

October, 2010

Achieving Operational Excellence in Wholesale Distribution: Poised for Recovery?

Wholesale distributors have faced challenges in the wake of the worst economic recession in recent times. Often caught in the middle between manufacturers and retailers, wholesale distributors are also threatened by disintermediation efforts from both ends. The Q3 2010 Aberdeen Business Review found the top 2010 goal for this sector to be improved profitability, leaving many distributors in search of operational excellence. Now as we close out what has proven to be a daunting year, as we begin to see glimmers of hope on the horizon, what must wholesale distributors do to be poised for recovery? Can Enterprise Resource Planning (ERP) provide benefits to improve operational performance and provide a level of differentiation that will allow distributors to grab their fair share of market as the economic indices begin to rise?

Distributors Have Been Hit Hard

The quarterly Aberdeen Business Review monitors both the business goals and strategies of companies across a broad spectrum of industry sectors, and also the impact of current economic conditions. While the recent economic downturn has wreaked havoc on many sectors, wholesale distributors have been particularly hard hit (Figure 1).

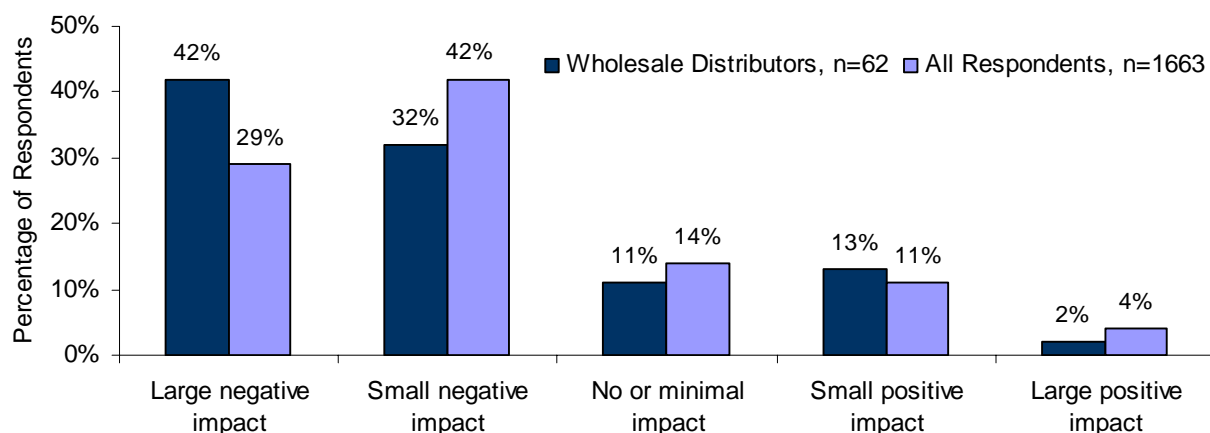
Sector Insight

Aberdeen's Sector Insights provide strategic perspective and analysis of primary research results by industry, market segment, or geography

Sector Definition

This Sector Insight is based on survey participation of 91 wholesale distributors responding to Aberdeen's annual ERP 2010 survey, along with 62 responses from wholesale distributors to the Q3 2010 Aberdeen Business Review.

Figure 1: Impact of the Economic Downturn



Source: Aberdeen Group, September 2010

While 71% of all companies surveyed experienced a negative impact, wholesale distributors were 45% more likely to characterize it as a "large negative impact."

As a result, 71% of distributors cut discretionary spending and 39% cut or deferred projects that required capital spending. While adoption of ERP is often mistakenly thought to be pervasive, over 50% of Distributors have yet to invest in an integrated suite of modules that will provide the operational and transactional system of record for their business. At the end of 2009, the Aberdeen Business Review found only 49% of distributors had implemented ERP. For those going into 2010 without already having made such an investment, it was likely deferred.

For those that have invested in ERP, Aberdeen finds the average implementation achieved results that could be used to justify the investment, while top performing implementations drive double digit cost reductions and improvements in schedule and efficiency. Therefore those without ERP lag significantly. Now as 65% of all respondents and 71% of distributors surveyed believe we have entered into a period of economic recovery, it will be all that much more critical to catch up to those who have already made the investment in ERP, and to strive to achieve the same performance as the "Leaders" in executing the most successful implementations.

Defining the "Leaders"

Aberdeen defined "Leaders" as the top 30% of aggregate performance scorers using the criteria shown in Table I. "Followers" represent the remaining 70%. These metrics were selected because of their relevance in assuring the performance of wholesale distribution and also for the potential impact implementation of ERP can have on them. Improvements captured were measured not as year over year changes, but as a direct result of ERP implementation. As efficiencies are gained, operating costs and cycle times from order to shipment are reduced. These, along with reductions in administrative costs and reduced inventory levels provide at least part of the basis in justifying the investment in ERP.

"We met objectives set forth at start of project and was within budget both in terms of time and money."

~ Staff, Small Distributor

Table I: Top Performers Defined as "Leaders"

Definition of Maturity Class	Mean Class Performance
Leaders: Top 30% of aggregate performance scorers	<ul style="list-style-type: none"> ▪ 17% reduction in operating costs as a result of ERP ▪ 98% inventory accuracy ▪ 95% complete and on-time shipments ▪ 12 hours cycle time from order to shipment ▪ 13% reduction in cycle time as a result of ERP
Followers: Remaining 70% of aggregate performance scorers	<ul style="list-style-type: none"> ▪ 10% reduction in operating costs as a result of ERP ▪ 94% inventory accuracy ▪ 90% complete and on-time shipments ▪ 56 hours cycle time from order to shipment ▪ 7% reduction in cycle time as a result of ERP

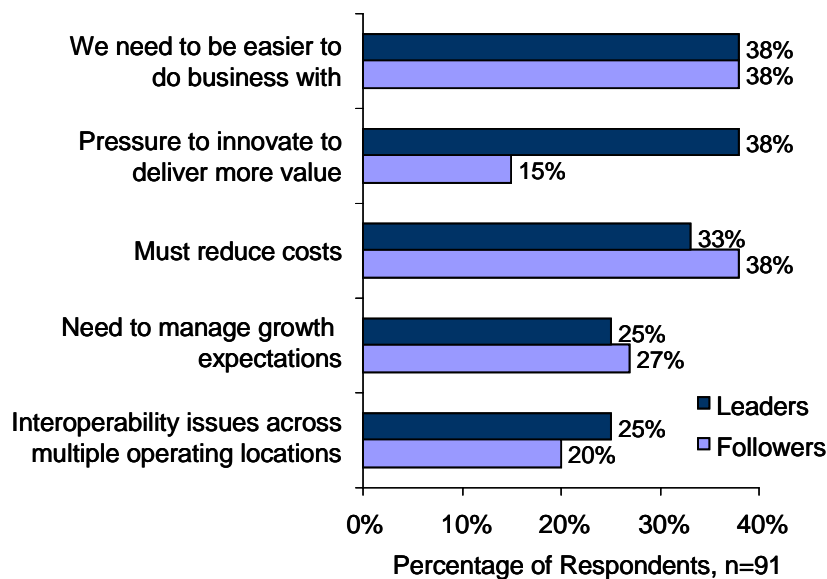
Source: Aberdeen Group, September 2010

These “Leaders” use ERP to standardize business processes, organize for continuous improvement, and provide visibility and exception management.

Business Drivers Impacting ERP Strategies

Before exploring the key differentiators which lead the Leaders to significantly higher return on ERP investment, it is important to understand the business drivers behind the justification of ERP. Figure 2 shows us that Leaders focus on the customer and innovating to add more value, while Followers (although equally driven to improve customer experience) are more focused inwardly on cost reduction. Fueling growth and supporting interoperability across a distributed environment were also found to be significant drivers.

Figure 2: Business Drivers Impacting ERP Strategies



Source: Aberdeen Group, September 2010

In response to these pressures, Leaders see particular value in standardizing business processes, including those in both the front and back office (Figure 3). ERP can provide the framework by which these standard business processes are structured, particularly when templates and best practices are delivered with the ERP solution. By following these suggested templates and work flows, not only are standards established, but the processes are best aligned to the ERP solution. Better fit results in added efficiency. Efficiency can then drive productivity, directly impacting the metrics upon which cost justification was based.

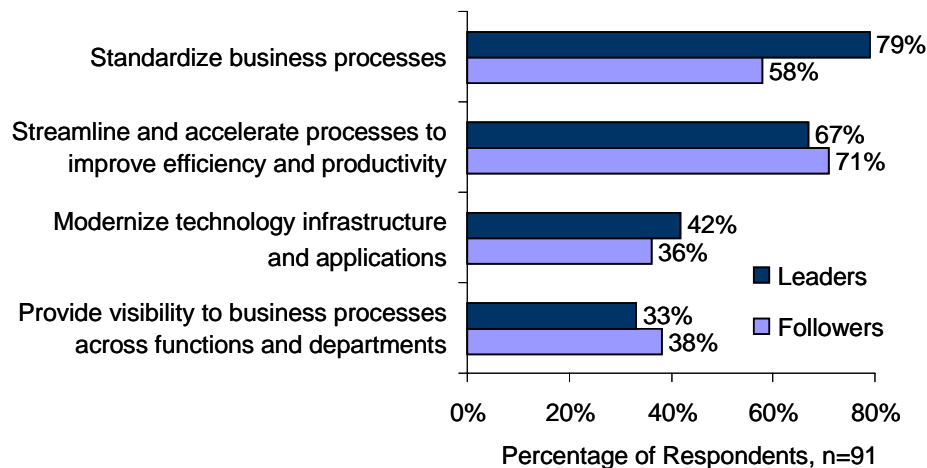
However, modern infrastructures are required to take full advantage of automation. While Leaders are only 17% more likely to identify modernizing technology as a "top two" strategic action, Aberdeen found them 27% more

"It gives us the ability to keep pace with our growing and changing business while reducing business friction."

~ CIO, Mid-Size Distributor

likely to be on the most recent release available from their ERP solution provider. As a result, we can hypothesize there is less need to undergo a technology refresh.

Figure 3: Strategic Actions of Leaders



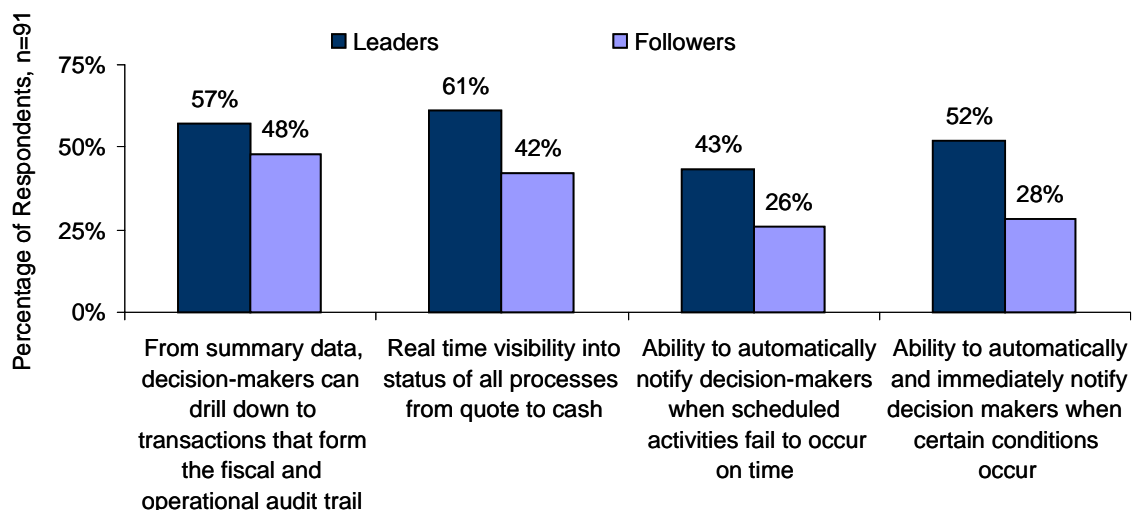
Source: Aberdeen Group, September 2010

Leaders Standardize

- ✓ 78% of Leaders have standardized procedures for order management and delivery / fulfillment the enterprise
- ✓ 70% have standardized enterprise-wide procedures for procurement, cash collection, and financial reconciliation
- ✓ 74% standardize the implementation of ERP across the (possibly distributed) enterprise

And finally, providing added visibility rounds out the top strategies of both Leaders and Followers. This is slightly less of a priority for Leaders, but in fact, Leaders already outpace followers in providing efficient transparency at all levels (Figure 4). Not only do Leaders have 45% better visibility from quote to cash, they are better equipped to manage by exception.

Figure 4: Better Visibility Leads to Better Performance

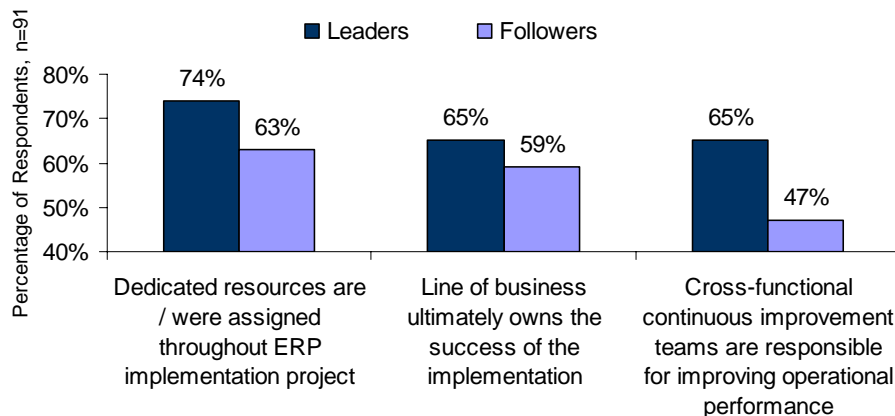


Source: Aberdeen Group, September 2010

Managing by exception allows Leaders to stay at an appropriate level of summarization (supporting efficiency and productivity), only drilling down to the operational and transactional detail when deemed necessary. This deep dive may be triggered by a perceived anomaly at the summary level or by an alert generated either when a scheduled activity fails to occur or when certain conditions are detected. By blending event management capabilities with ERP functionality, something an ERP solution based on a modern technological architecture is likely to provide, managers, executives and other decision makers are better informed and better enabled to take immediate proactive or corrective action.

Given the rapidly changing technology landscape today, keeping current with both functionality and underlying architectures requires focus and commitment organizationally. Executive commitment is a widely recognized prerequisite for a successful ERP implementation. This commitment is evidenced by dedicating the appropriate level of resource to the initial implementation. Often the best people to assign to the implementation team are indeed the best people in the organization and the ones the enterprise can least afford to be taken away from their "day jobs" and their primary responsibilities. Yet it is clear that this level of dedicated resources produces more and better results in the long run (Figure 5).

Figure 5: Organizational Commitment



Source: Aberdeen Group, September 2010

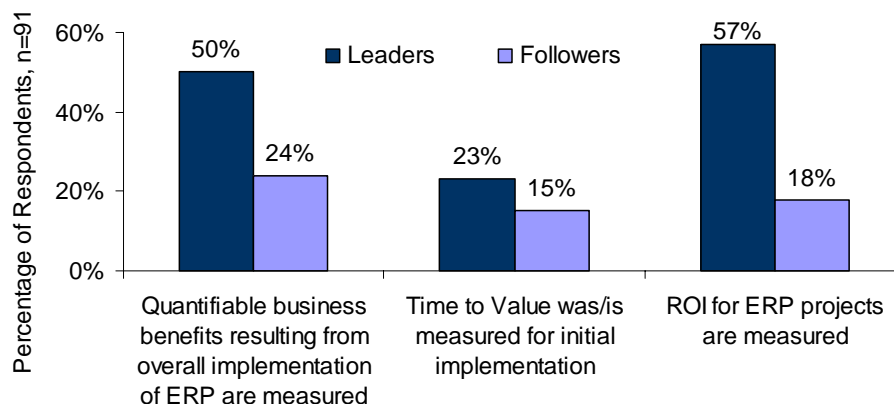
Another important factor is the "ownership" of the success of the implementation. When the Information Technology (IT) department holds the ultimate responsibility, often the success is measured in length of time to implement and the cost of the effort. On the other hand, when the line of business executives responsible for overall operating costs, and customer-facing metrics such as complete and on-time shipments are responsible for the implementation, these metrics are more likely to be used as the measure of ERP success. These are the same metrics that can cost justify the investment in ERP and also prove the value.

This value has no expiration date. Leaders are 38% more likely to have cross-functional continuous improvement teams seeking gains in operational performance. By involving line of business with IT and applying the same concepts to ERP, implementations can be an on-going source of additional cost savings, schedule improvements, efficiency and productivity. By measuring these gains, continued executive support is ensured and the ERP solution continues to produce a return on investment.

Quantifying the Benefits of ERP

Indeed Leaders are more than twice as likely as Followers to measure the benefits of ERP. A growing number of Leaders is also measuring time to value. One important aspect that differentiates Leaders from Followers in this regard is their approach to customization. Leaders estimate their level of customization at 13%, compared to Followers at 24%. At the same time, Leaders are able to perform 57% of the tailoring required without programming, compared to 47% for Followers. These percentage gains all serve to lower the cost of ownership of ERP and drive value more rapidly.

Figure 6: Organizational Commitment



Source: Aberdeen Group, September 2010

In the end though, it is in the measurement of ROI for ERP projects where the Leaders are the most clearly differentiated. Not only are the Leaders 216% more likely to measure ROI, they are 144% better able to quantify benefits from ERP (Table 2). While we saw the primary business drivers impacting the ERP strategies of Leaders are customer focused, top performers are also able to drive costs out of the business and support growth efforts. Those benefits most likely to be quantified by Leaders are those which directly impact operations and costs. While the majority of Followers do acknowledge the same business benefits as our Leaders, they are almost twice as likely to characterize these benefits as "perceived" but are unable to specifically measure monetize the results.

"During the transition there was no downtime. It was a significant upgrade. All reports from employees were positive."

~ Executive, Small Distributor

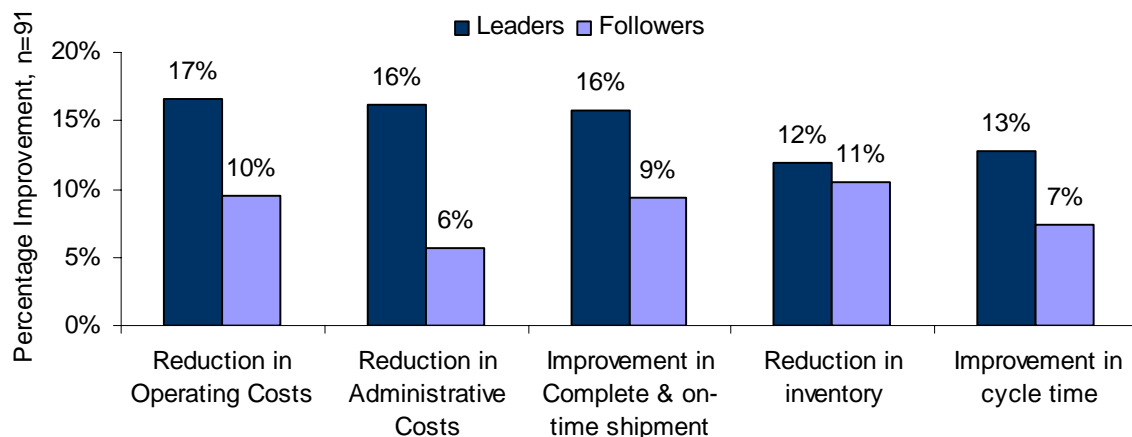
Table 2: Leaders Quantify/Monetize Results

Quantifiable Business Benefit	Leaders	Followers
Reduction in operational costs	67%	18%
Reduction of general administrative costs	54%	15%
Reduction or redeployment of headcount	50%	22%
Reduction in inventory costs	63%	31%
Better utilization of resources	50%	18%
Increased profits	46%	20%
Increased revenue	42%	18%
Increase in value delivered to customers	46%	24%
Reduced Time to Decision	29%	16%
Support growth without additional headcount	58%	20%

Source: Aberdeen Group, September 2010

The difference in actual results is quite dramatic (Figure 7). Not only do we see significant differences in the metrics used to determine "Leader" status, we also see very substantial administrative cost reductions. Given inventory is truly the life blood of a wholesale distributor, it is not surprising to see more modest gains here. Yet, both Leaders and Followers experienced double digit inventory reduction. Indeed, the results even the Followers were able to achieve as a result of implementing ERP lead us to believe that those which have not yet invested in ERP are leaving substantial gains on the table.

Figure 7: Improvements as a Result of ERP Implementation



Source: Aberdeen Group, September 2010

As the economy progresses through its recovery, will those without ERP be poised to take advantage of that recovery? They certainly will not be positioned as well as those already reaping the benefits of ERP implementations.

Required Actions

A well-managed ERP implementation can be a continuing source of efficiency, productivity and operational improvements, resulting in quantifiable cost savings, schedule improvements, reduced cycle times and increased inventory accuracy.

No ERP?

For those who have yet to invest in an ERP solution, ask yourself the following questions:

- Are your costs under control? How much could you improve your business through double digit savings of operational, administrative and inventory costs? Consider the benefits of improved complete and on-time shipment, cycle time reductions and improved inventory accuracy.
- Do you have the necessary visibility into your business to enable you to make clear and confident decisions?
- Are you able to standardize processes across the organization?
- Do internal inefficiencies negatively affect your ability to provide the level of service required to retain existing customers and compete for the business of new customers?

The answers to these questions could provide you with the cost justification to embark on a new journey to implement ERP. In this case, consider the following recommended actions.

- Select an ERP solution with specific expertise in wholesale distribution.
- Establish a baseline of metrics for operating, administrative and inventory costs, along with current customer facing metrics, including percent complete and on-time shipments, cycle times to measure your responsiveness.
- Set goals for the project, including aggressive but achievable timetables
- Align the organization to meet goals and continuously improve
- Most importantly, measure the results

"Our current ERP meets all or most of our business process functions."

~ Manager, Small Distributor

ERP is Implemented: Not A Leader?

For those wholesale distributors with ERP implementations which may not have produced results equivalent to those of our Leaders, the following questions are more suitable:

- Does your ERP implementation have sufficient executive commitment to foster support from both IT and all appropriate

lines of business? If not seek executive level support for dedicated resources, assign ownership to the line of business people that stand to gain most from the implementation and foster a culture of continuous improvement.

- Do you have standard front and back office processes and are they currently well supported by your ERP solution? If not weigh the trade-offs between replacing your ERP with a better fit solution, revamping your implementation with specific goals for improvement, or customizing or tailoring your solution to better meet your needs.
- Regardless of your next step, establish a baseline of metrics for current costs, along with customer facing metrics, including percent complete and on-time shipments, inventory accuracy and cycle times to measure your responsiveness. Set goals for improving
- Most importantly, measure the results

And lastly, Leaders in wholesale distribution must continue to improve. As capital and credit begins to free up and more and more distributors see ERP as a path to competitive advantage, these top performers will be challenged to seek additional benefits from their existing ERP implementations.

For more information on this or other research topics, please visit www.aberdeen.com.

Related Research

[*ERP in SME: Fueling Growth and Profits*](#);
August 2010
[*Think Your Organization Is Too Small for ERP? Think Again*](#); June 2010

[*SaaS ERP: Trends and Observations*](#);
December 2009
[*ERP in the Midmarket 2009*](#); July 2009

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