

REPORT CARD UPDATE

The Findings of a National Study
of Manufacturer-Distributor
Working Relationships



The Industrial
Performance Group
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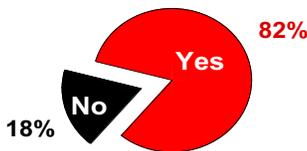
Executive Summary

Manufacturers and distributors can significantly improve sales performance and profitability by changing the nature of their working relationships.

That's the conclusion to be drawn from a four-year study of 750 manufacturers and 500 distributors conducted by the Industrial Performance Group, a Northfield, Illinois, firm that specializes in supply chain and distribution channel management.

This study reveals that 82% of manufacturers and 92% of distributors believe that sales performance and profitability are being negatively impacted by problems in their working relationships.

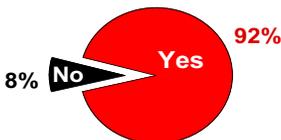
Fig. 1 Negative Impact on Manufacturers' Business



This research effort is a follow up to the 1997 benchmark

study *Report Card on Manufacturer-Distributor Relationships* conducted by the Industrial Performance Group.

Fig. 2 Negative Impact on Distributors' Business



This study shows that relationship-based problems manifest themselves in key ways. For manufacturers, the biggest problem with their distributors is a lack

of commitment to their products and promotional programs.

Participating manufacturers also report that distributors lack sales and marketing skills as well as the ability to effectively manage inventory.

The number-one problem for distributors is the ineffective or inconsistent management of

territories by manufacturers. The result is multiple and often conflicting channels to market, including direct selling.

This condition greatly reduces the level of distributor commitment to and trust in the offending manufacturers.

The research also reveals that manufacturers continue to do a poor job of providing direction for their distributors. Only 17% of distributors indicate that they have clearly defined goals and plans with manufacturers for accomplishing these goals.

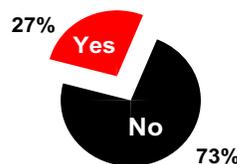
Many of the same problems surfaced during the 1997 benchmark survey. Data from the second phase of the study reveals that conditions in their working relationships appear to be getting worse.

Nearly half, 49% of manufacturers, and 42% of distributors tell us that the overall level of commitment in their working relationships is very low.

This represents a nine percentage-point drop from the benchmark established in 1997.

Fifty-one percent of distributors and 34% of manufacturers indicate that there is a low level of cooperation in their working relationships. This is significant in that it indicates that the level of trust in these relationships is also low since the two are highly interrelated.

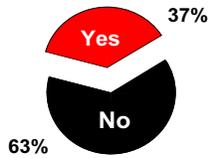
Fig. 7 High-Quality Two-Way Communication with Distributors



The greatest area of concern is the extremely low level of communication between manufacturers and distributors. Seventy-three percent of manufacturers and

63% of distributors indicate that high-quality two-way communication is virtually nonexistent in their working relationships.

Fig. 8 High-Quality Two-Way Communication with Manufacturers



Communication is the glue that holds the working relationship together.

Survey responses show that the level of communication be-

tween manufacturers and distributors has declined significantly over the past four years. Without this sharing of information, relationships are prone to high levels of uncertainty and conflict which severely hinder performance and profitability.

The Industrial Performance Group's findings should serve as a wake up call for manufacturers and distributors alike.

By neglecting to maintain their working relationships, manufacturers and distributors are being forced to spend more on sales and marketing budgets while their margins get squeezed even further.

Nonetheless, these findings should not be viewed as an indictment of either manufacturers or distributors.

The real message of this study is that tremendous opportunities exist for both parties to improve sales performance and profitability simply by strengthening their working relationships.

Toward this end we suggest that you and your management team:

- Study this report carefully and discuss the implications for your company;
- Determine what you can do to improve the level of commitment, cooperation, and communication in your current working relationships; and
- Encourage your industry trade associations to make the issue of manufacturer/distributor working relationships a high priority on their agendas.

Taking action to improve the working relationship is hard work, but it yields high returns.

Some manufacturers and distributors will do a better job of using this information to make positive changes. That's the nature of competition.



Introduction

Manufacturers and their distributors are being challenged by the globalization of markets, the emergence of new technologies, and customers whose demands are ever increasing. Despite these growing complexities, the basic issues remain the same for manufacturers and distributors alike: Increase sales performance without sacrificing profitability.

In the 1997 *Report Card on Manufacturer-Distributor Relationships*, the Industrial Performance Group discovered that manufacturers are less than enthusiastic about the overall performance of their distributors.

The 250 manufacturers who participated in the initial survey indicated that distributor performance was lacking in critically important areas such as commitment to suppliers, sales capabilities, and the ability to penetrate local markets.

In addition, manufacturers expressed concern regarding an emerging trend in distributor inventory management--stocking less inventory and ordering more frequently from their suppliers.

While these findings were certainly not revolutionary in nature, there was, however, a noteworthy conclusion to draw from the data: *Distributors themselves cannot be held solely responsible for many of their perceived shortcomings.*

Instead, the data from this first study clearly indicated that manufacturers must shoulder the lion's share of the blame for poor distributor performance.

The 1997 data, combined with field interviews, indicated that manufacturers were not doing an adequate job of telling distributors what was expected of them in terms of market coverage, sales goals, service levels, and inventory levels to be maintained.

In addition, the data indicated that manufacturers were not doing a good job of defining training and educational objectives for distributor sales personnel and in making training readily available.

The general conclusion that came from the first phase of this research effort was that a loose approach to managing manufacturer/distributor working relationships was the primary cause of most of the problems both parties were experiencing.

Current Environment

A lot has happened since the findings from the first Industrial Performance Group study were released four years ago.

The economy has slowed and teeters on the brink of recession, with three of the world's largest economies, The U.S., Japan and Germany, showing stagnant or declining GNPs in the most recent quarters.

Many of the old industrial giants have lost ground to upstarts who are more responsive to ever-changing market conditions.

On the one hand, customers have become more familiar, comfortable, and frequent purchasers of products sold directly on the web.

On the other, we have seen the meteoric rise and fall of the first wave of e-business strategies.

We have also seen razor-thin margins compressed to record lows in many industries.

Has anything changed in terms of the working relationships between manufacturers and the distributors who represent them in the marketplace?

The answer appears to be no, and strong evidence suggests that conflict in these working relationships is increasing, while trust and communication are declining.

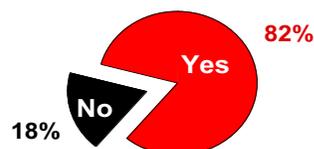
Preliminary Findings

Since 1997, the industrial Performance Group has conducted survey research and field interviews with an additional 750 manufacturers and 500 distributors.

This research reveals that manufacturers and distributors voice the same complaints, and they resonate even louder today.

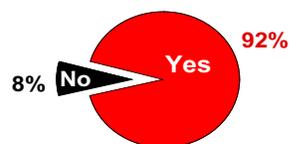
Manufacturers indicate that the number-one problem they experience with their distributors is a lack of commitment to their products and programs.

Fig. 1 Negative Impact on Manufacturers' Business



Manufacturers also report that distributors lack sales and marketing capabilities as well as the ability to effectively manage inventory.

Fig. 2 Negative Impact on Distributors' Business



When asked if these problems are having a measurable impact on their business, 82% of manufacturers indicate that distributor performance problems result in increased sales and marketing costs, lost sales volume, and the further erosion of margins.

Distributors respond that the number-one problem they experience with manufacturers is ineffective or inconsistent territory management. The result is multiple and often conflicting channels to market, including direct selling. This condition greatly reduces the level of distributor commitment to and trust in the offending manufacturers.

Distributors also tell us that an overall lack of direction and support from their suppliers results in confusion, conflict, and the duplication of efforts. Ninety-two percent of distributors indicate that these problems result in increased sales and marketing costs, lost sales volume, and further margin erosion.

What is significant about these findings is that both manufacturers and distributors agree that problems in their working relationships are having a negative impact on sales performance and profitability.

Improving the Working Relationship

Everyone talks about the importance of the manufacturer/distributor working relationship yet very little information exists on the subject.

A primary objective to the second phase of the Industrial Performance Group's research effort is to find answers to the following key questions:

- How do you define the working relationship between a manufacturer and the distributors who represent them in the market place?
- How do you objectively measure the relationship?
- How do you manage the relationship so that it produces mutually beneficial results?

The Eight Attributes of Peak Performance

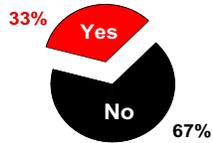
Survey data and field interviews with hundreds of manufacturers and distributors in a wide variety of industries enabled the Industrial Performance Group to identify eight attributes that determine the sales performance and profitability of manufacturer/distributor working relationships.

- 1) The manufacturer and distributor share a clear and common understanding of the conditions that exist in their industry;
- 2) They have developed goals and plans for accomplishing these goals;
- 3) The manufacturer and distributor are highly sensitive to the ever changing needs of their mutual customers;
- 4) They have clearly defined the roles and responsibilities of each party;
- 5) They take action to assure that everyone involved has the knowledge and skills to effectively perform their assigned roles and responsibilities;
- 6) The manufacturer and the distributor engage in high-quality two-way communication;
- 7) They are both strongly committed to their relationship; and
- 8) There is a high level of cooperation between the manufacturer and the distributor.

An assessment of The Eight Attributes of Peak Performance in phase two of our research reveals that the root cause of the sales performance and profitability problems for manufacturers and distributors is primarily an overall lack of direction.

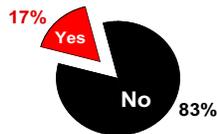
In other words, they do not have clearly defined goals in place, nor do they have plans to accomplish these goals.

Fig. 3 Have Clearly Defined Goals With Distributors



Only 33% of manufacturers indicate that they have clearly defined goals in place with their distributors.

Fig. 4 Have Clearly Defined Goals with Manufacturers



It is important to note that only 17% of distributors hold this same perception.

Goals are important because they establish the fundamental purpose of the working

relationship. They define the specific outcomes that both parties are working to accomplish. Without clearly defined goals, the working relationship is prone to uncertainty, conflict, and poor sales performance.

Plans define the specific actions that must be taken in order to accomplish a goal. Without plans, manufacturers and distributors end up performing random and often unrelated activities that are costly and ineffective.

Only 25% of manufacturers and 17% of distributors indicate that they have plans in place to accomplish their goals.

This finding is significant because the absence of a plan leads to poor decision-making, wasted resources, increased costs, and poor sales performance.

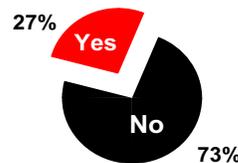
A lack of clearly defined goals and plans is further compounded by a low level of commitment and very low levels of communication and cooperation between manufacturers and distributors.

Commitment is the extent to which both parties are willing to allocate their resources (time-money-people) in support of the goals of the working relationship.

Nearly half, 49% of manufacturers, and 42% of distributors report that the level of commitment in their working relationships has suffered a nine percentage-point drop from the benchmark established in 1997.

Communication is the glue that holds the working relationship together. It provides a mechanism for coordinating and monitoring the resources in the relationship.

Fig. 7 High-Quality Two-Way Communication with Distributors



In addition, the efficient collection and sharing of information can provide manufacturers and distributors with a first-to-market competitive advantage in today's constantly shifting environment.

Fig. 8 High-Quality Two-Way Communication with Manufacturers



Sixty-three percent of distributors and 73% of manufacturers indicate that two-way communication is virtually nonexistent in

their working relationships. This represents a significant decline from the benchmark established in 1997.

Cooperation is the extent to which the manufacturer and its distributors work together to set goals, develop plans, monitor progress, and take corrective action when necessary. Cooperation and trust are highly interrelated.

Half, 51% of distributors and 34% of manufacturers, report a low level of cooperation in their working relationships.

Fig. 9 Low Level of Distributor Cooperation

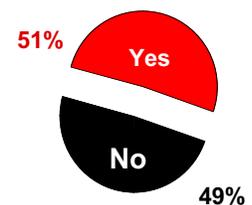
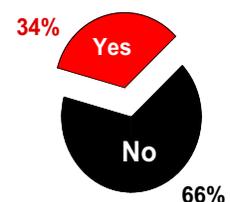


Fig. 10 Low Level of Manufacturer Cooperation



This finding implies that the level of trust in their relationships is also low and relates directly to the decline in levels of commitment and communication in these working relationships.

Without trust, there is no commitment, communication or cooperation.



Conclusions

Manufacturers and distributors both agree that problems in their working relationships are having a negative impact on sales performance and profitability.

The survey data also indicates that both parties are keenly aware of the need for mutual goals, long-term planning, and better communication. However, good intentions do not by themselves produce results.

So why is it so hard for manufacturers and distributors to change the nature of their working relationships when they know that doing so will improve sales performance and profitability?

Complacency appears to be the most common barrier that keeps manufacturers and distributors from taking action to improve their working relationships.

Complacency occurs when the way things are done seem normal and comfortable because they are familiar, not because they are the right things to do.

Complacency is reinforced when the members of a business team share a false set of beliefs regarding conditions in their industry,

their position within the industry, the needs and expectations of customers, and how they should compete.

The following statements are signs that an organization may be gripped by complacency:

“Everyone has problems with their distributors”

“We just need to be more focused”

“The customers are just confused”

“We’ve been through tough times before”

“This has always worked in the past, why change?”

“If we all just work harder, everything will be OK.”

The one thing you can count on is that nothing is going to change until someone proves that the status quo should no longer be supported.

Managing the manufacturer-distributor working relationship has never been easy. In today’s environment it has become even more complicated and demanding. Taking action to improve the working relationship is hard work, but it yields high returns.

As customers continue to demand more and more from their suppliers and severe price and service warfare becomes the norm in most industries, a manufacturer/distributor working relationship with high levels of trust, communication, and cooperation can often be the difference between being a leader or being an also ran.



About the Industrial Performance Group

The Industrial Performance Group specializes in helping manufacturers and distributors to increase sales volume, improve profitability, and build customer loyalty by better managing the relationships, processes, and practices in supply chains and distribution channels.

We help our clients accomplish these goals by:

- 1) Helping them identify the root causes of their problems;
- 2) Helping them develop workable plans for improving sales performance and profitability;
- 3) Assuring the successful implementation of these plans by helping them identify and overcome the barriers to change.

To find out how the Industrial Performance Group can help get you started on the road to improved sales performance and profitability, call us at 800.867.2778
or visit us at

www.indusperfgrp.com



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