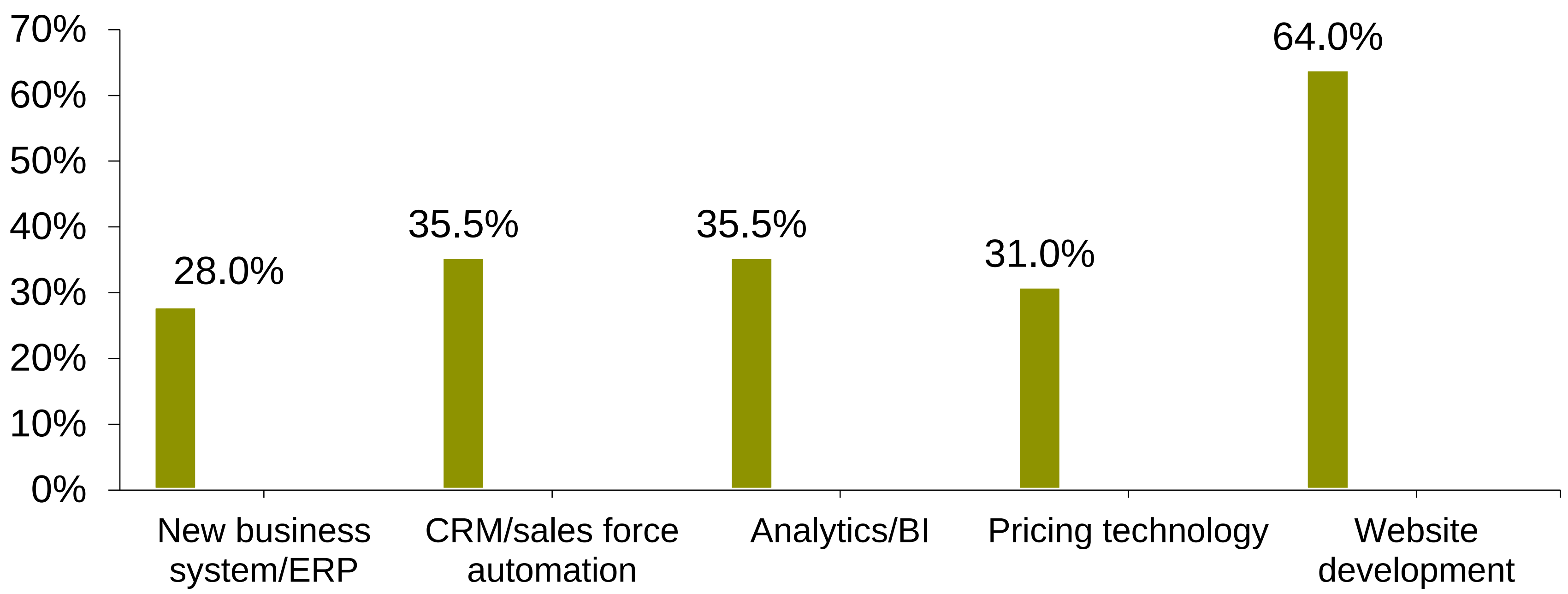
- 1-Click Ordering
- Free shipping
- Corporate credit lines
- Gift/store cards
- No order minimums

SERVICE DIFFERENTIATION



Source: *Modern Distribution Management-* Real Results Marketing

TECHNOLOGY INVESTMENT PLANS



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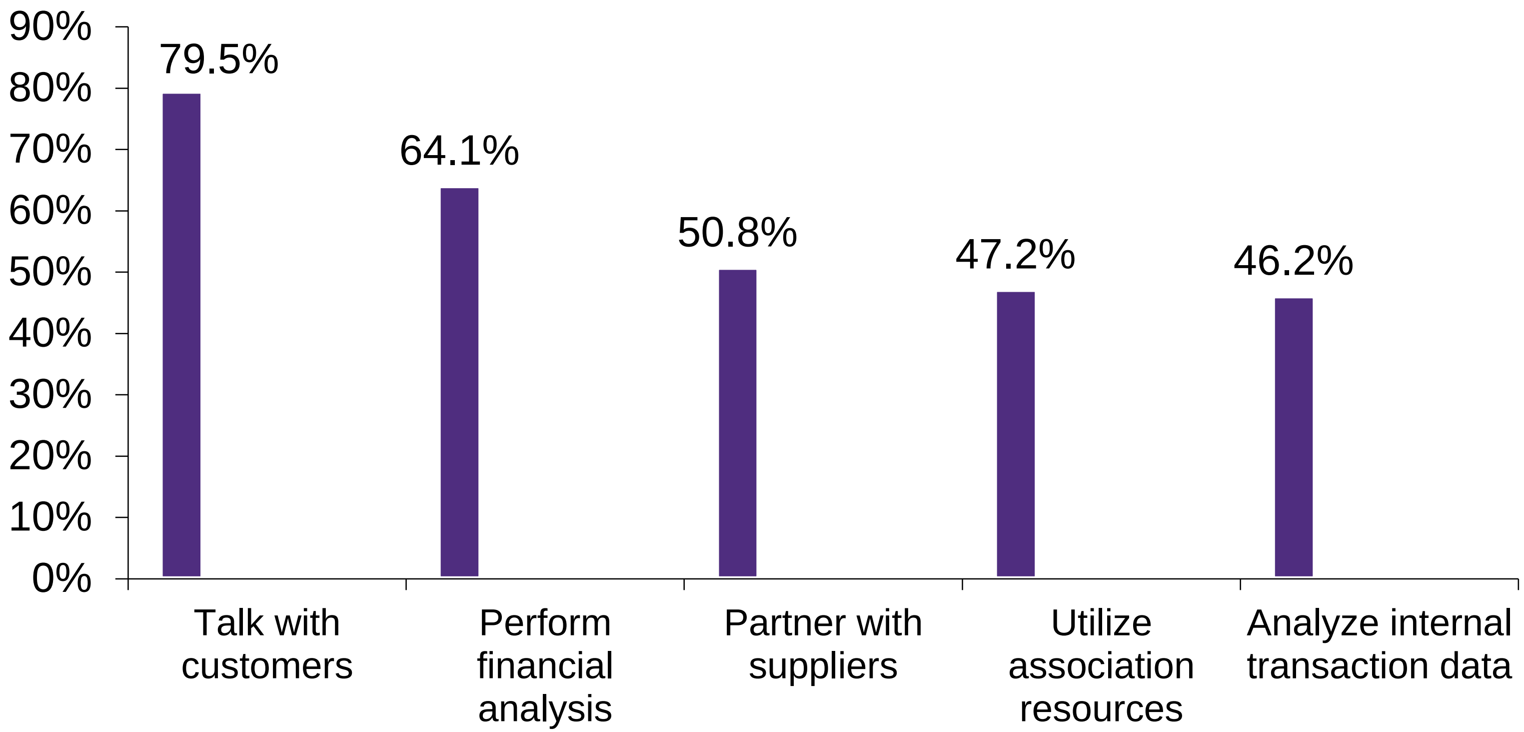
EVALUATING NEW OPPORTUNITIES



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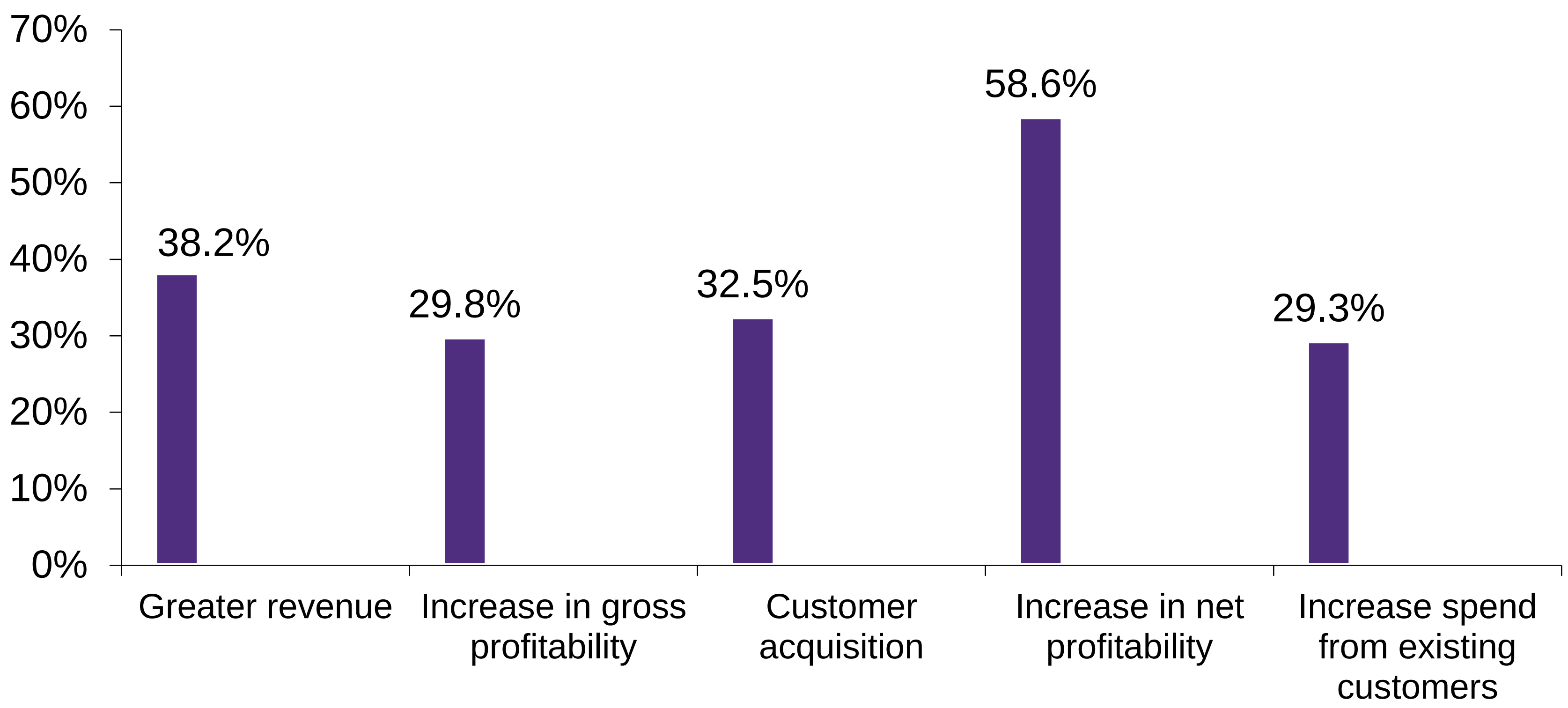
TOP INDICATORS USED TO MEASURE SUCCESS



STAYING COMPETITIVE

- Distributors can offer services beyond distributing products:
  - Re-stock products
  - Consult on product placement
  - Provide innovative and additive products

STAYING COMPETITIVE

- Distributors can add value to distinguish themselves from price:
  - Light manufacturing and assembling to make larger components
  - Product tutorials
  - Expand online capabilities
  - Primary focus on customer satisfaction

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SOLUTIONS

Performance improvement
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Operational advisory

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