

Distributor/Reseller Marketing

A Riddle Wrapped in a Mystery Inside an Enigma

Distributor/Reseller Marketing

Over the last 50 years, changes in distribution occurred at a snail's pace. However, over the past five years, and more significantly in the next five years, changes in distribution will be fast and numerous. Marketing through distributors and resellers is complex enough, but those companies that have not developed a clear understanding of the basics of "channel marketing" will likely experience declining revenue and market share.

Distributor/reseller marketing is more complex today because:

- > The emergence of electronic commerce challenges the underlying rationale for distribution channels
- > Distributors are investing heavily in electronic commerce and other technologies to offer better online systems and lower cost structures
- > Integrated supply contracting is changing the relationship between manufacturer, distributor and end user
- > Outsourcing of logistics functions is emerging as an alternative to direct fulfillment or traditional distribution channels
- > Hybrid solutions that combine direct and distributor activities are now very common

Distributor/Reseller Marketing

Despite the increased complexity of distributor/reseller marketing, manufacturers are being forced to answer the question, “How do we more effectively and efficiently market our products through distribution?” Answering this question has become increasingly important because:

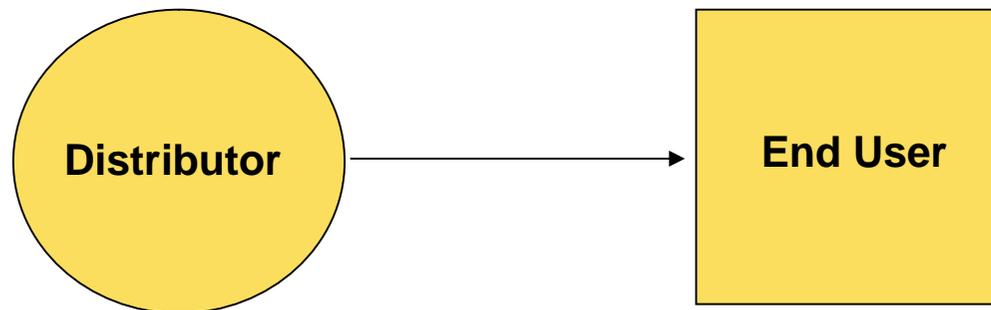
- > Most U.S. businesses have directed their purchasing departments to drastically reduce the number of suppliers with which they do business. This trend favors the use of distribution over direct selling
- > Large distributors have gotten large through mergers, acquisitions and consolidation. The investments they have made have significantly lowered their costs of operation, making them very efficient marketers
- > Conflict between channels is greater than ever with more channel options available
- > New channels, including integrated supply contractors, electronic commerce, catalog and even retail superstores, require different support/investment from the manufacturer

Through our experience in helping companies increase their market share in distribution, we have identified certain basic concepts that are common to all facets of distributor marketing. In this booklet, a series of questions and answers provide the framework for developing an understanding of these distribution concepts. They are the key to resolving the distributor/reseller marketing.

Why Do End Users Buy from Distributors and Other “Third Parties?”

End users buy from distributors and resellers for reasons other than the products they provide. Distributors provide a number of advantages that cannot be obtained from the manufacturer.

End-User Advantages in Distributor Buying

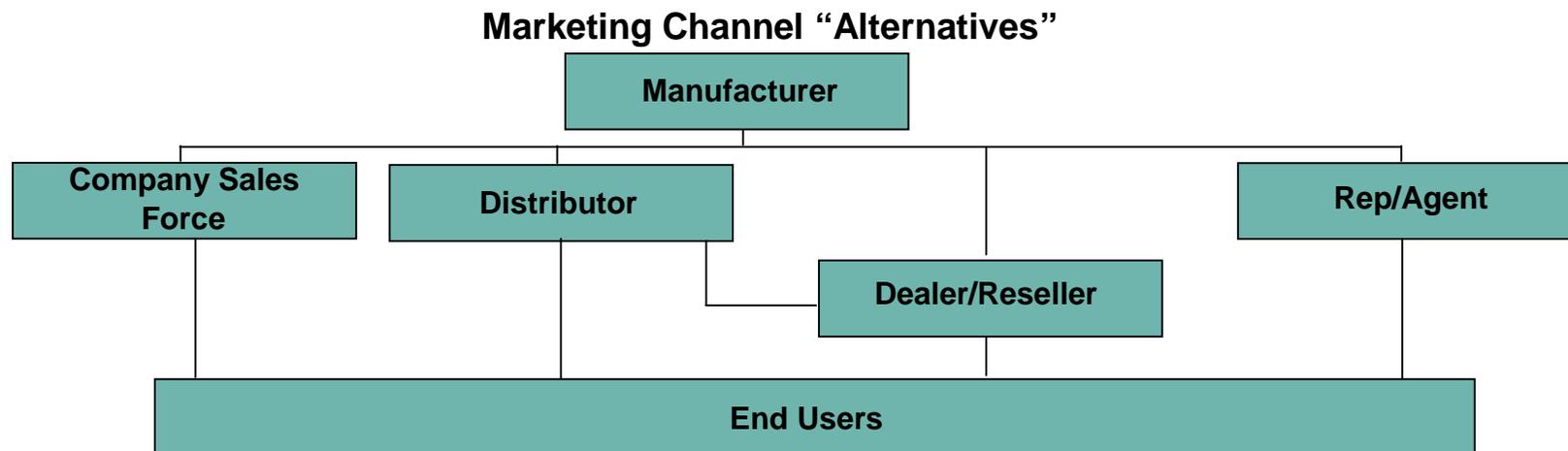


- > Bundling of products (hardware, software and services)
- > Ordering and delivery flexibility
- > Inventory cost/support

- > Technical support
- > Single-source convenience
- > Single-source accountability

Why Do End Users Buy from Distributors and Other “Third Parties?”

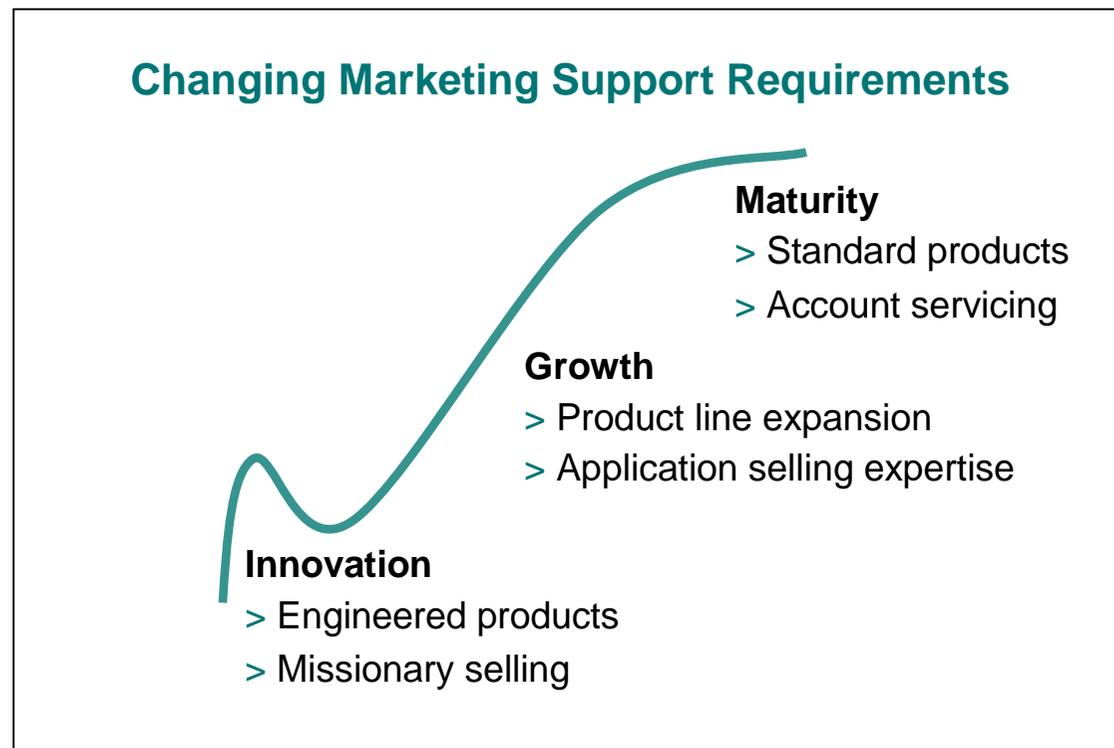
Many marketing textbooks describe three alternatives for marketing to the end user. Distribution, however, performs a unique role in the marketplace and is not an alternative to the field sales force, manufacturer reps or sales agents.



It is increasingly common to find a manufacturer protecting specific large end-user accounts for its direct sales force only to find that the end user would prefer to buy through a distributor/dealer because of the unique value-added activities provided.

Why Does Distribution Change in the Marketplace?

Different stages in the market life cycle require different types or levels of marketplace support. These conditions exist whether a product is marketed direct or through distribution.

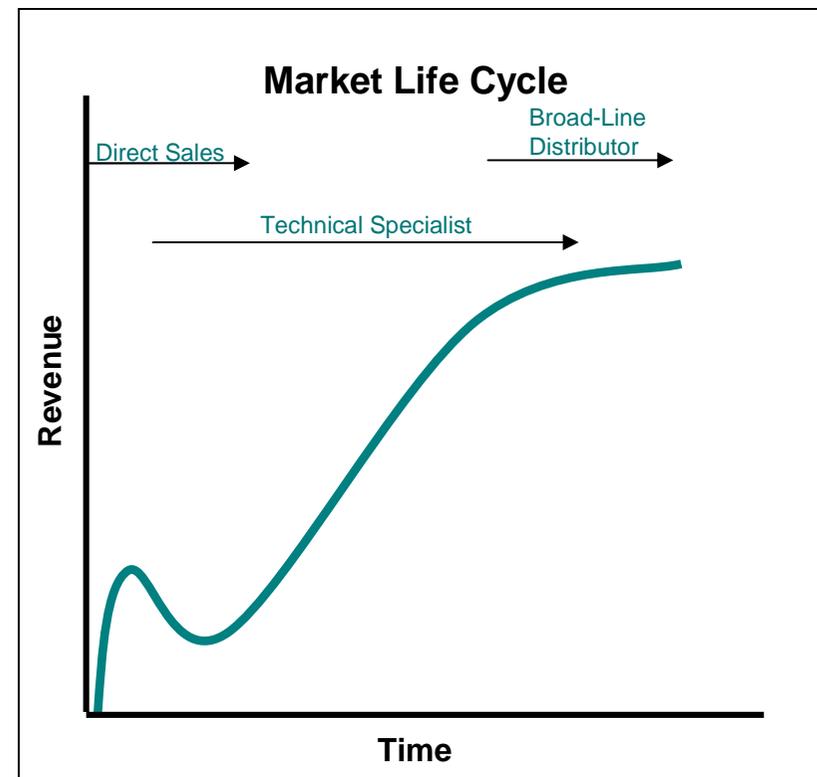


Why Does Distribution Change in the Marketplace?

Because end-user needs change from technical support to account servicing as a marketplace matures, the type of distributor that is effective in each stage also changes:

- > Direct sales is required for missionary selling because distributors/resellers will rarely develop new markets for you
- > Technical specialists provide the technical support required during the growth period
- > Broad-line distributors displace technical specialists when markets mature and account servicing is the predominant end-user requirement

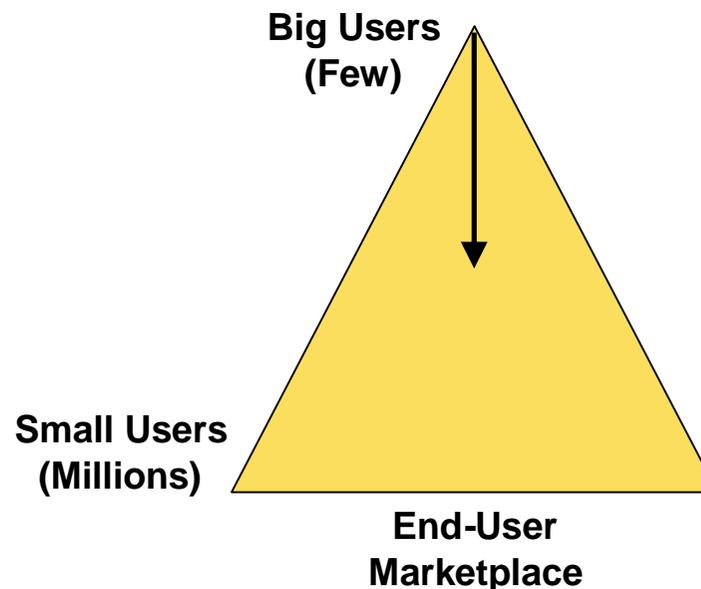
Failure to recognize distribution changes that evolve during the maturation process usually results in dramatic shifts in market share positions.



Why are Different Types of Distributors Necessary?

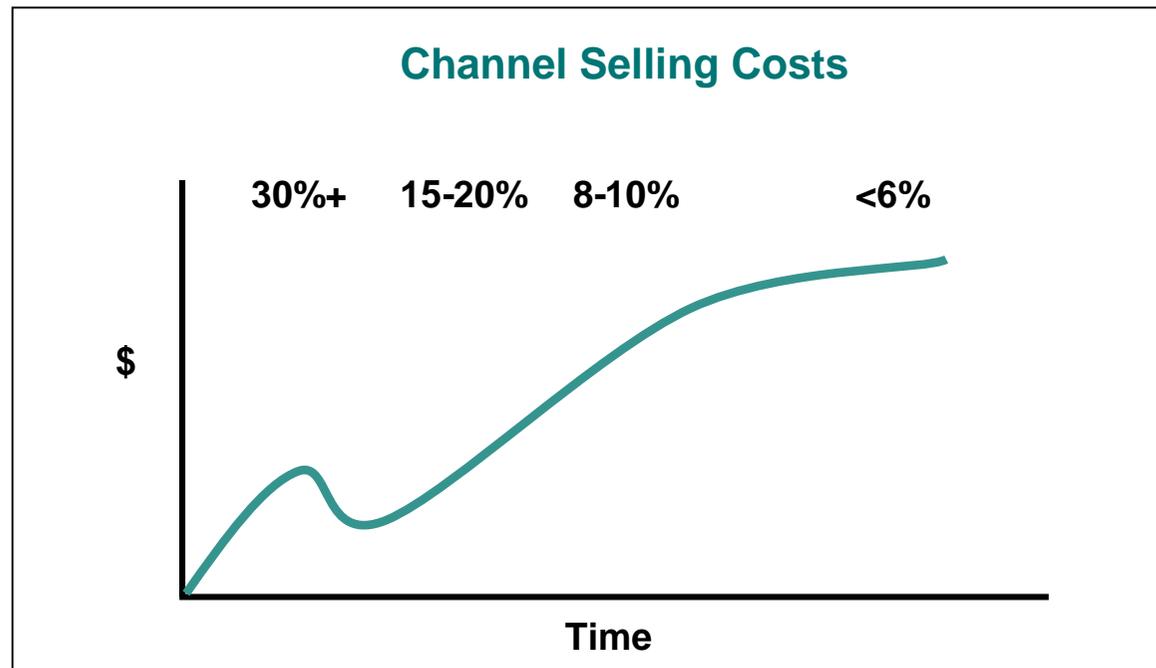
New technologies almost always move down the user triangle. Marketers, therefore, will need to market through broad-line distributors and technical specialists simultaneously. This type of coverage will meet the needs of a broad range of end users:

- > Large, mature, repeat buyers with logistical needs
- > New, smaller, first-time buyers with technical support and education needs



Why are Different Types of Distributors Necessary?

The use of multiple channels adds further complication as each channel type has significantly different costs/margin structures and significantly different support expectations. Channels operating at various points on the life cycle incur dramatically different selling costs (the total cost of the internal and external sales forces).

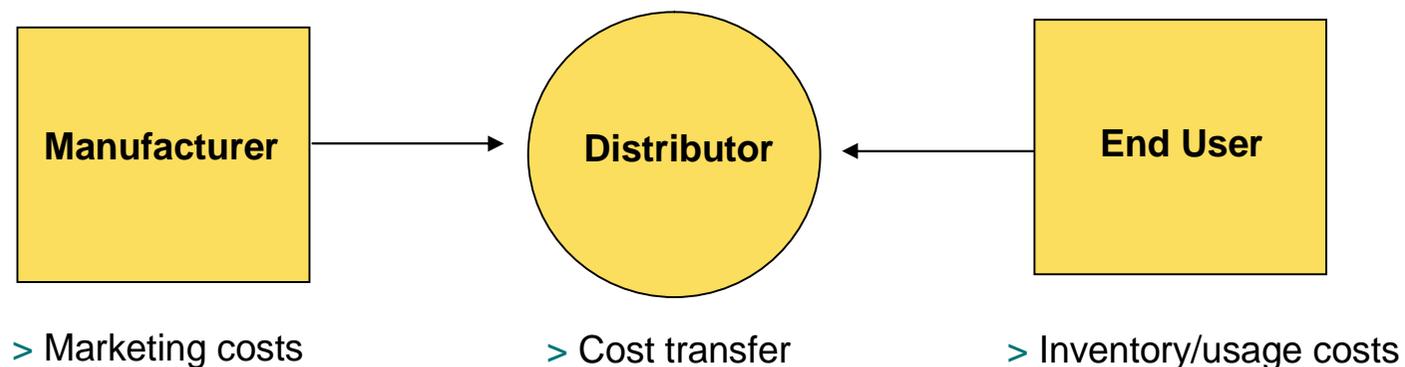


What is the Economic Role of the Distributor?

Historically, the economic role of the distributor/reseller was to transfer marketing costs from the manufacturer into its own business.

Today, with a greater focus on the total costs in the supply chain, the reseller's role is to take responsibility for the functions it can perform more efficiently than either the manufacturer or the end user.

The Economic Role of the Distributor

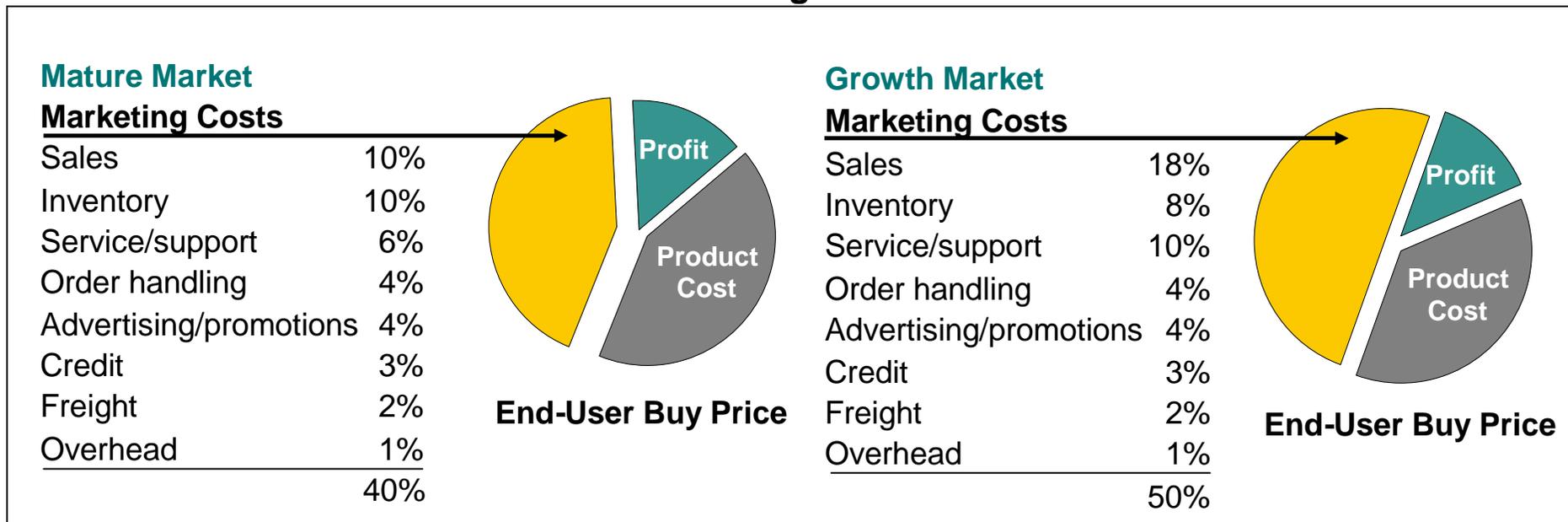


What is the Economic Role of the Distributor?

Marketing costs are defined as all costs incurred from the time the product leaves the production line until it reaches the ultimate end user.

In mature markets, these costs typically amount to approximately 40% of a product's selling price (to the end user). In growth markets, marketing costs can account for 50% of a product's selling price.

Marketing Costs

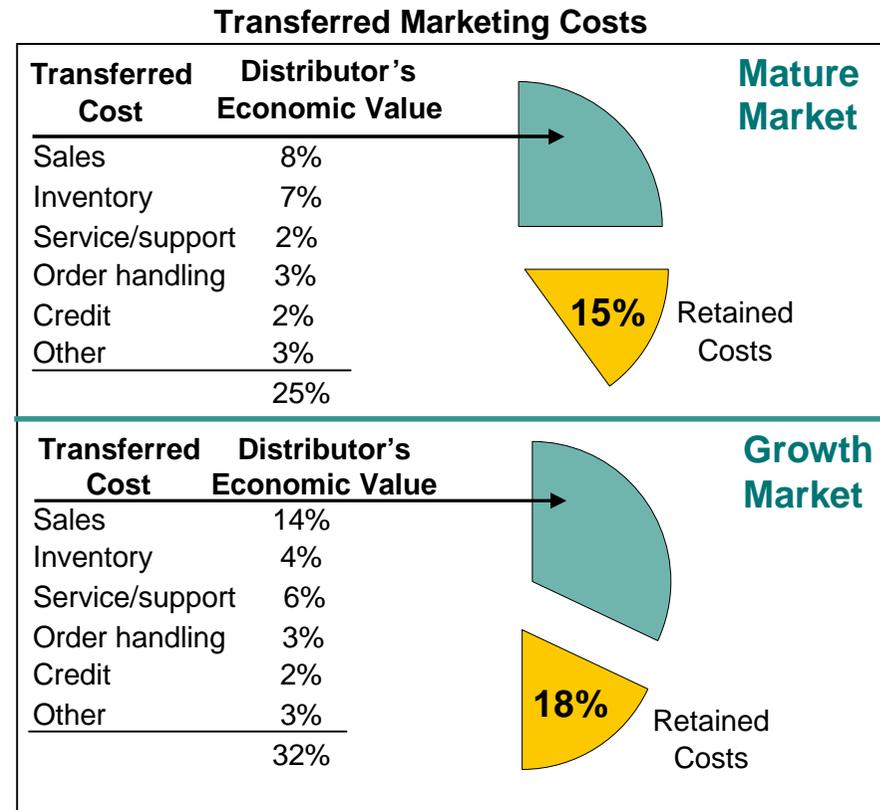


What is the Economic Role of the Distributor?

A distributor or dealer transfers out a portion of the marketing costs that the manufacturer would otherwise incur.

The manufacturer retains a portion of the marketing costs, including:

- > Managing the distributor marketing program through its field organization
- > Developing marketing and promotional programs to complement the distributor's sales activities
- > Carrying some finished goods inventory
- > National advertising, trade shows, etc.
- > Providing second-level technical support

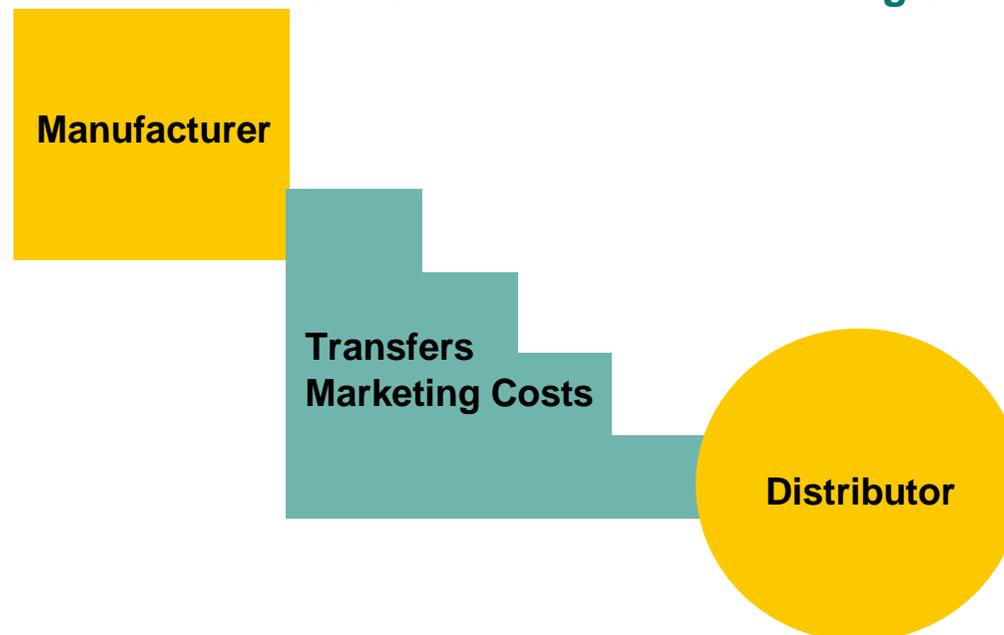


The sum of the transferred costs represents the distributor's economic value in the marketplace. The discount the distributor receives merely compensates it for the functions and activities performed.

What is the Value of the Distributor Discount Pricing Structure?

The discount pricing structure is the mechanism which defines a buyer's price and what the buyer must do to achieve that price. A properly designed discount structure compensates the buyer (dealer, distributor or end user) for the activities performed on behalf of the manufacturer. It also allows for the differentiation among buyers based on the different activities they perform.

The Role of the Distributor Discount Pricing Structure



What is the Value of the Distributor Discount Pricing Structure?

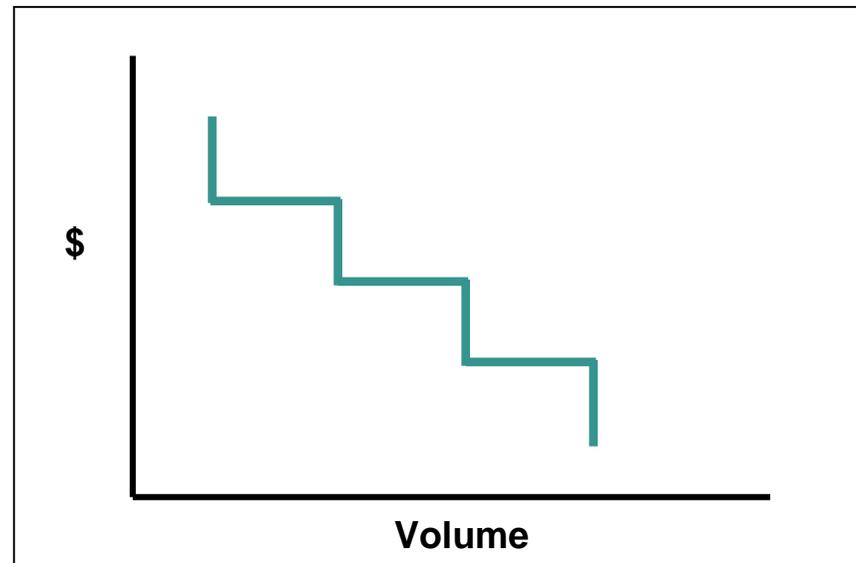
A well-designed pricing structure satisfies the following requirements:

- 1. It equitably transfers marketing costs from the manufacturer to the distributor**
- 2. It is legally justifiable**
- 3. It fits the characteristics of the marketplace**
 - > Primary vs. secondary vs. tertiary products
 - > New vs. mature markets
 - > Distributor size
- 4. It provides an economic basis for resolving common problems encountered in supplier/distributor relationships**
 - > Drop-ship business
 - > Distributor and direct selling in the same marketplace
 - > Different distribution channels handling essentially the same product line
- 5. It complements and supports your overall marketing strategy**

Discount Pricing Structures

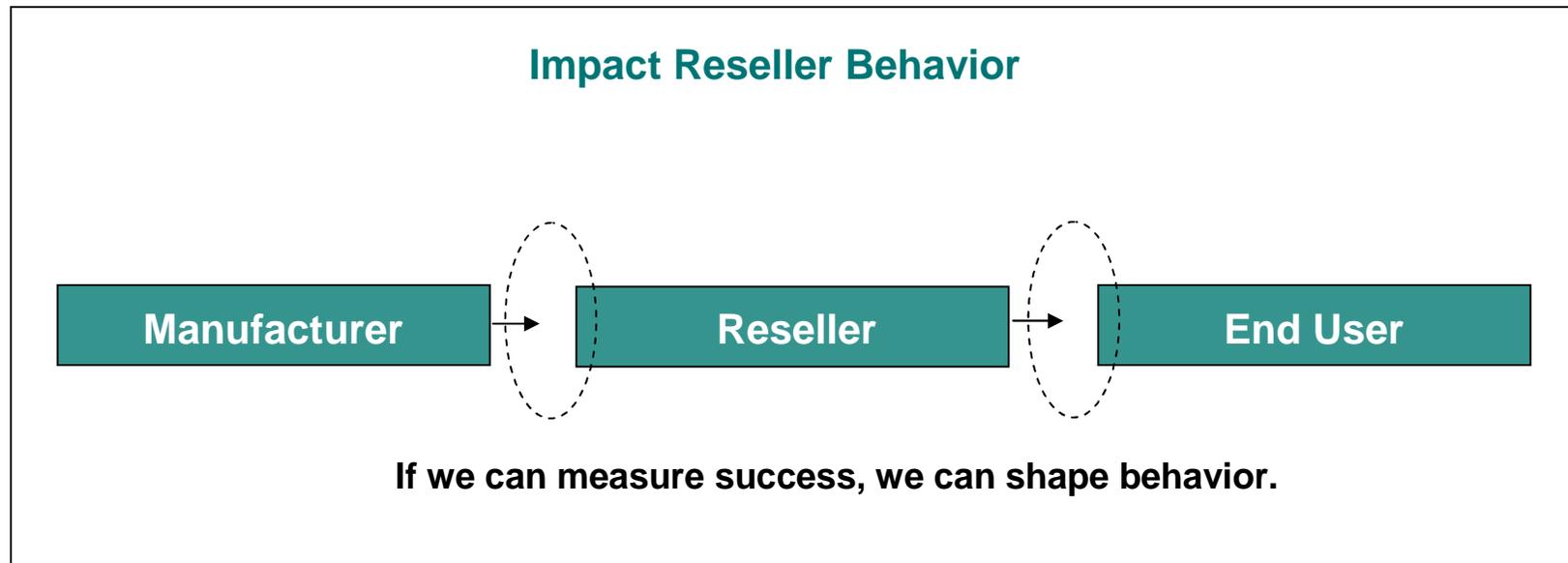
Discounts based on volume (order size and/or annual volume) are effective in directing a reseller's buying behavior. However, there are several problems with solely using volume discounts:

- 1. They are rarely legally justifiable based on a cost transfer defense**
- 2. They often reward large broad-line resellers at the expense of small technical (value-added) resellers**
- 3. They often create gray marketing or simply shift sales from one quarter to the next**



Discount Pricing Structures

Discount structures that reward resellers for activities performed in combination with appropriate volume incentives allow you to more precisely shape your resellers' buying, selling and operational behavior to meet customer needs.



What is the Field Sales Force's Role in Distributor/Reseller Marketing?

The manufacturer's sales force is responsible for managing market coverage through its channel marketing program. To do this effectively, they must understand each reseller's business. If you market through thousands of dealers, this is not possible. To deal with the complexity, the manufacturer should understand each dealer/reseller subsegment or type.

Every distributor serves as a "window" to the marketplace; its unique perspective stems from its:

- > Product line
- > Customer base
- > The nature of its business

If a distributor's window does not match your marketplace window, it cannot deliver your market share objectives:

- > The distributor cannot write business that it does not see
- > The distributor will not call on new customers just to sell your product

A distributor cannot deliver more than its share of the market.

In distribution, the manufacturer's market share is the sum of the market shares delivered by individual distributors. Therefore, a manufacturer must select the distributors capable of delivering its share objectives. Since knowledge of each distributor's window is critical in managing marketplace coverage, distributor selection must be done on a territory-by-territory basis. This becomes the primary responsibility of field sales management.

How Can Channel Conflict be Eliminated?

IT CAN'T! Manufacturers seeking share and revenue growth typically have to expand the types and numbers of distributors/resellers marketing the manufacturer's products.

As manufacturers expand distribution, they achieve greater market coverage, but create channel conflict in the process.

Channel conflict cannot be eliminated, but it can be managed. Approaches to managing conflict are numerous and include:

- > Activity-based discount structures
- > Dual credit/compensation when the direct channel competes with the distribution channel
- > Exclusive territories (geographic or vertical markets)
- > Dual branding strategies
- > Product differentiation by channel
- > Placing restrictions on distributors
- > Utilizing dealer/distributor councils to communicate and resolve problems

Remember, a little conflict is a good thing – it means you have good market coverage.

What are the Major Mistakes that Manufacturers Make in Marketing Through Distribution?

In designing and operating a distributor/reseller marketing program, management must insure that the following basic concepts are not violated.

- 1. Channel marketing begins not with the channel, not with the manufacturer, but with an in-depth understanding of end users**

- 2. Manufacturers do not sell to distributors/resellers; they sell through distributors/resellers:**
 - > Distributors are not your customers; they are the means of reaching the customers
 - > Loading programs only puts product on the distributors' shelves. A sale is not made until the product moves into the hands of the end user
 - > Manufacturers and their channels should engage not in adversarial or arm's-length relationships, but in partnerships. However, 50/50 partnerships do not work; someone must lead

What are the Major Mistakes that Manufacturers Make in Marketing Through Distribution?

- 3. Distributors and resellers rarely develop a market for technology; rather, they service existing markets:**
 - > Manufacturers should be prepared to sell direct when introducing new technologies
 - > Distributors cannot take an existing product into a marketplace that they do not service – their product lines will not support the effect
 - > Manufacturers frequently expect distributors/resellers to develop markets and are frustrated when they do not

- 4. Market demand determines how much of a product (all brands) will be sold by the distributor/reseller:**
 - > Market acceptance or rejection determines which brands the distributor sells
 - > Attempts to change distributor brand emphasis are limited by the end user's willingness to accept substitutes
 - > Channel mind share is 90% economics. Manufacturers must show how their products will fit/improve the channel's business model

- 5. Managing channels is very different from selling directly to end users. Different programs, time horizons and salespeople are usually required**

Final Thoughts

The basic distributor/reseller marketing concepts continue to appear deceptively simple. They are, however, difficult to execute in practice. Marketing management's typical reaction to the concepts that we have outlined is agreement; nonetheless, existing distributor/reseller marketing programs that consistently violate these concepts are allowed to continue.

Decision-making responsibility for distributor marketing programs is often delegated to the lower level of the marketing organization. Because of its complexity and its impact on profit margins, final decisions on distributor/reseller marketing programs should be retained by top-level marketing management. Day-to-day decisions should be passed to the regional levels.

We know from experience that the concepts presented form the foundation for constructing and operating a channel marketing program that will sustain and increase your market share.

If you carefully apply these concepts to your present channel marketing program, your business relationships with your distributors/resellers will improve. As a manufacturer, you may not like some of the decisions that these concepts require you to make, but you will avoid many of the costly marketing mistakes that we frequently encounter.

THE CONCEPTS WORK!

An Invitation

Work with Frank Lynn & Associates when you need an objective perspective from an organization with extensive experience in channel marketing across numerous industries. Our senior partners have more than 100 years of experience helping clients to:

- > Select the right channels
- > Improve the effectiveness of their channel programs
- > Improve the efficiency of their channel programs

To find out how we could work together, we invite you to schedule a complimentary half-day meeting in our Chicago office to discuss your specific business challenges. To set up a meeting, contact our Client Services Coordinator at [312.263.7888](tel:312.263.7888).

Frank Lynn & Associates

Frank Lynn & Associates, Inc. is an international channel marketing consulting firm. Since 1973, we have provided our clients with in-depth knowledge and expertise in channel marketing – the marketing of products through dealers, distributors, specialty retailers and other types of resellers. We are known in the marketplace as “The Channels People” because of our expertise in this field. Our mission is to utilize our knowledge of marketplace dynamics and economics to help our clients generate creative, actionable solutions.

During our 33 years, we have assisted clients in:

- > Growing their business
- > Entering new markets
- > Launching new products or new technologies
- > Entering channels that are new to the company
- > Reducing conflict among indirect channels
- > Reducing conflict between a direct sales force and the company’s indirect channels
- > Evaluating marketplace synergies for acquisition candidates
- > Focusing marketing and organizational resources of the company
- > Increasing profitability
- > Segmenting end users into groups more likely to buy the company’s product or service
- > Understanding their marketplace by providing market-based information and insight about customer, channel and competitive behavior
- > Developing actionable strategic and tactical marketing plans