



SAP Industry Briefing

**INCREASE PROFITABILITY
THROUGH OPTIMIZED DISTRIBUTOR
BUSINESS PROCESSES**

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EXECUTIVE SUMMARY

A customer calls to place an order and within seconds your system shows that you have an inventory of 2,000 cases in red, green, or blue at the price of U.S. \$100 per case. It also shows that the customer is creditworthy, so you immediately approve the order for 100 cases in each color. The invoice is generated automatically and entered into the accounting system. A message is sent to the warehouse to get the shipment ready for the customer, and a purchase order is simultaneously generated and sent to the manufacturer to replenish the supply.

While in the system, you decide to check on the profitability of your sales order and projected future sales. It indicates that your net margin is very high, so you decide to increase your purchase order. The system advises that you are entitled to a hefty discount if you buy a full truckload from that supplier. You then plug the numbers into your procurement system, and it tells you how much to buy in order to reach the ideal quantity.

For most wholesale distributors, the above scenario is far from reality for many wholesale distributors. What if you have acquired five businesses in the last few years – all located in different states? Each operates on a separate system, none of which talk to each other. Your customers are furious because you are out of product and you cannot get additional inventory until next week. Ironically, you think you have the items in one of your locations, but the warehouse staff is still trying to figure out where they put the last shipment that was delivered. Meanwhile, the accounting department has just spent the last week arguing with the supplier about a claims dispute on a chargeback processed last year.

Situations like this can cause distributors to make the commitment to search for an enterprise wholesale distribution solution. This technology, specially designed for distribution processes, can improve operational efficiency and profitability while supporting innovative business models and customer services. It offers a full range of industry processes – from demand and supply planning, purchase-to-pay, warehouse management, order to cash, financials, and human resources. Through enabling enterprise technology, distributors can integrate marketing, logistics, and financial management capabilities to meet the needs of their customers and their business. In addition, distributors can analyze operations and profitability to drive responsiveness internally and across the supply chain.

A TIME FOR GROWTH AND CHANGE

Approximately 275,000 distributors in the United States employ 5% of the nation's working population and play a part in roughly 80% of purchases. Despite predictions stating that the Internet would replace these firms, they have endured the test of time. According to the U.S. Census Bureau, the industry has grown between 7% and 8% each year.

Research from Pembroke Consulting shows that more than 80% of distributors are family-owned, privately held businesses. If they want to continue to pass the business down through the generations, these businesses need a strategy to maintain or grow that business. Distributors can accomplish this by expanding their core offering to include similar categories of products. Alternatively, they can maintain their niche, but expand geographically. Both of these growth strategies are commonly executed through acquisition.

Distributors find that increased operational complexity and new cost structures come with expansion and new revenue streams. They need to make decisions about their inventory, buildings, people, and systems. They must choose between keeping the status quo, integrating and consolidating, or establishing a shared-service arrangement.

Meanwhile, business requirements are changing rapidly. Suppliers and customers are asking for more services, accessibility, visibility, and accommodations. For instance, suppliers want advanced receipt settlement and vendor-managed inventory services, while customers want the ability to place, price, and track sales orders online.

Yet, many distributors are operating on aging, shallow technology stacks. The acquired businesses are often running their operations on disparate, nonintegrated systems and have a mounting pile of projects that require thousands of man-hours, queued up to be handled by small IT staffs. These organizations are beginning to understand that it may be time to retire legacy systems.

Since creating and maintaining software is not a distributor's core competency, many are looking toward enterprise wholesale distribution solutions that provide out-of-the-box functionality. Pembroke Consulting estimates that one-fifth of U.S. distributors with revenues of more than U.S. \$25 million have already implemented these solutions, and industry analysts expect this number to rise to two-thirds in the next five years.

THE SEARCH FOR A SOLUTION

The software selection process can be daunting for distributors. There are several applications on the market ranging from generic enterprise resource planning (ERP) solutions to industry-specific wholesale distributor applications. Distributors must also consider the price of the software, including implementation costs and maintenance costs over time. In addition, the vendor's credentials must be taken into consideration, particularly their long-term viability and their understanding of the distributor's business.

The right solution should enable a distributor value chain to be composed of:

- **Planning** - Distributors must plan what they are going to sell and what they need to buy to execute those sales.
- **Procurement** – Distributors must decide from which suppliers they are going to source the goods and quantities of those goods.
- **Warehouse management** - Processes must be put in place, and facilities must be made available for receiving, unloading, and storing goods. As much as 60% of the average distributor's operating expense is payroll, and half of the payroll goes to people working in the warehouse.
- **Sales order management** - The fulfillment process should include goods pricing, checking of the customer's creditworthiness, and inventory availability, billing, and collecting.
- **Business analytics** – The business' profitability (by product and by customer) must be monitored continuously so problems can be addressed quickly. For instance, analytics may reveal that a price increase on a particular product is necessary, or that a customer account may need a different level of support.

All these functions should be integrated within one solution that is gradually rolled out to the entire enterprise. Most distributors choose to implement a solution in one branch and train that staff how to use it before rolling it out to other areas, a few at a time. With each implementation, distributors become more adept at the process.

A WELL-OILED MACHINE

A fully integrated solution allows distributors to increase net revenue through better customer service. Approximately 60% of back orders are cancelled. By using technology to help ensure product availability, distributors can mitigate the risk of losing sales because of back orders.

The technology also helps reduce time to market, which increases the likelihood that a distributor will win business as new products are introduced.

Distributors can leverage the solution to help enable a new sales channel. Many expand their use of product catalogs, realizing that these catalogs offer retailers a convenient way to shop. Retailers tend to buy more when they shop via this method.

Some distributors have increased their top-line revenue by almost 12% by introducing new catalog sales channels. A retailer may be looking in the catalog for an item and come across several other items that are needed. They add the item to its cart and increase the total sale.

Besides generating new revenue, the solution can help reduce the cost of goods sold. Distributor's profit margins are tight; typically, 75% of a product's price is the cost, 25% is gross profit, and the net profit is only about 2%. A wholesale distribution solution allows companies to automatically optimize their purchase orders.

Often, a supplier offers a better price for ordering a full truckload of goods instead of a partial truckload. The wholesale distribution system looks at a window of purchase orders with the same origination and destination points. It automatically consolidates the purchase orders, determines the number of cases or the weight that constitutes a truckload and then makes a recommendation that takes advantage of the truckload discount.

Suppliers often give distributors a 60-day notice that there will be a price increase on all products in a category. As a result, the distributor may want to consider placing a larger than normal order before the increase takes effect. The system can look at the difference between the old price and new price (the price delta) and inventory carrying costs (fixed expenses) to determine the optimal amount of each product to purchase.

The solution can also improve accounting and administrative productivity to facilitate the chargeback process. For example, a manufacturer may make a deal with the end-customer at a price less than the distributor's cost. The manufacturer then reimburses the price difference to the distributor after a chargeback claim is filed. The distributor has to keep track of how much is sold for which customer, over a specific period of time, with multiple deals to make a chargeback claim.

Any administrator can keep track of one deal with one supplier, but the job is much more challenging when there are thousands of suppliers and customers and hundreds of thousands of product agreement combinations. Claims may not get filed and, when claims are filed, the accuracy is questionable. The claim must then go through a dispute cycle during which the distributor has not collected its cash in a timely fashion. Technology can help prevent this scenario from occurring.

Finally, technology improves warehouse productivity. When the warehouse unloads trucks during the day, it often puts the goods anywhere there is an empty space and records the location. Then, another goods movement is made to consolidate and reorganize the product so it is in an efficient place. A wholesale distribution system provides directed put-away instructions on where the goods should go the first time around, so there is no need to move it later. It also improves warehouse productivity with put-away strategies that show which items are popular and fast-moving and which are slow-turning, aged, and obsolete. This allows for stock location optimization.

SUMMARY

Faced with shrinking margins, cost-cutting pressures, and the emergence of new players (such as logistics service providers), wholesale distributors are changing their business models. They are proactively looking for opportunities to offer customized, value-added services, tap new revenue sources, distinguish themselves from the competition, and improve customer loyalty. To reduce costs, they are identifying core business processes and uncovering outsourcing potential.

Legacy systems are often not efficient, agile, and flexible enough to allow distributors to compete in today's marketplace and execute growth strategies. That is why these firms are turning toward fully integrated, packaged ERP solutions to help achieve their goals.

Ideally, distributors need technology that provides full supply-chain visibility, quick access to accurate information, and the ability to automate routine processes from the purchase order to delivery and payment. As soon as a customer places an order, the distributor needs to be able to check the inventory, approve the order based on the customer's creditworthiness, notify the warehouse, and automatically replenish the supply at the most

favorable prices. In addition, it must be able to monitor profitability by product and customer.

A wholesale distribution solution offers a variety of benefits, including improved service levels, reduced capital investment in stock across the supply chain, lowered cost of goods sold, streamlined operations, and decreased overhead costs. Distributors can optimize their logistics processes by bundling together orders and making the best possible use of storage capacity. They can also offer value-added marketing and sales services, ranging from Internet sales to repackaging direct-store delivery and supplier-managed inventory.

Many distributors probably think achieving this level of efficiency can only happen in their dreams, but with the right technology, plan, and vision, the ideal scenario can become a reality.

POWERED BY SAP NETWEAVER®

SAP for Wholesale Distribution is powered by the SAP NetWeaver, the integration platform that supports both SAP and non-SAP systems. The open architecture of the SAP NetWeaver platform lets distributors transform their business processes incrementally, with step-by-step migration, to achieve fast return on investment. The highly intuitive, role-based environment of SAP NetWeaver lets users access information from different sources through a single interactive format.

For more information on the many ways that SAP for Wholesale Distribution can help your business, call your SAP representative or visit us online at <http://www.sap.com/industries/wholesaledistribution>.

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