The Big 3 market strategies

BY JOE SULLIVAN

When you boil it all down, everybody in this business goes to market in one of three ways, or maybe a combination of a couple of them. When it comes to distributors, though, the best of the best are usually the most focused. The days of all-things-to-everyone electrical distribution are over. Distributors need to have clear and distinct approaches to the market. The three basic approaches (we might call them the Big Three) are:

- Convenience;
- Lowest delivered cost;
- High service/knowledge.

A distributor who wants to do well over time—or even to build value for a possible future sale of the business—needs to determine which approach best suits his or her company's strengths and markets, and then explicitly focus market planning and most other strategic decision making on that approach.

In the arcane language of the marketing gurus, there is a term for "approaches to the market," and it makes more obvious sense than many things said in the "marketese" dialect. The term is "value proposition." Of course a value proposition can have quite a bit more substance

In this section:

Illustrations by Kevin Hopkins

than the three outlined above. But stripped down to the bare essentials, every electrical distributor's value proposition is based on one or more of the Big Three. We will look at each in turn.

1. Convenience value proposition offers customers rapid and easy access to the items they use the most. Think of it as a 7-11 Electrical Supply model. The convenience electrical distributor goes to market in much the same way as any other convenience store operator. Inventories are tailored to the most common needs of the customer—and are not very deep. We are talking mostly about A and B items. Location is very important to the convenience value proposition. This may be through counters near major customers, on-site trailers or perhaps mobile units that make house-calls, so to speak (like roach coaches for pipe and wire). Convenience can also have service elements such as kitting of parts, though the level of service is limited.

2. Lowest delivered cost is a value proposition that requires buying power and considerable logistical skill. It is the most difficult of the value propositions, especially for smaller distributors who lack economies of scale.

Lowest delivered cost is pretty much the mindset of the European giants like Rexel and Sonepar, and certain big American firms as well. Obviously, lowest delivered cost is heavily price-driven, but it can also include features that reduce the customer's cost of purchasing or receiving. For that reason, lowest delivered cost is a big part of the as-yet-to-be-realized promise of both EDI and the Internet. Very low error rate shipping, and reduced paper ordering and receiving can play a big role in this value proposition.

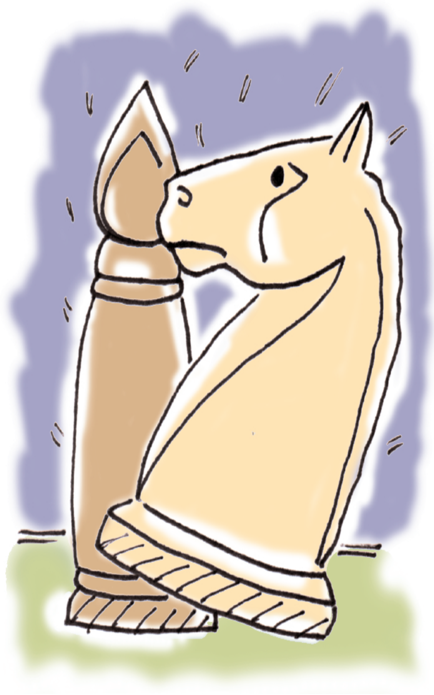
For example, a commercial or industrial customer may set up a process whereby anyone on a given list may order from a trusted distributor, without going through purchasing or generating a P.O. The customer is presented with a single bulk invoice at the end of each month, or perhaps billed through a corporate credit card, and merely given an itemized monthly statement.

Another proven approach is to provide the customer with a CD-ROM catalog keyed to the customer's own internal part numbers. This can also be done on Web sites, of course. There are plenty of other ways to play the game. The point is that anything that appreciably reduces the customer's cost of doing business with the distributor is just as much a part of the lowest delivered cost value proposition, as is raw price competition.

3. High service/knowledge value proposition is a beast of a different nature. It relies on value-added services to attract customers and develop bonds between them and the distributor. The key to success in the high service/knowledge value proposition is to provide expertise not easily developed, on which customers will depend, and which is not sold primarily on price. All distributors offer service. It should not be inferred that the previous value propositions will succeed without good service. However, some distributors offer appreciably more in terms of expertise, training and assistance. These are often industrial houses, or those with strong lighting or voice, data and video businesses.

Service/knowledge distributors tend to keep experts on staff. They may offer customers various levels of technical training in installation, software or special features and applications. They may offer design services or easy access to help and support. In some markets where it does not wreck customer relationships, they may even edge into installation and start-up work.

Some distributors with the high service/knowledge model do nothing especially technical, but have developed deep expertise in identifying and sourcing supplies for specific industries. In effect, they build their business around what might be "C" or "D" items for other shops. Examples of niches that lend themselves to this kind of specialization include: specialty lighting for the hospitality industry; mining (especially the big electric digging and hauling equipment); and electric public transportation and overhead trolley supplies. There are probably dozens of other niches like these, but these examples are enough to make the point.



The days of all-things-to-everyone distribution are over.

Multiple choice

Some distributors appear to be able to make multiple value propositions work. This is especially true of larger, multi-branching operations, which may be, for example, lowest delivered cost contractor houses that have a lighting branch with a specialized niche. However, many such distributors would be very surprised to learn how much more profitable they could be if they narrowed their focus to what they can do best and most profitably, even if that means losing customers and sales (Gasp!! Wheeze!! Clutch chest!!).

It is simply a fact that distributorships are geared toward their primary lines of business in everything they do. Other things tend to be done less skillfully, and therefore less profitably. Furthermore, excess staffing may be required that cannot fully be absorbed by small niche operations. If a distributor's business system, purchasing practices and management mindset will permit it, multiple value propositions can work in theory, but the actual success rate in the real world is not especially high.

Focusing often brings profit growth at the expense of sales. It is a pretty good trade-off, when you think about it. One multi-branch distributor in the mid-Atlantic region made a decision to move into the convenience value proposition, and geared his market planning and purchasing toward that. He also kept his margins high, although early on that involved some real fights with some of his sales force. He lost "business," but gained profit. He has now been in the upper edge of NAED PAR margins and profitability for several years, and has a good, focused and successful business.

A distributor in the Southeast recognized that as a very small shop she had serious competitive disadvantages in the "full-line" contractor business, and also that such business does not make very much money anyway. She developed deep expertise in hospitality lighting, including sourcing obscure lamps and hard-to-find replacement fixtures. She also built a service-oriented team. With this, she left the contractor market entirely and, though still small today, has a bottom line as big as many much larger houses, and enjoys intense customer loyalty.

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A sizeable regional industrial house with Rockwell/Allen-Bradley as a lead line, decided to move away from a "whole market" approach, and focus on the industrial business and various related billable services. Its sales declined by several millions of dollars, while at the same time, its bottom line went from losses to very respectable profits.

For market planning, the implications are obvious and significant:

- **Do not be seduced by the "whole market"** when you gather data and make sales plans, but rather, think in terms of the clearly defined market in which you can do best;
- **If your company or branch is not focused, try to bring focus to it,** so as to clearly understand your own market and its requirements—which may be very different from those of the distributor down the street who serves somewhat differently defined markets;
- **Commensurate with the above, ditch the old concept of "full-line" distribution,** and provide only as full a line as your customers require—they will be just as satisfied (probably more so), and you will have much lower inventory and transaction costs;
- **In your planning process, look primarily at market information that directly affects you** and don't get rattled by extraneous data; e.g. if you are a residential contractor house, forecast housing starts mean a lot to you, but if you are an industrial automation distributor, you may not care all that much.

Profit is the ultimate business scorecard. Measured by profitability, the most successful men and women in this business are usually those with the best market focus. They do not try to be all things to all people. They know what their market is, and what it is not. They plan and make business decisions on profit with sales volume as a secondary issue. They and their employees live well.

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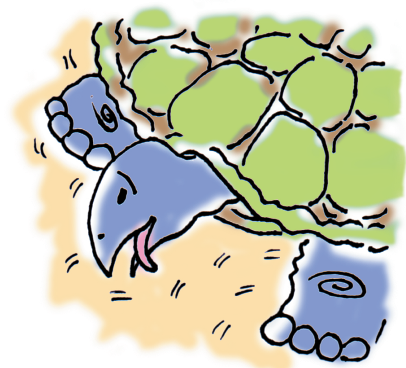

Slowing economy hits MROs

BY JOE SALIMANDO

Economic activity in manufacturing declined in April, according to the National Association of Purchasing Managers (NAPM), for the ninth consecutive month. So the recession that hasn't shown up in gross domestic product figures certainly has made itself apparent to MRO-oriented electrical distributors.

As reported by NAPM, the widely quoted purchasing manager's index (PMI) read 43.2% in April. More importantly, the index dipped below 50—at 49.9%—in August of 2000. A reading below 50 is thought to indicate a contraction in manufacturing.

What's more, the PMI has stayed below 50% since August, with the figure going below 45% in December and staying there for five months (thus far). And the NAPM's "Backlog of Orders Index" did not grow in April—the 12th consecutive month that it declined or was stagnant.

Essentially, with current business down, future business not looking good (as of writing this article), and the backlog stagnant or worse, it's unlikely that industrial concerns will be