

## The Next Big Things in “e”

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Remember when certain industry entities like SupplyForce, VerticalNet and SourceAlliance were going to change how we interacted with the customer? Remember how they were going to set you up with storefronts in e-megaportals and trading exchanges that would attract hundreds of thousands of customers and you would be left out in the cold, out of business if you didn't have one, too?

Remember how all computers were going to be connected and if you weren't connected, you'd be out of the trading loop? Remember how all your large industrial customers were going to be using e-procurement packages like Commerce1 and how you were going to need an e-catalog and a business system that could connect to these exchanges and let customers read into your inventory and pricing?

Remember how Andersen Consulting's Facing the Forces of Change said that over 45% of customer purchases from distributors would be electronic by 2004? Well, it's 2003, and precious few are buying on the web.

And finally, remember how distributors were going to be “dead” in the new economy, how they were going to be moved aside by auction facilitators like Freemarkets?

### **So what did “e” really do in this industry, and what real effect did it have? What will be the next big thing?**

Consultants like to grab hold of something and take credit for predicting the next “Killer App”. I admit it; I've fallen prey to that inclination at least once... falling in love with “e”. I learned my lesson, though, just by watching what happened over the last ten years since windows made computing easier for the masses.

What did I learn? There is never a really “next big thing” that takes our market by storm. We take time to absorb them. OK, so the Internet was a big thing. But it didn't grow in the same areas and in the same way that we thought it would. The really startling things happen steadily, over time, and exponentially. They start

small, but we don't keep track and they creep up on us. Then we look back and say, “Wow, it really WAS a big thing!”

For example, online purchasing never developed as fast as we thought it would. The best electrical distributors don't even approach 5% of sales online. Most that are doing “well” report 2% of sales. But something else happened since we headed for the hills on eCommerce halfway through the year 2000 when the e-bubble burst.

### ***Grainger.com snuck up on us.***

After all the different Grainger e-initiatives, they scrapped all the peripheral sites and scrapped their plans to spin off Grainger.com, electing to keep it in the core business. Grainger.com became 11% of Grainger sales.

***At \$420 million sales for 2002, assuming the electrical mix of approximately 20% is the same for online sales, Grainger.com would be the 55<sup>th</sup> largest electrical distributor in the U.S.A.***

Grainger's online sales have grown steadily from about 2.5% of total sales in 1999 to 5% in 2000 and 11% in 2002. Furthermore, Grainger reports that they get an 11 percent incremental increase in sales from customers that begin using Grainger.com. They also report that using personal buying lists (frequently purchased items) increases sales dramatically over customers that don't keep such lists.

Grainger, by the way, has done an excellent job of managing through the downturn in the industrial MRO market. Grainger increased profitability despite a downturn in sales, mainly by raising Gross profit by over two percentage points. Online sales could have had something to do with that.



### Grainger Operating Results 2000-2002

Income Statement	Dec 02	Dec 01	Dec 00
Revenue	4,643.90	4,754.30	4,977.00
Costs of Goods Sold	2,952.20	3,061.80	3,284.80
Gross Profit	1,691.70	1,692.50	1,692.20
Gross Profit Margin	36.40%	35.60%	34.00%
SG&A Expense	1,207.00	1,211.60	1,250.20
Depreciation & Amortization	93.5	103.2	106.9
Operating Income	391.2	377.7	335.1
Operating Margin	8.40%	7.90%	6.70%
Nonoperating Income	10.9	-10.5	20.9
Nonoperating Expenses	6.2	10.7	24.4
Income Before Taxes	397.8	297.3	331.6
Income Taxes	162.3	122.8	138.7
Net Income After Taxes	235.5	174.5	192.9
Net Profit Margin	4.60%	3.70%	3.90%

The only really big thing we've seen, and will continue to see, is how technology slowly (seemingly) but surely changes the way you work, and the many different applications it will have that together, will creep up on you if you don't stay current on technologies that could effect your business and your customer's business. However, when you look back at how fast some applications were adapted since 1996, you might change you mind about how much attention you should pay to technology developments.

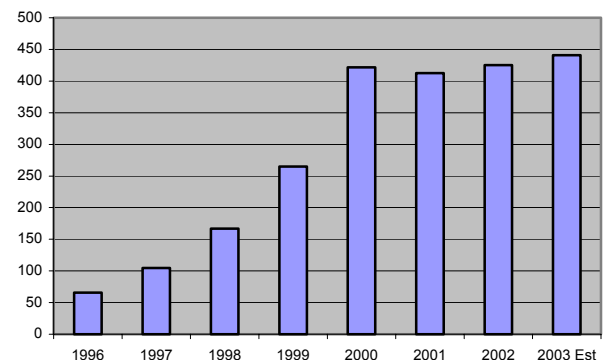
Look at how fast **email** has become a dominant form of communication! Microsoft Outlook was only launched in 1997. Now it's the dominant email and contact management application for the masses. It was easy to use, maybe too easy. Now people are trying to figure out how to filter email effectively because they get entirely too much.

So, why can't electrical distributors replicate those results on the web?

1. **We don't have good product data and images.** Currently available Industry data has flaws, shortcomings and customers can't trust the images or ratings data. Grainger contracts to have their product data built to their specifications.
2. Our web storefronts are not very exciting
3. Our web storefronts are not so easy to use
4. We don't market them as well as Grainger

**We thought that attractive content would attract customers and prospects to websites.** Instead, it turns out the most frequented pages are your contacts, your locations, your line card, and your e-Catalog on your storefront, if you have one. Customers don't necessarily like to buy on your website (it can't match the ease or fun of Amazon or Grainger), but they like to look things up. Why? Perhaps they've seen errors in your data. I have. That could be holding up progress in online purchasing. But I don't think it's holding it up a lot. It's a combination of things. Poor data is only one of them.

Cell Phone Shipments Worldwide (Mill of Units)



Look at how fast **cell phones** grew in the last 7 years, from 66 million units per year to an estimated 441 million units sold in 2003. They only hiccupped in 2000 as the tech boom stalled. Now they are back on the rise.

**Wireless applications like RF devices** have infiltrated the distributor warehouse, and smart distributors have discovered that the automated warehouse cuts down on receiving, picking and shipping mistakes. Most distributors don't even use RF devices in the warehouse for receiving picking and shipping orders. They might fall hopelessly behind when the next "little thing", RFID smart tags hit the scene, because these



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little devices could virtually eliminate the need for taking physical inventory on most products.

### **So what has really happened in the last 10 years, and what will happen next?**

Two really big things have happened that will open the door for a lot of little things, which together, will equal a big thing. It all has to do with leveraging the connectivity of the internet, working together, and getting different equipment to work together.

In late 1999 and 2000, I was on the speaking circuit talking about changes in distribution for 2005. The first change was "**Connectivity changes all the rules.**" Connectivity is about to explode on us. The stage is set, now we need to get connected with the foundation that has been laid.

### **Past Big Thing #1: Basic Computer Skills and Network Knowledge.**

Individuals have been well acclimated to business systems and computers. We have the basic skills. No matter how much you despise Microsoft or Bill Gates, Windows and a web-integrated Microsoft Office gave us a common medium for communicating, and made computers usable by the masses.

In addition to Windows, We've learned to really use email and contact lists. We have learned to use our cell phones, although not all the power features. We can surf the web. We know how to use word processing, spreadsheets, PowerPoint, maybe even a database and FrontPage for simple web publishing. But we really haven't learned to collaborate well using these tools yet. Why? Because we all work differently. We're still individualistic in the way we use technology, and we will always be, until technology gets smarter, channeling our inputs and thoughts into a common collaborative language with our coworkers, customers and suppliers.

**Past Big Thing #2: The Internet** emerged as a highway for transmission of data at reasonably high speeds. It opened the door for commerce and communications to flow. eCommerce, however, is not flowing like it could, because we've done things too individualistically in the past, and it is still a labor intensive process to get two different computers to communicate with each other. It is still the Tower of Babel out there

in distribution channels, with too few people that know how to translate from one system to another.

### **The Next Big Things: Many Smaller Things that work together.**

So, the next big thing is how things will start pulling together from all angles. It took a while, but the foundation is laid. We know how to use our computers individually, and the highways are built. But we don't know how to drive collaboratively so well yet, and we don't have a common fuel system: data standards for products and business communications.

Our problem is independence and fear, which limits collaborative communication. We want to do things our own ways in our own companies, and remain islands. We don't quite seem to believe that adhering to common communications and data standards will make all of us more productive. So many of us stick our head in the sand and sandbag industry efforts to build product and pricing databases like the IDW by giving them lip service, cryptic data or absolutely nothing at all but a cold shoulder. Fear, Apathy and Doubt need to be overcome for industry productivity's sake.

### **Next Big Thing #1: A Common Product Language**

It's almost 2004, and we still don't have a common product information database yet in this industry. Why not?

It all boils down to lack of awareness and apathy on the part of distributors and manufacturers. Plus, some manufacturers fear that a common database will make it too easy to compare theirs to others.

That's not all. The original premise for the IDW didn't take into account data requirements for true marketing usage. Sub-branding elements like Philips Alto lamps, Cutler Hammer Freedom Series Starters are not entered in fields so that e-catalog and print catalog builders can group products together on a page or consecutive pages. The IDW is still using the age-old Trade Service three level hierarchy for identifying products, which is more functional vs marketing-oriented. Plus, jpeg and gif images may look fine on the web, but they look terrible in print catalogs. High resolution tiff or eps images are required for decent print applications.



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Print catalogs, by the way, have not died. In fact, they serve as a great one-two punch with a web ordering system. Customers like choices.

The bottom line is that the IDW database needs to be enhanced, manufacturers need to understand the benefits of good product data, and both distributors and manufacturers both need to experience how good data can be used to both enhance operations accuracy and marketing effectiveness. We've got examples popping up around us that we can learn from.

### Next Big Thing #2: Wireless Networking

The explosion of easy to install consumer wireless (WIFI) network installations will drive corporate installations.

The Internet foundation has been laid. We've acquired the individual computer skills. The next big thing will be complete freedom to be always connected wherever, whenever, through all kinds of devices: Wireless communication networks, Ubiquitous sensors and Smart tags (RFID) will complete the connectivity picture.

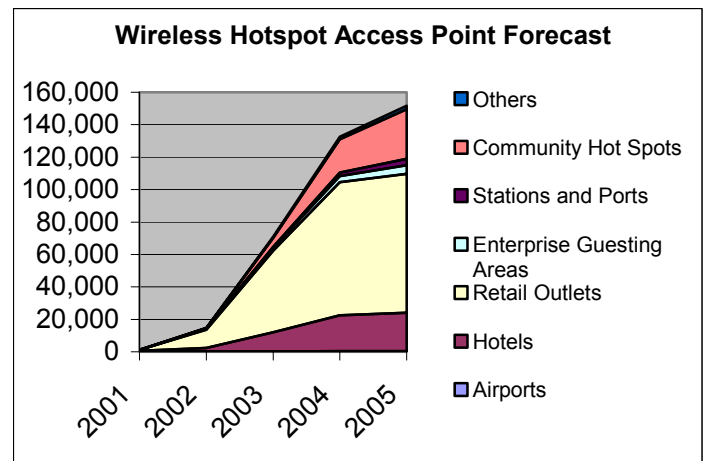
The only thing standing in the way of wireless proliferation is fear for your network security. Wireless proponents will need to overcome the current security paranoia, recently exacerbated by the rise in Internet Trojan horses and worms that scan the internet for open ports on poorly protected computers.

I believe Wireless will. It has too much potential to let it die, and there's too much untapped business productivity which wireless connectivity can help to realize.

One thing that will increase the demand for corporate wireless systems is the explosion in easy to install, economical wireless networking for the home. A recent IDC survey found that 33% of home networking systems used wireless at home, while only 27% of these had wireless access at work. The IDC report says that demand for wireless at work will be driven by workers that install wireless at home and come to expect it at work, and also by those that come to expect it once the network of "hotspots" becomes more ubiquitous in airports, retail stores like Starbucks, schools, libraries, hotels and other community places.

### Top 5 Worldwide Wireless LAN Equipment Vendors by Unit Shipments for 2002 (Thousand of Units)

Manufacturer	2002 Shipments (thousands)
Linksys	2,860.
D-Link	1,881.
Buffalo Technology	1,857.
Symbol Technologies	1,762.
Proxim	1,741.
Others	9,495.
Total	19,598.



Source: Gartner Dataquest (June 2003)

### Next Big Thing #3: Utility Computing

Alan Ganek, vice president of IBM's autonomic-computing initiative, said, in a Fast Company article: "The long-term promise of self-aware computers and software is greater reliability with fewer human baby-sitters. Right now, IT staffs at large companies are swamped with the tasks involved in "managing, maintaining, upgrading, and the care and feeding of their systems. That work squeezes out any innovative projects that they'd like to be doing to establish a competitive advantage."

Distributors may, at some time in the future, give way to utility computing. Some call this an ASP, or Application Service Provider, The concept is



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the same: Somebody else runs your system for you and you can run your business. Some distributors fear someone else housing their data, however.

But some pioneers will eventually overcome their fear and decide to throw caution to the wind and get rid of their headaches. Yes, they will let a business system provider do the whole job of running the computer system for them. Offsite, for the most part. The database will be accessed over the internet. You will have less software and data on your local machine and more on the provider's host. Owners and security freaks will have to get over the fact that there's not a lot of equipment in the back room with a lot of flashing lights. Imagine: concentrate on using the applications instead of keeping them running!

#### **Next Big Thing #4: CRM will come of age in distribution.**

Already, two CRM (Customer Relationship Management) applications are vying for a beachhead in distribution. Though no electrical distributor has jumped off the cliff yet with powerhouse Siebel systems, upstart Taylor Market Media Group's Sales Management Plus, tailored for the electrical distributor, and **NxTrend's Correlation™** CRM applications take different approaches. Correlation seems to track, manage, and report customer and employee interactions of any kind. For example, Automation powerhouse distributor McNaughton McKay uses it to track technical automation specialist activity and report the value added to customers. Correlation is also excellent at selecting customers based on transaction history or other criteria and automating the process of sending email campaigns.

**Taylor Market Media Group's SMP** approaches from a different angle. They are hell bent on giving the distributor the best targeting information possible to manage sales and marketing priorities. This powerful yet economical package has the best sales reports by customer and product line you've seen to date. You can see where you are vs last year on sales and gross profit, and think through the "holes" in your product sales. It also helps you target customers for marketing communications based on any demographic or transaction history data.

Where is CRM going? Nowhere really big until people figure out that you CRM specialists to

drive the process of maintaining contacts. It never works to leave the job of entering and maintaining contacts entirely up to salespeople. They need to be followed up after, and the CRM specialists that do the follow up need to have contact with customers as well. Successful direct marketers like dental supplies distributor Henry Schein will tell you that in spades. They have to do it.

**Next Big Thing #5: Smart tags and sensors** will give us the ability to collect and monitor just about anything anywhere.

Smart tags using RFID (Radio frequency identification) have the potential to eventually replace many UPC bar codes. They go beyond product identification, however, and can tell systems, where a product is, how it's been handled, and when it has been handled, or how long it has been in a location. Put a smart tag "reader" in a warehouse, truck, a store or even your customer's storeroom, and it can sense all the smart tags in the area. Yup, you can take inventory without humans being present, even eliminate the RF bar code reader and the user.

**Who's already using smart tags?** If you have a Speedpass to pay for gas at Exxon or Mobil, you're one of seven million people that have a version of the smarttag on your keychain.

**Gillette** uses the tags to track cartons of razors through a packaging and distribution center in Massachusetts. Eventually, these tags could also tell retailers how many of their products sit on shelves, just like distributors could virtually eliminate physical inventory and cycle counting for many products, or install smart tag systems in customer storerooms. Smart Tags could be affixed to rental equipment, assets, just about anything you want to keep track of.

Smart tags could be a long way off, though if they don't get someone with big money to give them a great jump start and catapult producers down the experience curve so the cost can get them down to less than 5 cents apiece. That will probably happen in 2005, when **Wal-Mart's** top 100 suppliers will be required to attach them to every pallet of products delivered. How long will it take to reach wholesale distribution? When manufacturers discover that they, too, can escape the rigors of physical inventory taking, maybe not too long. Smart tags could eventually be used to track the eventual location of products



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all the way to the customer. But that has huge privacy implications we probably won't crack.

### **Pulling All the Little Big Things Together**

In a recent Business Week interview, I think Bill Gates said it best. When asked where he saw the potential for growth in technology, he said:

"Look at business intelligence, workflow, collaboration, real-time communication: We've just scratched the surface. How do you make all those back-end systems easy to manage and secure? How do you make it easy to write Web-service applications that cut across the boundaries, inside a company and between companies? Now that we have all this Internet connectivity, how can buying and selling and planning be done differently? That's an unrealized dream. Our challenge is to make those dramatically simpler."

The answer is where I started this; Connectivity changed all the rules. Connectivity and individual computer skills need to grow into collaborative behaviors and business practices.

The foundation is there. In THIS industry, we've got to decide how we're going to leverage it.

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