

**T**he introduction of the Euro and the anticipated growth of electronic commerce are forcing companies to rethink their European strategies. Many multinationals have formed internal 'Euro teams' to examine the pricing and administrative problems these events will create.

But these teams are rarely asked to examine distribution strategy. This is unfortunate. Over the last 12 months we have spoken with leading manufacturers, distributors, and customers of chemical, entertainment,

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# Channel Management

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***E-Commerce is here, and the Euro will soon be in people's pockets.***

***Can your distribution policies cope?***

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computer, construction and safety products. We learned that:

- The effects of the Euro and the Internet will change how your products reach the market, who brings them there, and how these 'providers' should be rewarded
- traditional country-specific trading terms and discount conditions are inadequate to cope with these changes.

To understand why this matters and how much you may be affected, see how much your company has in common with manufacturers in the markets we investigated. First, all category leaders investigated operate worldwide, but most of their European distributors are small and regional. This is especially true in Germany, Italy, and Spain, less so in the United Kingdom. True multinational distributors are rare, and currently there are no pan-European distributors.

**T**he manufacturers still set their distribution policies country by country. The results: one company uses four fundamentally different sets of trading conditions in Western Europe, from pure volume-based discounts to traditional A-B-C systems. The top discount off list price which a distributor can receive varies by as much as 24 percentage points across Europe.

On the distribution side, the Euro and the

Internet are already causing increased competition and consolidation. Asked about the Euro's effects, one distributor said that "we will see the emergence of big, powerful distributors across the whole region. I'm convinced that in 5-10 years all slots will be taken. If you're not in, you're out."

**O**ne of his competitors, meanwhile, says his company "is worried about the Internet. We are afraid that we will lay the groundwork and the customer will make his next purchase on line. And who could blame them?" This is no minor problem. His company sells a certain branded product on-line for the around US\$1.00. The exact same product can be ordered – with the exact same effort – from a US on-line distributor for 40 cents.

As their size and power increase, industrial distributors – much like their counterparts in consumer goods – will start demanding the best rebates, discounts, and bonuses when they set up in another country. "It's extortion, plain and simple," as a marketing manager for a construction products company described it. As end customers wake up to on-line shopping, they will render European borders and the accompanying price differentials largely irrelevant.

If this situation sounds familiar, you are not alone. But you can solve the problem.

One of the most important lessons we learned from our talks with manufacturers is that distribution strategy – or channel management, if you will – must be an ongoing process and not just a series of ad hoc events.

We are not recommending sudden and swift harmonization of trading conditions across Europe. But we strongly suggest that you begin controlled convergence toward a consistent, economically sensible strategy for channel management. This strategy and the resulting trading conditions need to be customer-oriented, flexible, implementable – and appropriate for your company's market situation. Here's how to do it:

#### **1. Audit your current distribution conditions.**

**G**et your European sales and marketing managers around one table to describe their current condition systems. Why did they choose their particular strategy and set of conditions? What factors drove their decision? You and your managers will discover that the de facto strategies are different than what's on paper. You will also learn what your managers' strategies and motivations have in common.

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***Break down your distribution chain from the customers' point of view by asking two questions:***

***What do your customers expect?***

***Whom do they expect it from?***

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## **2. Determine your current market situation.**

**T**he currency markets speak of a two-speed Europe. In industrial distribution, there is a five-speed Europe. In discussions with your managers, find out how fragmented your domestic markets are, how polarized they are (gap between large and small dealers), and how they are growing. You will notice surprising disparities. In one case a Spanish subsidiary had trading conditions almost identical to Germany's, even though Spain's market situation had much more in common with Italy than Germany.

## **3. Identify what your customers expect**

**B**reak down your distribution chain from the customers' point of view by asking two questions: what do your customers expect, and whom do they expect it from? National differences are not as great as you might believe. Customers in Germany, France and Spain often answer the same questions with the exact same words. Many manufacturers and distributors still do not know precisely what their customers want and especially from whom they want it. The misunderstandings are often subtle, but nonetheless critical when you are trying to put together a customer-oriented distribution policy. With the answers to these questions, you will be able to redefine the roles you and your distributors need to perform, taking your own goals and cost structures into account.

## **4. Develop potential options for a new system**

**T**his system has two components: the functions you want to reward, and the way you package those rewards. In other words, you reward those functions which lead to customer value, and you 'sell' the system to your distributors in line with their market power. As their power grows, you need to 'pick the winners' among your distributors and work closely with them. The stronger your winners become, the more you should integrate them as partners. As one manager said, "the emphasis shifts from how much did you buy? to how well did we work together to develop our market?"

## **5. Implement.**

**H**ow do you convert volume-based and A-B-C systems into a function-oriented, modern channel management system overnight? You don't. In fact, you can't. Managing your distribution channels is an evolutionary process. In a first step, leave your discount or rebate levels the same on average, but change the way you reward distributors. You need to work closely with your European sales and marketing managers to see what these changes will mean for their individual distributors.

If designed and implemented correctly, your new system will reward and promote quality and professionalism in your distribution chain. You will gain a flexibility which individualized national systems cannot provide, and you give your distribution chain a much stronger customer orientation.

To develop customer-oriented, flexible, and implementable trading conditions, you will need to:

**1. Audit your current distribution conditions.**

Get your European sales and marketing managers around one table to describe their current condition systems.

**2. Determine your current market situation.**

Find out how fragmented and polarized your domestic markets are. You will notice surprising disparities.

**3. Identify what your customers expect.**

There are two central questions: what do your customers expect, and whom do they expect it from? With these answers, you will be able to redefine the roles you and your distributors need to perform.

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Managing your distribution channels is an evolutionary process. You need to work closely with your European sales and marketing managers to see what these changes will mean for their individual distributors.

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