Executive Summary Brief

Understanding Jan-San Redistribution

A Guide for Manufacturers, Distributors, and Wholesalers in the Sanitary Supply Industry

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Introduction:

Redistribution of Sanitary Supply products has evolved to the point that most channel manufacturers and distributors recognize its value. Many Jan-San distributors, both large and small, purchase from wholesalers; and many manufacturers are taking advantage of the benefits offered by wholesalers.

At the same time, there are distributors and manufacturers who are not yet taking full advantage of the benefits offered by wholesale redistributors, often due to uncertainty and concern about the wholesaler's role.

This Executive Summary outlines the business impact of wholesaler redistribution for both manufacturers and distributors, and explores the key questions and issues raised by both. It is organized as follows:

- Why Use a Wholesaler?
- How Does Wholesaler Redistribution Work?
- The Economics of Redistribution for Distributors
- The Economics of Redistribution for Manufacturers
- Building An Effective Wholesaler Redistribution Program
- Barriers and Enablers

*The book, **Understanding Jan-San Redistribution**, provides much more detailed analysis and case studies to help guide your decisions.*

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A Guide for Manufacturers, Distributors, and
Wholesalers in the Sanitary Supply Industry***

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Why Use a Wholesaler?

Successful wholesalers have grown because they are uniquely positioned to provide great value to both manufacturers and distributors.

Sanitary Supply manufacturers and distributors enter into wholesaler redistribution programs for one or both of the following reasons:

1. To reduce costs
2. To build volume

To the Sanitary Supply ***manufacturer***, a sound redistribution strategy will yield:

- outsourced management of small, high-cost-to-serve customer orders
- access to new customers who are otherwise difficult to reach and serve
- reduced credit risk
- simplified logistics
- additional sales support
- accelerated sampling response

Jan-San ***distributors*** who source products from wholesalers likewise benefit from:

- faster inventory turns
- shorter lead times
- more frequent deliveries
- no minimums per manufacturer
- the efficiency of one order, one delivery, and one invoice for multiple manufacturers
- higher service levels
- improved fill-rate economics

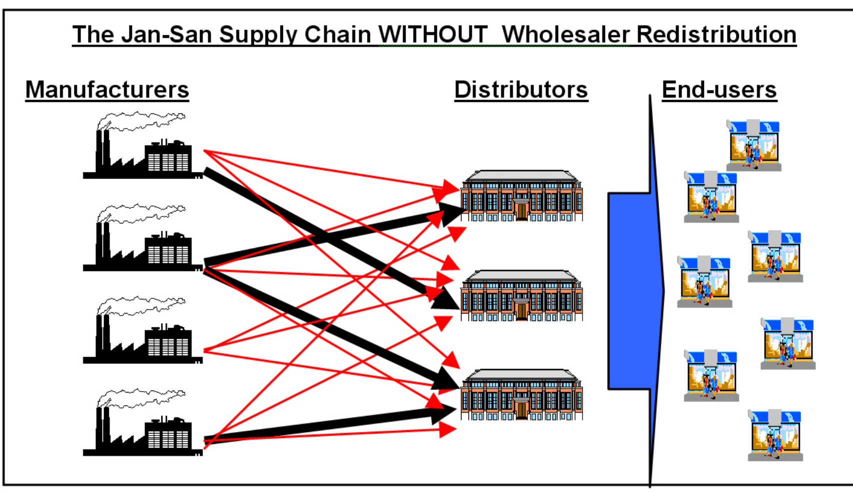
How Does Wholesaler Redistribution Work?

To the uninitiated, redistribution via a wholesaler would appear to be an unnecessary “extra step” in the Jan-San supply chain, shoehorned between manufacturers and their distributor customers.

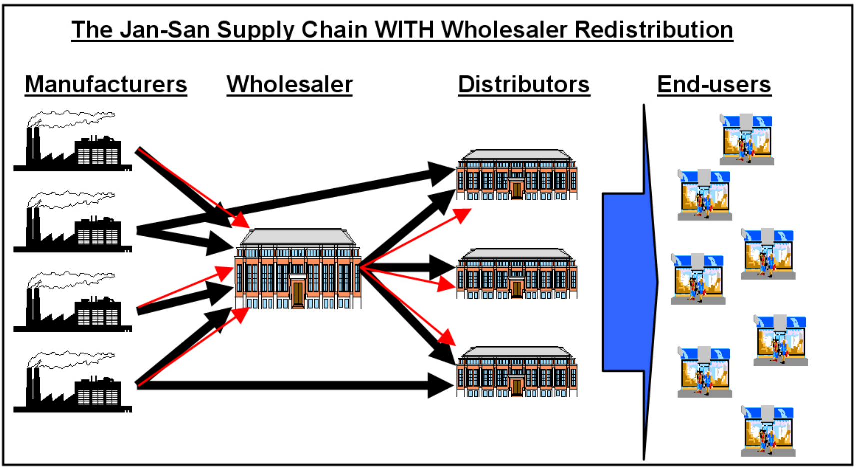
But just as the Jan-San distributor provides a broad range of products to the end-user, the Jan-San wholesaler can simplify and streamline the supply chain between manufacturers and distributors. The wholesaler does this by purchasing large quantities from multiple manufacturers, consolidating the products in his warehouse, and providing just the right mix of products to his distributor customers.

The result is elimination of small, high-cost orders for the manufacturer, and improved inventory turns and service levels for the distributor.

The diagram below depicts the Jan-San supply chain without wholesalers being involved. The thin arrows represent LTL shipments and the bold arrows represent truckload shipments.



The diagram below represents the Jan-San supply chain with Wholesalers facilitating the flow of product from Manufacturers to Distributors. Notice the reduction in smaller shipments and a more efficient flow of products to the Distributor level, often resulting in higher service and fill-rate economics at the End-User level. Notice also the overall reduction in outbound shipments for the manufacturers, and inbound shipments for the distributors.



The reality of converting reduced activity with fewer shipments to reduced cost is addressed in Understanding Jan-San Redistribution. For now, let it suffice to recognize that if activity drives cost, then the elimination of activity must result in the elimination of cost.

In return for these services, manufacturers generally pay an allowance to their wholesalers, which reflects the manufacturer's cost avoidance and other factors which are discussed in Understanding Jan-San Redistribution. The distributor may pay a higher price for the products than he would if he dealt directly with all of his manufacturer suppliers, but this price premium is offset by the benefits of lower inventories, faster inventory turns, lower order management costs, and improved service levels to the end user.

The Economics of Redistribution for Distributors

From a distributor's perspective, redistribution also provides an effective solution to several persistent problems. **Inventory turns** are a major driver of distributor profitability, and redistribution offers the opportunity to make a significant improvement in this area. Without redistribution, the order cycle for a small-volume product line can easily be every 6-12 weeks; with redistribution, the distributor can receive product on a weekly (or even more frequent) basis.

Service levels to end-users are another key measure of distributor performance. During the "downtime" between orders, a distributor often runs out of one or more items from a manufacturer, but must wait until he can put together a minimum order before receiving replenishment. This results in out-of-stock cuts or substitutions, which raise problems for the manufacturer, distributor, and user alike. With frequent deliveries and shorter order lead times, wholesalers provide the opportunity to significantly improve outbound service levels.

When one considers that redistribution offers the potential to reduce cost, improve service, increase inventory turns, and broaden the product offering without requiring additional space, it is easy to understand why savvy distributors embrace it. All of these benefits contribute to improved profitability via "fill rate economics," or the cumulative effect of providing high service levels with fast turns and low inventory costs.

Understanding Jan-San Redistribution will provide detailed worksheets and instructions to help distributors calculate the impact of sourcing products through a wholesaler vs. buying direct from the manufacturer. These worksheets take into account the changes in product cost, inventory turns and average inventory value, and calculate the ROI and Turn-Earn ratio for both direct and wholesaler sourcing.

Based on this information, distributors can make informed decisions about which lines are best sourced from a wholesaler, vs. purchased direct.

Understanding Jan-San Redistribution also contains GO DEEP ON FILL-RATE ECONOMICS; CHANGE STRATEGY, an article by wholesaling expert Bruce Merrifield (www.merrifield.com). This article presents a real-world case study in which:

- The distributor buys as much as they can from a wholesaler on a vendor managed inventory (VMI) basis.
- The wholesaler delivers in the middle of every night, 5 days a week so that whatever is sold out of the distributor's warehouse today or is ordered for next day delivery can get to the customer the next day after being cross-docked first thing in the morning.
- The distributor can then experiment with new ways to sell the next day availability of the wholesaler's additional 8500 items that they stocked above and beyond the distributor's 1500 stocked items.
- The distributor leverages the wholesaler's web catalog for all 10,000 items in their cash-n-carry, "wholetail" store just as Grainger and REI have done.

This example also demonstrates the "intangible" value of wholesaler sourcing, showing how shorter order lead times and improved service levels produce a "multiplier effect" on the distributor's financial results.

The Economics of Redistribution for Manufacturers

Before entering into a wholesaler redistribution program, a manufacturer should gain a solid understanding of how redistribution will impact his P&L. There are three major areas to consider:

- Cost Avoidance
- Revenue Impact
- Marketing Value

Understanding Jan-San Redistribution goes into great detail to help Sanitary Supply Manufacturers quantify these impacts.

Cost Avoidance:

When existing business is switched from direct to wholesaler service, a manufacturer has the potential to reduce both hard Logistics Costs, and softer Order Management costs.

Logistics Costs include the costs of shipping product to customers, and may also include deployment and forward warehousing if the manufacturer ships from mixing centers.

Order Management costs are often more difficult to quantify, but doing the work is usually an eye-opening experience. Order Management costs include all of the activity from receiving and entering orders through booking loads to extending credit, billing, and collecting. When the “percent of orders” is compared to the “percent of volume,” manufacturers begin to see that they are often “laboring like an elephant to give birth to a mouse!”

Once these costs are quantified, the manufacturer can calculate the Cost Avoidance opportunity represented by wholesaler redistribution.

Revenue Impact:

For the Sanitary Supply manufacturer, wholesaler redistribution offers the potential for increased sales volume on several fronts. The ability to reach hundreds of previously unknown distributors, jobbers, cash & carries, etc. is an obvious opportunity. But even existing direct customers who switch to redistribution may be sources of new volume, as a result of:

- Faster recovery from out-of-stocks
- “No minimum per SKU” policies which improve sampling response and minimize new item risk
- Ability to offer the manufacturer’s entire product line, without keeping it all in stock

But there may also be some important negative revenue impacts to consider.

Manufacturers who enforce strict bracket pricing will need to account for revenue slippage when a wholesaler buys at free-on-board (FOB) plant prices to serve existing business that was billed at the highest delivered price bracket. Special prices, bids, and trade deals all take on an added level of complexity when they are managed through redistribution. And the wholesaler's pricing practices relative to the manufacturer's price list must be clearly understood in order to develop an effective program.

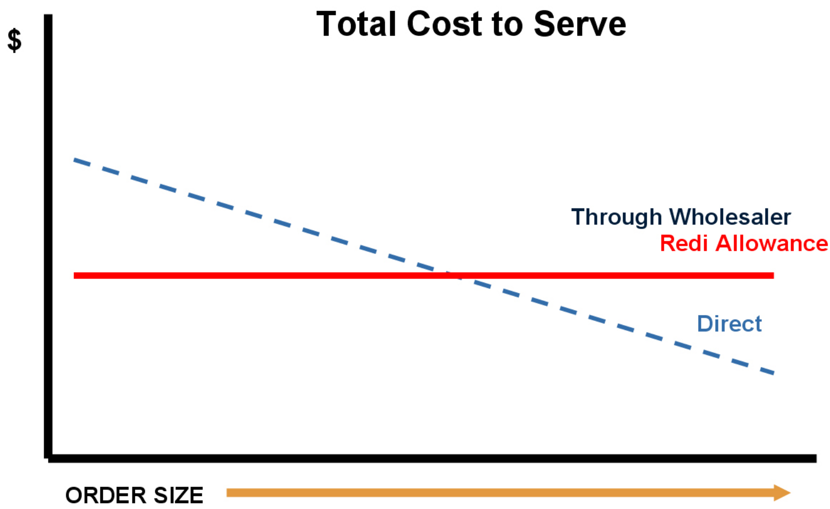
Marketing Value:

Another consideration is the Marketing Value of having your products available through wholesalers. Most manufacturers are initially attracted to redistribution as a means of reaching and servicing the small, non-mainstream distributors who represent incremental new business. The value of suddenly selling previously unreachable customers is very high, and Sales and Marketing people are instinctively prepared to pay for this value.

Building an Effective Redistribution Program

In order to take full advantage of the benefits of wholesaler redistribution, manufacturers must understand their Total Cost to Serve for various order sizes. Generally speaking these costs are very high for small orders, and decrease as order size increases.

When distributor orders are fulfilled through a wholesaler, the manufacturer incurs a flat cost regardless of the quantity shipped.



NOTE:
For purposes of illustration, we use “cost per pound” as the unit of measure for logistics costs. The Sanitary Supply industry is characterized by product lines which exhibit a wide range of “densities” (case weights and cubes), as well as values per pound.

For this reason, we must avoid generalities about quantifying costs. While a “per lb” approach makes sense for some items, others might be better measured “per cube” or “per case.”

Manufacturers are well served to quantify their costs to fill various order sizes on a "direct" basis, then compare this to handling the same orders via a wholesaler.

Conditions in the logistics industry are putting unprecedented pressure on Sanitary Supply manufacturers and distributors alike. The combination of record high fuel costs, reduced transportation capacity, and government regulation is placing a premium on supply chain efficiency. On a per-pound-basis, LTL is much more expensive than TL, especially if product falls in the higher priced freight classes. The value a wholesaler provides in this instance cannot be understated.

In addition, number of SKU's, pallet quantites vs. loose case quantities, and other customer order variables also drive cost into the process. Consideration must be given to all of these factors.

Understanding Jan-San Redistribution includes tables and detailed instructions to help manufacturers organize and analyze their Total Cost to Serve. Armed with this information, manufacturers will be able to make sound decisions regarding which customers are better served via redistribution, and the value provided by their Jan-San wholesalers.

Barriers and Enablers

Despite the growth of wholesaling, there is still a considerable amount of high-cost, small-order shipment activity from manufacturers to distributors in the Jan-San channel. While this can be attributed in part to “tradition” or “inertia,” it is also true that manufacturers, distributors, and even wholesalers cling to some beliefs and practices which perpetuate the inefficiency.

In this section, we identify these beliefs and practices (barriers), and offer suggestions (enablers) for overcoming them on the road to building a more efficient supply chain.

Barriers: Manufacturers

- Refusing to pay distributor allowance programs when volume flows through a wholesaler
- Abdicating business-building responsibility to the wholesaler
- Offering wholesaler service as “an option,” without encouraging high-cost, small-order distributors to use it

Barriers: Distributors

- Fear of losing the manufacturer relationships
- Clinging to “Gross Margin” as the sole determinant in sourcing decisions
- Allowing “resentment” to cloud judgment regarding wholesalers

Barriers: Wholesalers

- Refusing to provide trace reports to manufacturers
- Focusing only on “turnover customers,” not new customers
- Allowing “cost creep” to erode supplier profitability

Enablers: Manufacturers

- Establish and enforce appropriate order minimums and bracket pricing
- Encourage your small order/high-cost distributors to source your products via wholesalers
- Demonstrate to your distributors that “physical movement of boxes” is not the same as “relationships and communication”

Enablers: Distributors

- Analyze your product portfolio to see which lines suffer from slow turns and poor service levels; work with your suppliers and wholesalers to switch to wholesaler sourcing
- Ensure that your wholesalers and manufacturers work together to maintain the flow of information and sales/marketing support

Enablers: Wholesalers

- Provide trace reports to help manufacturers understand their business and provide appropriate distributor support
- Communicate thoroughly with suppliers to ensure a mutual understanding of target customers and pricing practices
- Work with suppliers to penetrate new accounts which are best served via wholesale redistribution

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Review Detailed Wholesaler Profiles in the Complete Guidebook:

Understanding Jan-San Redistribution.

About the Author

Dave DeWalt is President of Franklin Consultants, a firm that serves manufacturer clients on a variety of strategic, marketing and distribution-related projects.

Dave is widely recognized as an expert on the subject of redistribution. He has been published in Food Logistics magazine, and has conducted redistribution workshops for the Foodservice Sales and Marketing Association and the Chain Purchasing Conference. Dave also publishes the monthly "Foodservice Marketing Insights" newsletter; subscriptions are available from the "Free Resources" page of his website, www.franklin-foodservice.com.

Prior to launching Franklin Consultants, Mr. DeWalt was an Associate with A.T. Kearney. Industry experience includes fifteen years in Marketing, Sales, and Executive positions with Sara Lee Bakery, Vlasic Foods, and Awrey Bakeries.

Dave has a Bachelor's Degree in Hospitality Business from Michigan State University, and a Master's Degree in Marketing and Finance from the Kellogg School of Management, Northwestern University.

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This FREE *Executive Summary Brief* is the companion to SSWA's **Understanding Jan-San Redistribution: A Guide for Manufacturers, Distributors, and Wholesalers in the Sanitary Supply Industry**.

The complete guidebook can be purchased through authorhouse.com

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