

2021 State of Manufacturer Sales Channels:

Suppliers' Reliance on Distributors Decreases

By Dean Mueller and Jonathan Bein, Ph.D



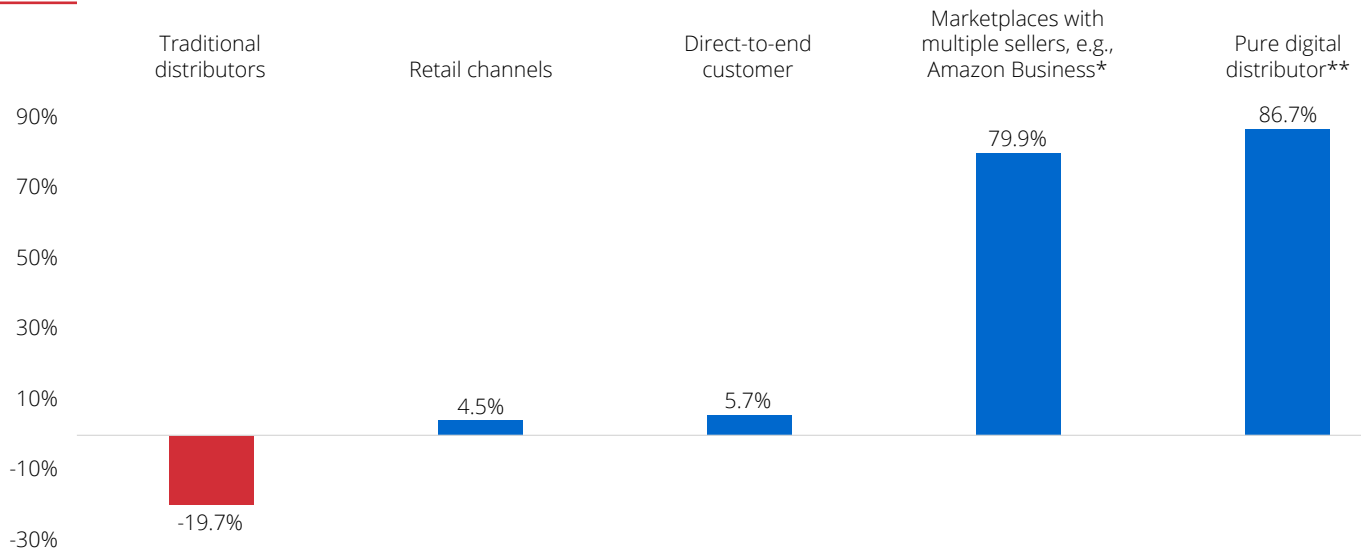
For the past 20 years, we've heard that manufacturers will rely less on distributor channels and more on direct-to-end user sales. Now, it's coming to fruition.

No doubt, manufacturer sales channels are evolving, and that has a significant impact on how distributors need to think about their business. Distributors that want to grow and lead in their space must have cutting-edge digital capabilities and a value proposition that goes beyond price and availability to succeed.

A growing number of end-users want purchasing options beyond the traditional distributor. That means for some sectors, revenue through traditional distribution will significantly decrease as customers' buying behavior continues to shift.

Based on DSG research, manufacturers predict a 1270 basis points drop in the share of sales they expect to get from distributors in the next five years, as published in "Channel Transformation from Supplier to Customer," our recent National Association of Wholesaler-Distributors (NAW) report. From the distributor standpoint, that is a 20% drop (Chart 1 on page 3).

Chart 1: How Do You Expect Your Sales Through Each of These Channels to Change Over the Next Five Years?



***Third-Party Marketplaces:** Websites like Grainger's Zoro and Amazon Business that offer a wide and diverse offering from distributors, manufacturers and retailers.

****Pure Digital Distributors:** Distribution companies that work exclusively with manufacturers to hold inventory and fulfill orders for their business buyers.

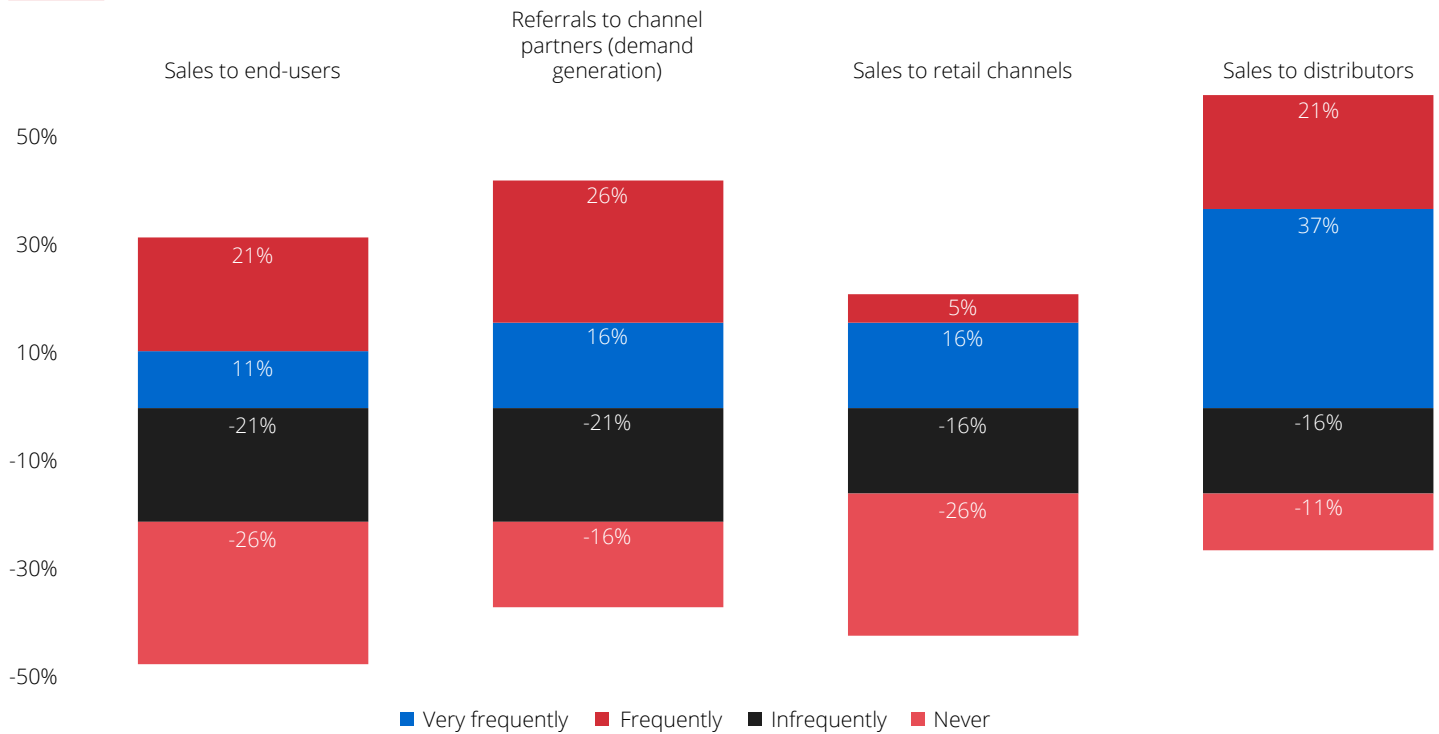
So, what's driving the changes in distribution strategies and what is responsible for the growing channel conflict? This report provides insight into the state of manufacturer sales channels – and what it means for today's distributors.

Even as manufacturers forecast sales through traditional distributor channels to decrease by nearly 20% over the next five years, they expect to see sales increase in retail channels, and with direct-to-end customers, third-party marketplaces and purely digital distributors (Chart 1). When asked what is driving their companies' channel shift, manufacturers cited:

- Improving ease of buying for customers
- Fewer end-users purchasing from distributors and spending more online due to quick shipping and availability of vast purchase information
- Traditional distributors not making necessary digital investments to meet expectations of "digital-native" buyers

For these reasons, having robust digital capabilities are no longer optional for distributors who want to retain channel share as a distributor's lack of strong online presence is by far the most important concern held by manufacturers.

Chart 2: How Manufacturers Use eCommerce



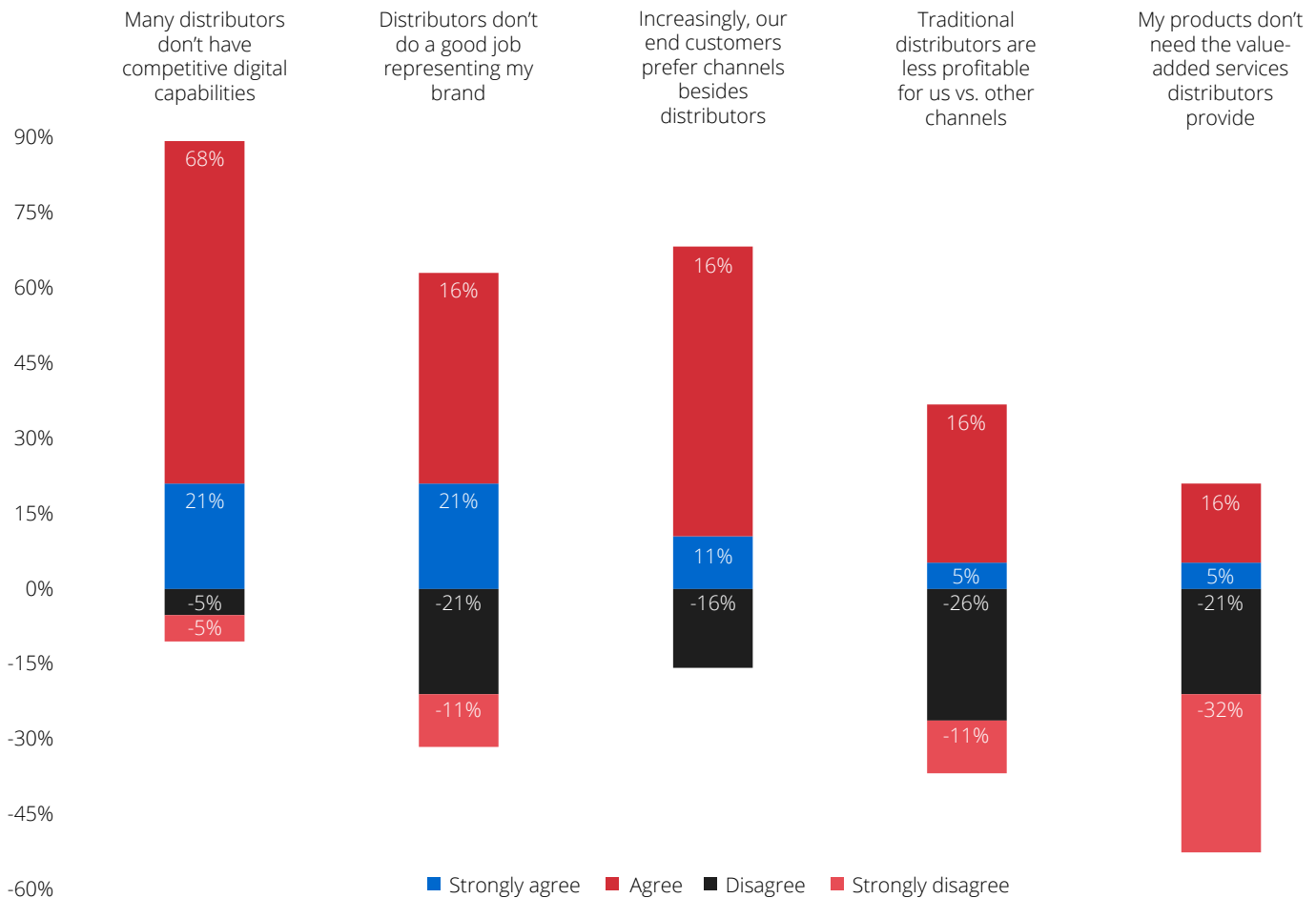
How manufacturers are using ecommerce

About a fifth of manufacturers are frequently selling direct to end-users through ecommerce, and another 11% said they very frequently sell direct online (Chart 2). But manufacturers are also leveraging their ecommerce platform in other ways. Fifty-eight percent of manufacturers reported using ecommerce to facilitate sales to distributors, and 42% provide demand generation to channel partners via ecommerce.

A growing number of manufacturers are introducing ecommerce to previously untapped channels such as end-users and retail for three reasons:

- 89% of manufacturers said many distributors lack the competitive digital capabilities they are looking for in a channel partner.
- 69% said end customers prefer an omnichannel approach outside of traditional distributors.
- 63% believe distributors don't do a good job representing their company's brand.

Chart 3: Factors Driving Change in Manufacturers' Distribution Strategies

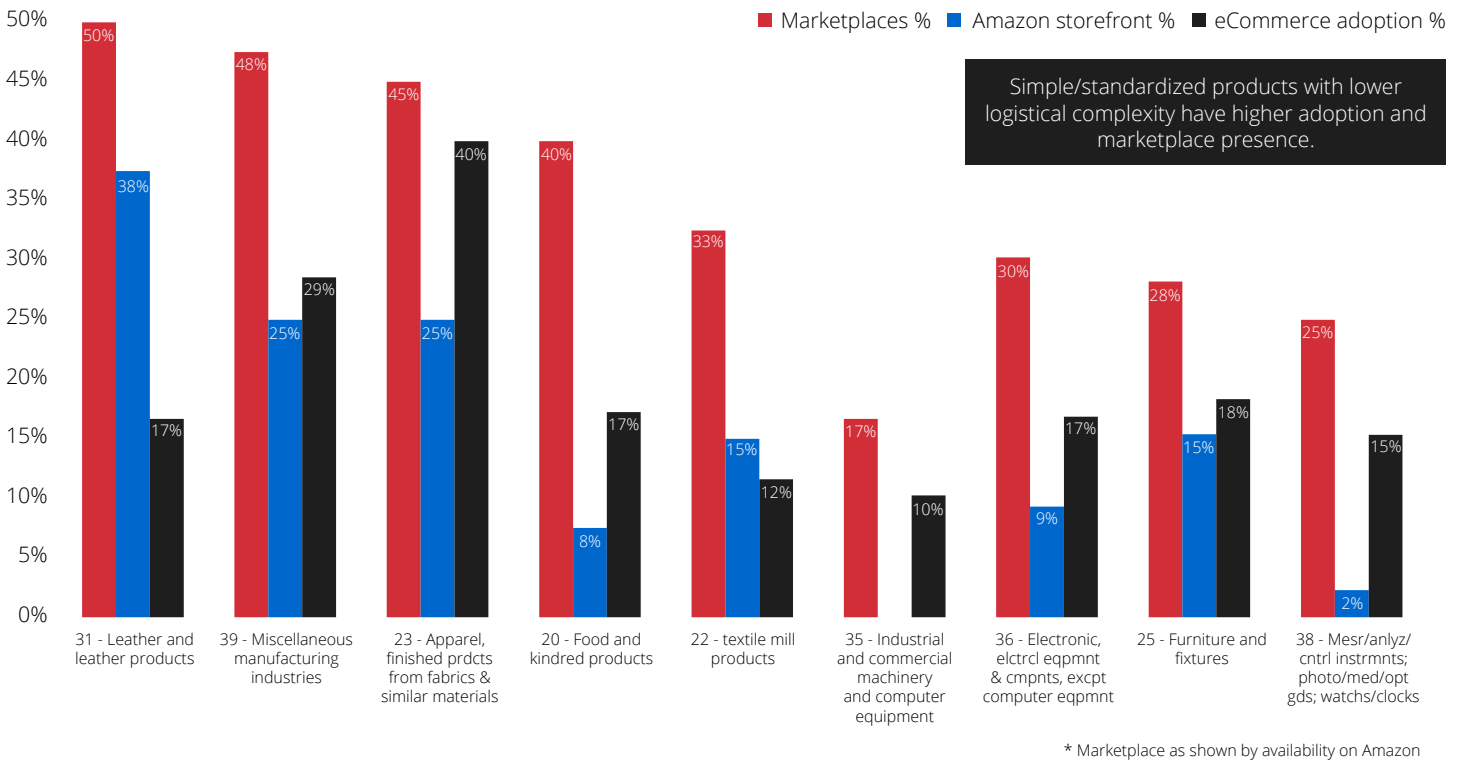


* Neither Agree/Disagree Removed for Clarity

Certainly, a new generation of buyers who want to shop online is driving this shift. Buyers today prefer more efficient and seamless electronic purchasing methods, and those expectations have been accelerated by the ongoing pandemic.

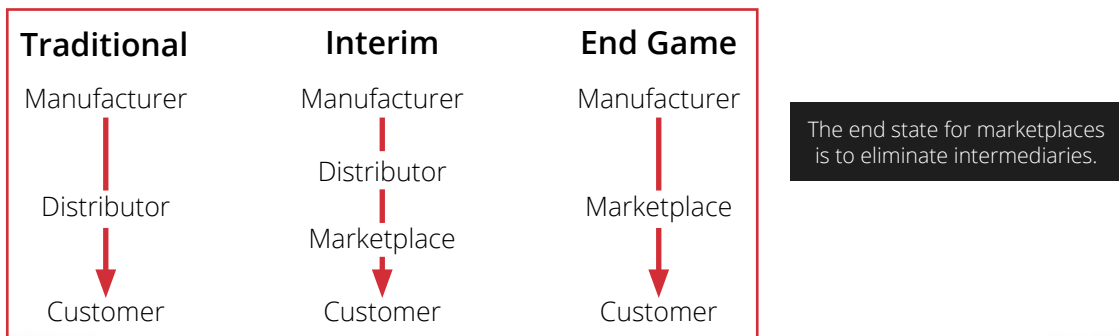
But product type and complexity matters. We looked at 4,000 manufacturer websites across multiple sectors to track ecommerce adoption and marketplace usage by manufacturers based on Standard Industry Classification (SIC). We found that simple and standardized products with lower logistical complexity have higher adoption online and presence on marketplaces. Examples of these include sectors such as leather and leather products, miscellaneous manufacturing industries, as well as apparel and finished products from fabrics.

Chart 4: eCommerce Adoption & Marketplace* Usage by SIC



As we moved into industrial sectors where there is more opportunity for value-add, such as industrial and commercial machinery, electronic components and instrumentation, manufacturers had lower adoption rates and marketplace presence. Highly technical products represented a much smaller piece of the digital pie. In these areas, manufacturers still rely heavily on distributors to provide the advice, application expertise and technical knowledge that is currently not possible to deliver digitally.

Chart 5: Channel Evolution

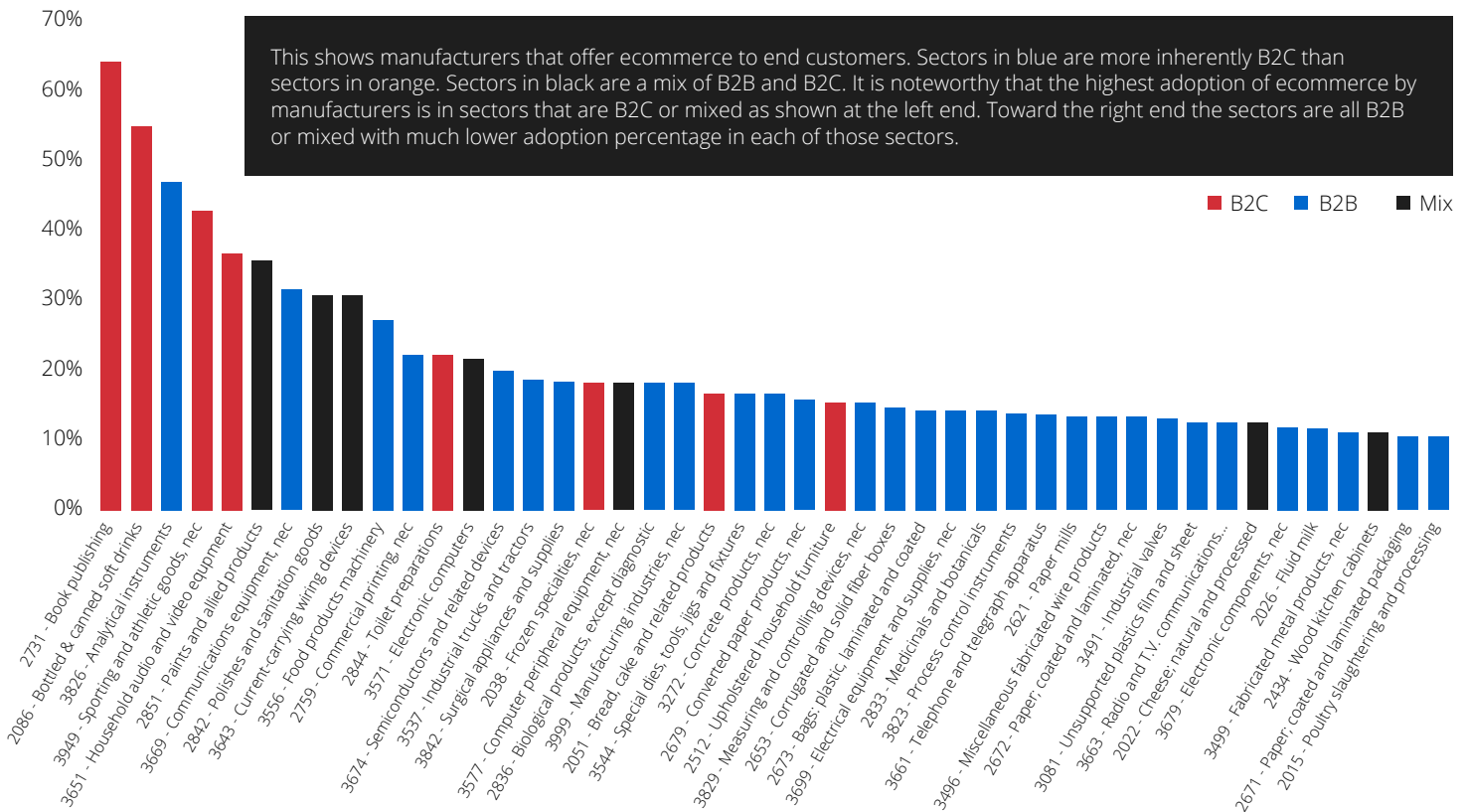


Whereas traditional distribution channels remain of great importance to many manufacturers, distributors face a growing threat of being replaced by pure digital competition, particularly for product mixes that are more vulnerable to channel shift. In fact, the end state for some manufacturers and some marketplaces is to eliminate intermediaries like the distributor (Chart 5). One manufacturer said: “Customer demand requires manufacturers move to ensure brands and products reach the end-user regardless of channel. Digital is — and will continue to be — the fastest-growing channel.”

That’s not to say all is lost for the traditional distributor. One manufacturer agreed that the distributor can and should still play a critical role in the channel: “The need for additional channels is not great as many traditional distributors are building robust digital offerings. Direct-to-end-user sales may grow based on end-user demands, but that is very inefficient and costly.”

In other words: The more technical the need, the greater the importance of distributors.

Chart 6: eCommerce Adoption in 4-Digit SIC: Business or Consumer Orientation



Complexity and technical support offer insulation

Technical products that require extensive product knowledge are more insulated from channel shift. For example, distributors that configure systems, offer product kitting or calibration services are not as likely to be hurt by the manufacturers' shifting channels. Some manufacturers also reported they will continue to value the role of the distributor and believe end-users will continue to want to consolidate purchases with distribution partners that "understand their business."

"We are still fiercely protecting our distributors and expect they will continue to add value in ways we as a manufacturer cannot or do not have the appetite for. Our distributors will use technology to serve them in a way to enhance business relationships — not replace them," said one manufacturer.

On the other hand, products more vulnerable to channel shift are typically considered less complex and easier to sell online and include:

- Cleaning supplies
- Janitorial supplies
- Office supplies
- Electronics
- MRO items
- Personal protective equipment

Marketplaces outside of the traditional distributor inherently focus on non-complex transactions like the ones above. As a result, traditional distributors that focus on digital capabilities, product knowledge and selling skills for complex transactions can create an insulative layer of protection against direct-to-end-user sales and manufacturers' use of marketplaces.

What can distributors do to protect their piece of the pie?

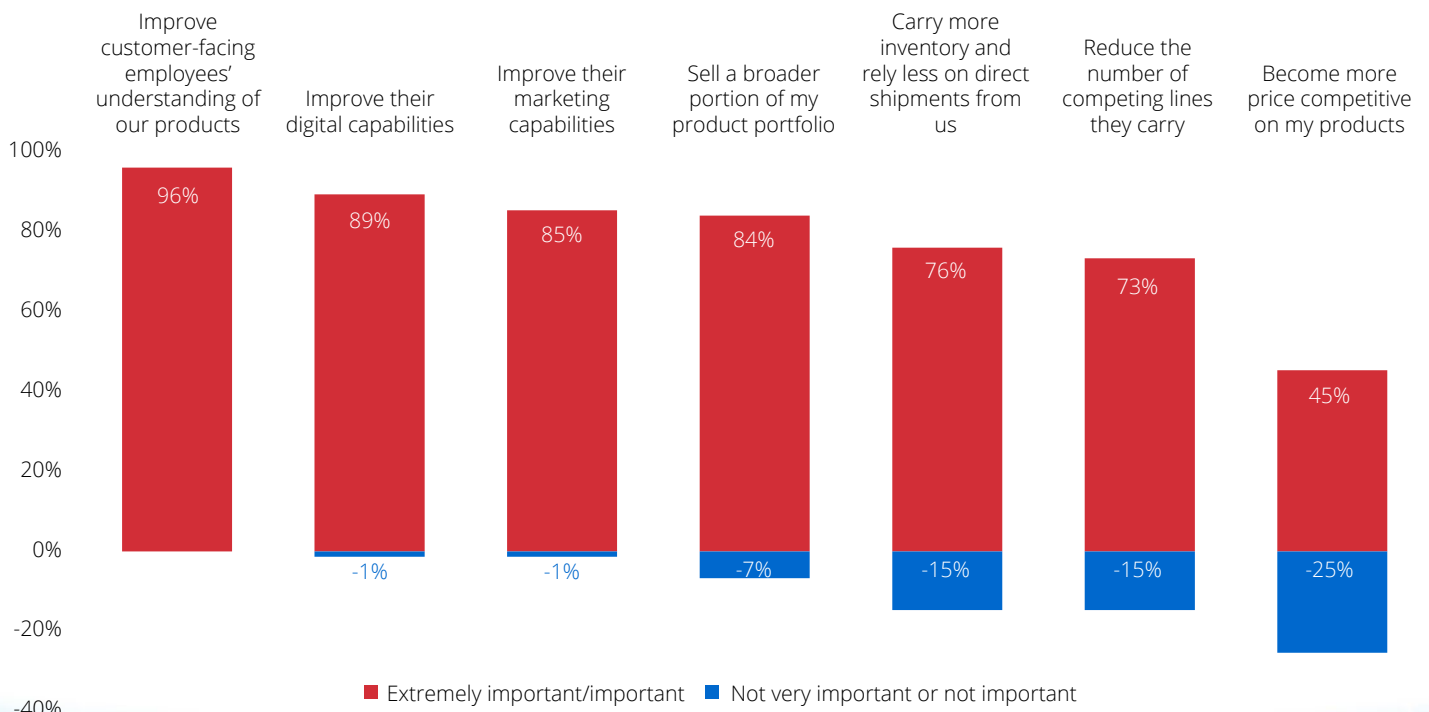
For sectors that are vulnerable, all signs point to traditional distributors getting a smaller piece of the pie; there's no getting around that. Fortunately, there's no better time than now to re-evaluate your value proposition and expand your digital footprint. Communicate with your suppliers and identify new and effective

ways you can become more valuable in the complex transactions they lean on you for. Begin to view manufacturer relationships in the same way you have nurtured customer relationships for decades.

We asked manufacturers what distributors could do to differentiate themselves from the competition and solidify their channel partnerships. An overwhelming 96% of respondents said it would help to improve customer-facing employees' understanding of their products. Other top recommendations included:

- Improve digital capabilities
- Improve marketing capabilities
- Sell a broader portion of the manufacturer's product portfolio
- Carry more inventory and rely less on direct shipments
- Reduce the number of competing lines they carry

Chart 7: What Distributors Can Do to Become More Important to Manufacturers



“Ensuring they have employees that have experience and expertise in our products and application of our products. Ensure their sellers have professional selling skills. Create compensation programs that will help focus efforts on our products where it is financially responsible,” said one manufacturer.

Other responses included:

“For us, it’s that distributors represent our brand properly and allow us to work with them in the field to convert business they otherwise wouldn’t have.”

“Distributors need to be more transparent in the end-users and applications where our parts are used. The most successful distributor relationships we have are totally open.”

One manufacturer encouraged distributors to share more user and sales data with them. Expanding the relationship beyond the transaction would incentivize the manufacturer to invest more in the distributor, helping them become more successful online, grow their business and increase brand advocate opportunities.

How can distributors offer value beyond logistics to ensure long-term survival?

As manufacturers continue to evolve distribution strategies to reach end-users, it’s clear traditional distributors must rethink their approach. Every year, business is won or lost based on the experience you deliver to the customer and your channel partners.

Protect your business from disruption by:

- **Simplifying online transactions.** Make your company easy to do business with. Ensure your technology stack supports a positive online experience and is flexible to meet the demands of your end-user. Make it as easy as possible for your customers to access information, find products online and navigate your website. This is especially important on those products that don’t require a value-add or have logistical complexity and are thus more vulnerable to channel shift.
- **Differentiating value-added services.** Understanding and monetizing value-added services is critical to the future of the traditional distributor. Offer value-added services for

an omnichannel approach that include logistics services like kitting, labeling and asset tracking, information services like safety consulting, technical support and financing alternatives, and value-added processing such as product modifications, repairs and software setup.

- **Embracing digital transformation.** Distributors need to take bold action and create an omnichannel strategy in line with their customers' purchasing journey. Increase digital marketing and extend awareness of manufacturer offers and promotions. Help manufacturers gain share with prospects and new buyers. Upskill your teams to sell solutions, not just products. And prioritize online and offline customer experiences.
- **Implementing multiple technologies for touchless ordering.** Touchless ordering through email order automation, EDI and punchout decreases the time and cost for the transaction and increases profit for the distributor. Set a goal to increase the percentage of orders you can automate or process without human intervention. Over a two- to three-year period, you'll experience significant cost savings if you can move that number to 50%.

About This Research

This research was conducted by Distribution Strategy Group. The research included online surveys for nearly 200 participants across a variety of manufacturing sectors. We also reviewed more than 4,000 manufacturing websites across sectors, and 500 manufacturers' presence on Amazon Business.

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About Distribution Strategy Group

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

Distribution Strategy Group offers strategic guidance for distributors in the face of disruption, including:

- Digital and ecommerce strategy
- Customer lifecycle management strategy
- Customer analytics
- Sales channel strategy

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