Marketplace Strategy for Distributors

By Ian Heller and Jonathan Bein, Ph.D.

Large digital marketplaces are forcing distributors to rethink their ecommerce strategies.

Since the beginning of ecommerce, distributor websites have primarily offered one company's product assortment – their own. It is time to reconsider this paradigm. B2B customer buying preferences are shifting toward the simplicity of online marketplaces. Distributors whose websites only reflect one company's products will suffer a major disadvantage.

In this whitepaper, we will explore what marketplaces are, their value proposition and how you can adapt your ecommerce strategy to compete.

Digital Marketplaces: The Modern Disruptor

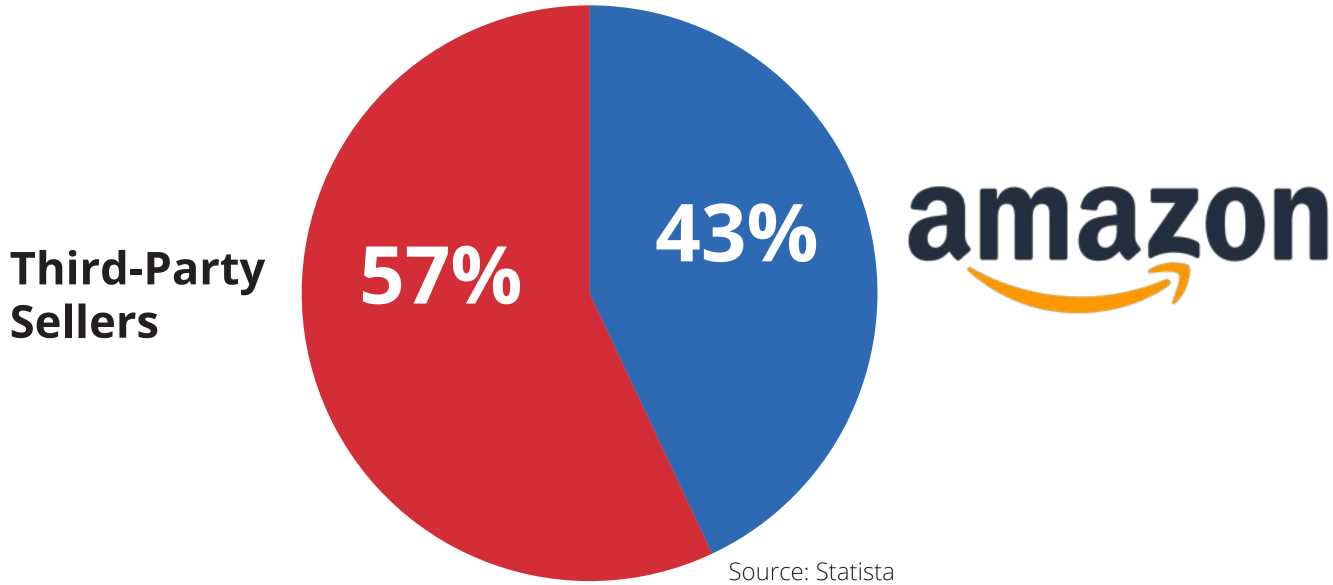
A digital marketplace is an ecommerce platform connecting sellers to customers. Some marketplaces only work with third-party sellers and do not own or move inventory. Other marketplaces (like Amazon) are hybrids, meaning that while they have a network of third-party sellers such as distributors, retailers and manufacturers, they also sell products out of their own stocks.

The value proposition of marketplaces goes back to the telecommunications era. Metcalf's Law explains that the value of a telecommunications network is proportional to the square of the number of nodes. In other words, if you only have two phones connected to your network, you can only make one connection. If you have eight phones, you can make 28 connections – which drives up the value of the network exponentially.

The same can be said for online marketplaces: The value of a marketplace rises as the number of users (buyers and sellers) increases. Because of this, most digital marketplaces derive value from their connections rather than from owned assets.

For instance, Airbnb is a platform that connects renters and property owners. Although Airbnb owns almost no properties, the company generated $47 billion in bookings last year. The same can be said for eBay; although eBay does not own any warehouse space or inventory, the company generated $87 billion in Gross Merchandise Volume (GMV) in 2021.

Third-Party Seller Share of Amazon



Source: Statista

Amazon is another example of a disruptive marketplace. Statista estimated that in 2022, 57% of Amazon's gross merchandise sales would come from third-party sellers. In many cases, Amazon has never held the inventory that it sold. Instead, a third-party seller did the picking, packing and shipping; Amazon was just making the connection between buyer and seller.

Marketplaces offer just about everything – from creative expertise via Upwork to romance (some DIY required) via Match.com. In this report, we'll focus on two types of merchandise platforms:

- **Broadline Marketplaces:** These marketplaces operate across many categories and customer segments. Examples include Amazon Business, Zoro and Varis.
- **Vertical Marketplaces:** These marketplaces are more niche; they have focused products and customer segments. Examples include GHX (healthcare), ePlane (aerospace parts) and Verical (electronic components), a division of Arrow Electronics.

A substantial number of B2B marketplaces are in development or already operational. In fact, Digital Commerce 360 reports that there are at least 400 marketplaces in the B2B space. While most of these marketplaces are vertical, the number of broadline and multi-segment sites is growing.

With so many digital marketplaces available, we asked 344 distributor customers how many they buy from. The majority of respondents (55%) said they buy from three or more; only 12% answered, "none."

UK consultancy Wunderman Thompson recently released a study that surveyed various B2B buyers (including those in the U.S.) about how they buy indirect materials. The respondents from small and mid-sized companies reported purchasing from Amazon and Amazon Business more than any other supplier or channel. While Amazon wasn't the top choice for enterprise-level companies, larger organizations still reported making between a quarter and a third of their total purchases through online marketplaces.

As a final point, we asked 167 manufacturers and other suppliers to distributors about their relationships with traditional distributors and how they expect those relationships to change over the following five years. Respondents reported they expect sales through traditional distributors to fall from 64.9% to 52.2% over the next five years. In contrast, they expect sales through marketplaces and pure digital distributors to rise from 9.5% to 17.1%.

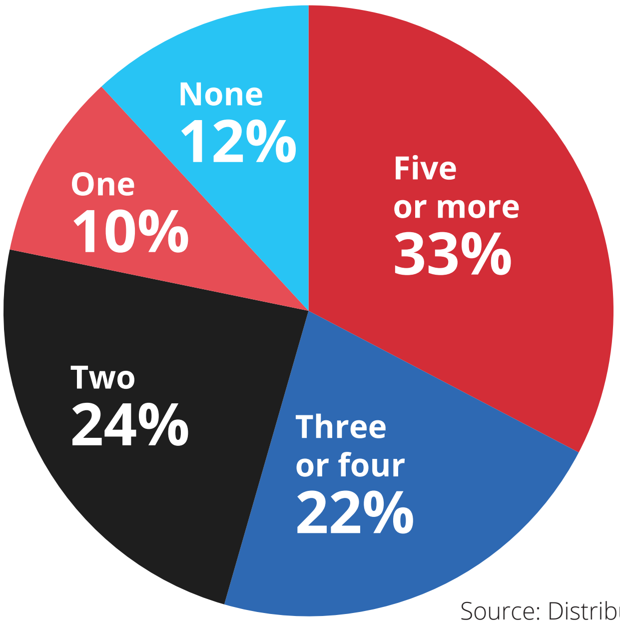
Distributors' channel partners agree – marketplaces are taking share in B2B. Distributors must reevaluate their digital and marketplace strategies to protect their customer base and market share.

Successful B2B Marketplaces

Of the 400+ B2B marketplaces, a few stand out from the rest. Amazon Business, for example, is one of the largest B2B marketplaces in the world. Digital Commerce 360 estimated that in 2022, Amazon Business would account for 32% of all B2B marketplace sales. In addition, the same report found that nearly 40% of business buyers make at least 26% of all corporate purchases on Amazon Business.

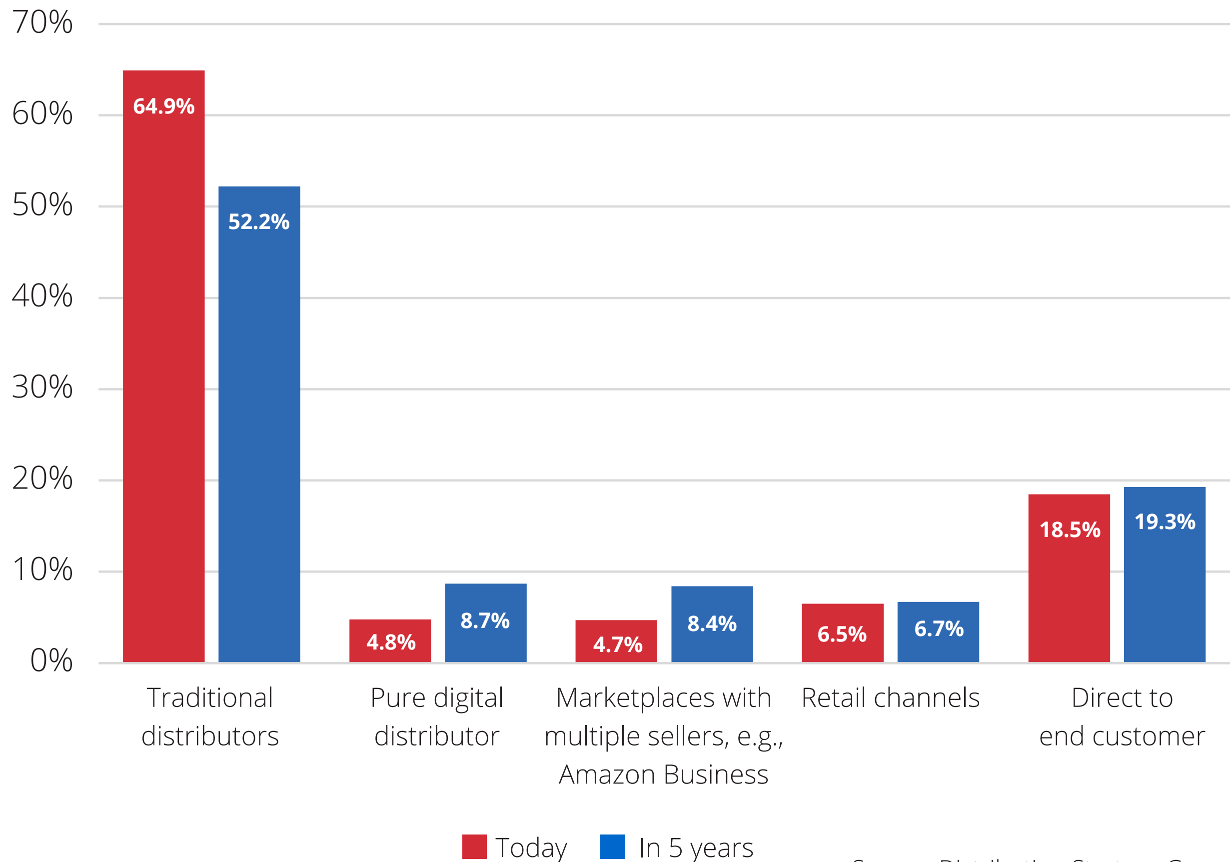
Amazon Business is open to customers of all sizes and offers added value through features such as detailed analytics and discounts for customers who use their Amazon AmEx cards. Amazon Business and distributors target many of the same industries. Many of the organizations highlighted on their "customer success stories" page look like ideal distributor targets.

Number of B2B Marketplaces Distributors' Customers Buy From



Source: Distribution Strategy Group survey

Manufacturers' Sales Expectations by Channels



Source: Distribution Strategy Group survey

Another example of a prominent B2B marketplace is Varis, owned by the ODP Corporation (formerly Office Depot). ODP hired several executives who built Amazon Business to build Varis and compete with their former employer. The company defines itself as a "digital commerce software-as-a-service and procurement company" and has a closed network of "trusted" partners across multiple marketplace categories.

Other notable and emerging marketplaces include:

- Supply Tigers
- Bay Supply
- eBay Business Supply
- Alibaba

Understanding the Value of Digital Marketplaces

Distributors' value-added services are their most significant advantage over marketplaces. Unlike traditional distributors, digital marketplaces are standardized and designed to fulfill basic needs. Marketplaces do not offer many value-added services because they don't want to have any people involved in their transactions. By simply taking orders and exchanging information between the buyer and the third-party seller, marketplaces can scale without incurring variable costs.

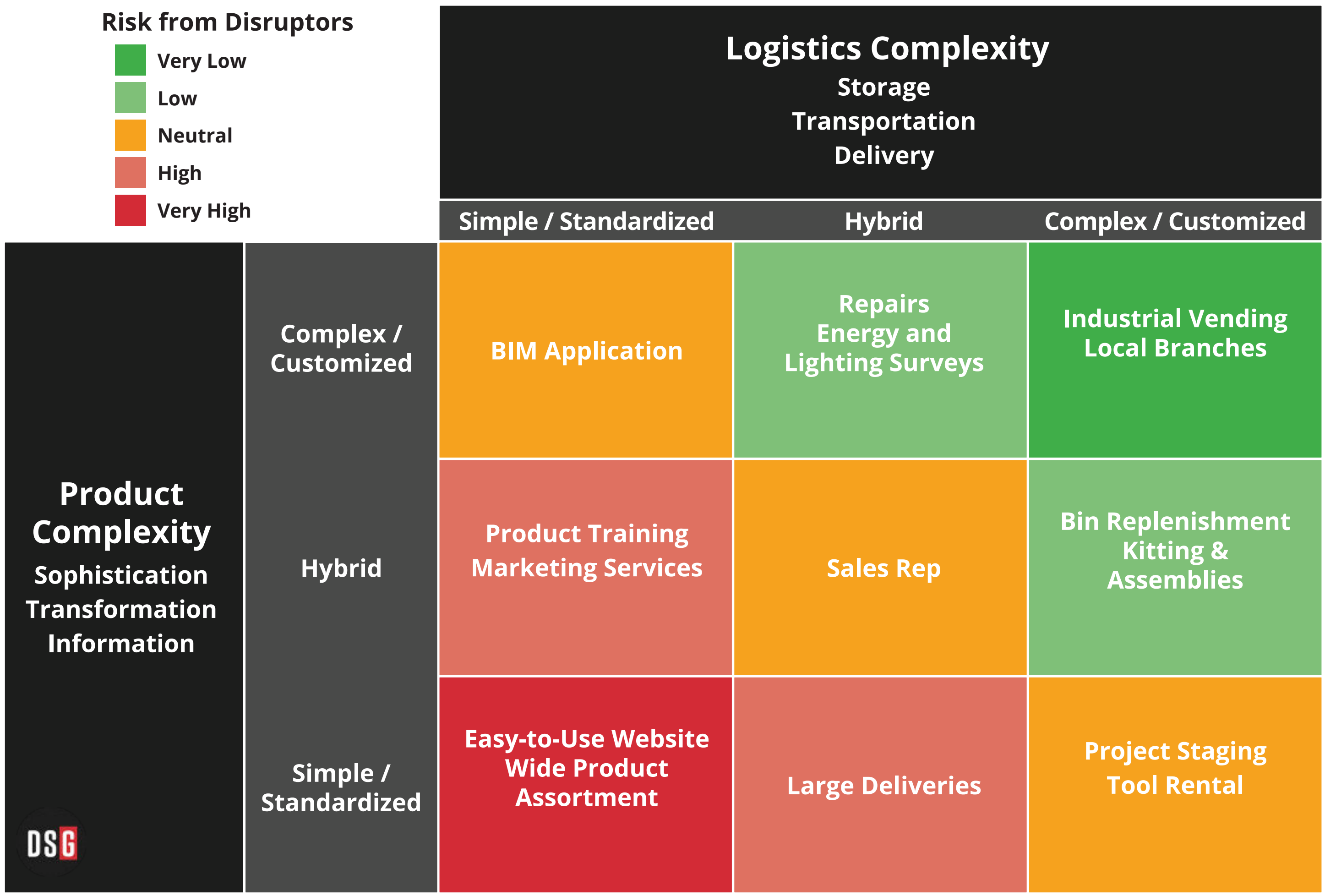
Unlike marketplaces, distributors have employees involved in every order shipped from their own stock: Someone has to pick, pack and ship the merchandise. Most distributors have outside sales reps and people who answer the phone. That brings additional cost vs. a pure digital model, but it also means distributors can offer extensive value-added services to meet a variety of unique customer needs. For example, if Ford orders supplies from a marketplace, it will receive its order and nothing else. On the other hand, if Ford buys from a traditional distributor, it may also receive around-the-clock support, replenishment assistance, vending support, safety training and a variety of other services.

Marketplaces excel at standardized transactions and offer customers outstanding ecommerce capabilities, supported by millions of SKUs and reliable, fast, standardized delivery.

Distributors, on the other hand, thrive at complex services but often struggle with even basic digital capabilities. For instance, distributors offer industrial vending, have local branches and offer repairs, conduct energy and lighting surveys, and do bin replenishment, kitting and assemblies. These services are at minimal risk of disruption from marketplaces. On the other hand, traditional distributor websites often lack the user-friendly features customers have come to expect from an online shopping experience.

However, as marketplaces mature and grow more advanced, they may begin to offer more value-added services to complement the basics. To fight back effectively, distributors must continually improve their services and make things like online search and ordering much easier for customers.

The Distributor Relative Value Model



5 Phases of "Marketplacification"

As we begin to consider strategic options for distributors, we arrive back at the notion that websites that only carry one company's products will be at a disadvantage over time. Customers don't want the inconvenience of hopping from site to site to find what they need. Most B2B buyers would prefer to source from a single channel or platform when given the opportunity. Distributors must adjust their ecommerce strategy to maintain relevance.

There are five phases in the progression toward building a marketplace:

Phase

1. Only offering your own SKUs and services
2. Working with suppliers and manufacturers to incorporate drop-shipping options into your website alongside your own products. By taking advantage of drop-ship capabilities, you can expand the number of SKUs you offer without having to invest in more inventory.
3. Cultivating a working relationship with complementary distributors to host their items on your site alongside your own. For instance, if you are an HVAC distributor, you could work with an electrical or plumbing distributor to create a more robust product offering. While there may be some overlap, expanding your product assortment via partnerships is an excellent way to differentiate yourself and provide more value to customers.
4. Opening your site for third-party sellers to list their products alongside yours. This is a hybrid model, similar to Amazon Business. With this model, you run the website, but other distributors or manufacturers use your platform to sell their products for a fee or cut of the profits.
5. Developing a purely digital marketplace to connect customers and third-party sellers. With this model, you would not own or manage any inventory – you would purely act as the middleman between parties. Zoro is an excellent example of a third-party-only seller.

"Marketplacification" is a Spectrum

Our SKUs	Our SKUs + Mfg. Drop Ship	Our SKUs + Distributor Partner Items	Our SKUs + Third-Party Sellers	Third-Party Sellers Only
Most Distributors	MSC	Distributors Share Online Assortment	amazon business	zoro

Not all distributors will (or should) reach phase five. But few should stay in phase one – the market strongly favors extremely broad assortments and sticking to your own products is a big disadvantage.

Although you may never get to the point where your website acts as a platform for third-party sellers, it is dangerous to assume that you can get away with only offering your own product assortment for much longer. Customers want simplicity and convenience; if you don't meet customer expectations, they are likely to find someone else who will.

Strategic Steps for Distributors

Depending on how you respond to the changes around you, marketplaces will either be a threat or an opportunity.

Consider the example of Kodak and Fuji Film: Kodak knew digitization was coming. After all, the company invented the portable digital camera. But both the rate and the nature of the change took the company by surprise, eventually resulting in its bankruptcy. Fuji – which was similarly embedded in film and photo printing – leveraged its capabilities to make chemicals and LED screens and is still thriving today.

Here are four steps to help you redefine your marketplace strategy:

- **Embrace the complexity that differentiates you *and* build best-in-class ecommerce capabilities.** Distributors can no longer get by with just one or the other; you must execute well in both areas to maintain your place in the market and grow share.
- **Make marketplacification part of your strategic planning.** For example, you may choose to add supplier drop-ship SKUs to your website or consider partnerships with adjacent distributors. If you are a medium to large

distributor, it may be worth exploring the possibility of launching your own marketplace.

- **Don't sell on marketplaces that are also merchants.** These organizations have an inherent ability to compete with you. If you put your products up for sale on these platforms, they could use your data against you.
- **Consider test-selling on marketplaces that are not merchants.** Platforms like Zoro and eBay do not have product managers or the ability to buy and sell inventory. They operate solely as a connector between third-party sellers and their customers – making them a much safer alternative to merchants with their own fulfillment capabilities.

Marketplacification should be accounted for in every distributor's strategic planning. While some distributors are more affected by marketplaces than others, it's hard to understand the level of threat or opportunity without an in-depth analysis and dialogue with customers, suppliers and others.

Some marketplaces mentioned here are growing rapidly and taking significant market share. Because most distributors only see a little erosion to marketplaces right now, it's easy to ignore or overlook the threat. But there's little reason to believe the momentum these emerging competitors have established will lessen anytime soon. Distributors who carefully evaluate the threat and become experts in how marketplaces operate, compete and evolve are much more likely to emerge like Fuji instead of Kodak.

About the Authors

Ian Heller is Co-Founder & Senior Partner at Distribution Strategy Group, and has more than 30 years of experience executing marketing and e-business strategy in the wholesale distribution industry. He has written and spoken extensively on the impact of digital disruption on distributors.

Jonathan Bein, Ph.D. is the Co-Founder & Managing Partner of Distribution Strategy Group and has worked with many distributors to make their marketing a profit center. He has developed and applied analytic approaches for customer segmentation, customer lifecycle management, positioning and messaging, pricing, and channel strategy for distributors.

DISTRIBUTION STRATEGY GROUP

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Distribution Strategy Group's thought leadership, research and consulting services are provided by a team with decades of experience in the distribution industry. They have helped more than 70 distribution companies build a solid foundation to win in today's changing market.

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