



# Demystifying the Industrial Distribution Business Model

*Understanding How Distributors Make Money*



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# Ways the Distributor Adds Value

- Break large quantities into smaller lots
- Stock merchandise in convenient locations
- Carry products of many manufacturers
- Finance customer purchases
- Stand behind products and accept returns
- Identify reputable manufacturers
- Redistribute products efficiently
- Provide sales and product training
- Offer design, technical assistance, and service
- Possess local market knowledge
- Provide bids and estimates

*Are these Services only Valuable to the Customer?*

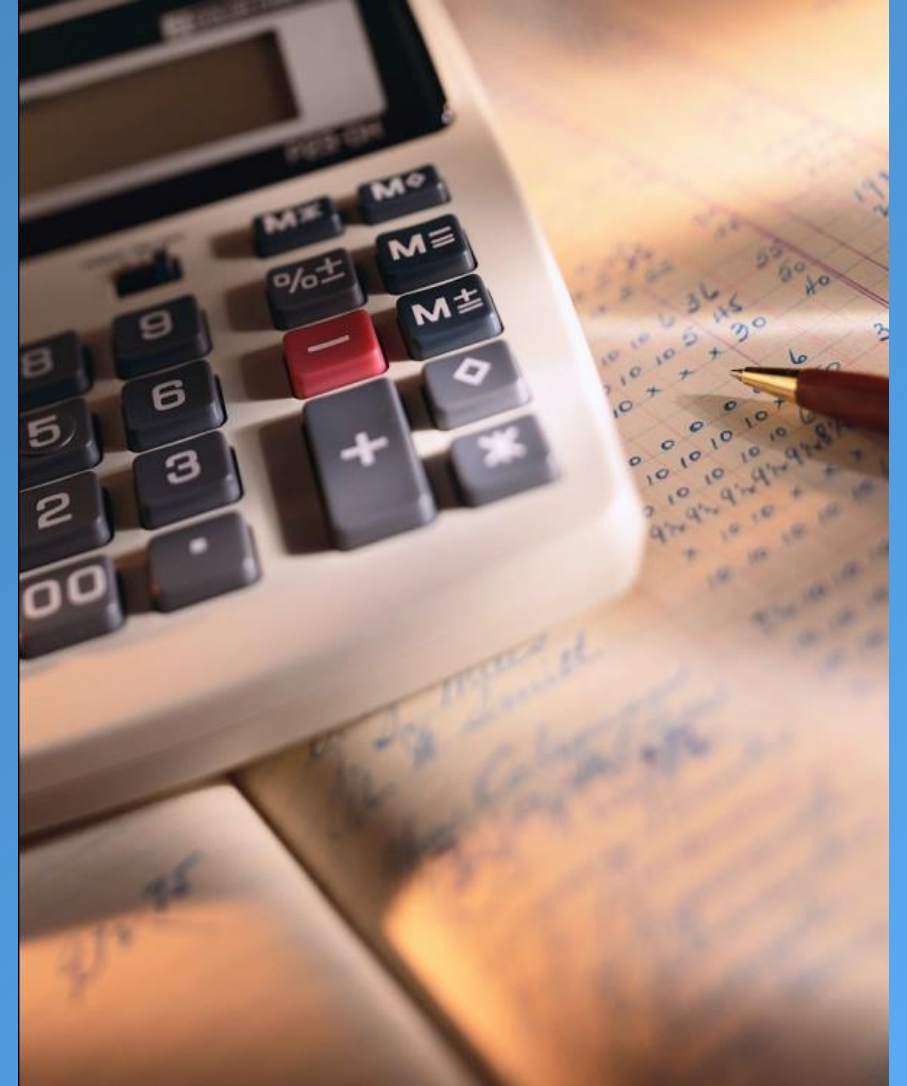


Distributor's Underlying Business Objective  
is:

Generating PROFIT\$

What is our Measuring Stick  
for Profitability?

- The Income Statement
- Also Know As:
  - Profit & Loss Statement
  - P&L





# Driving Net Profit

INCOME STATEMENT / PROFIT & LOSS STATEMENT / P&L		
Income	\$1,000	100%
-		
=		
-		
=		



# Driving Net Profit

INCOME STATEMENT / PROFIT & LOSS STATEMENT / P&L		
Income	\$1,000	100%
- Cost of Goods Sold	-\$744	74.4%
=		
-		
=		



# Driving Net Profit

INCOME STATEMENT / PROFIT & LOSS STATEMENT / P&L		
Income	\$1,000	100%
- Cost of Goods Sold	-\$744	74.4%
= Gross Margin	\$256	25.6%
-		
=		



# Driving Net Profit

INCOME STATEMENT / PROFIT & LOSS STATEMENT / P&L		
Income	\$1,000	100%
- Cost of Goods Sold	-\$744	74.4%
= Gross Margin	\$256	25.6%
- Operating Expenses		
=		



Operating Expenses	All Distributors	Best in Class	Total Revenue		
			Under \$15M	\$15M to \$50M	Over \$50M
Total Payroll Expenses	13.0%	12.4%	13.7%	12.7%	12.7%
Advertising and Marketing Expenses	0.3%	0.4%	0.5%	0.2%	0.2%
Freight Expenses	1.4%	1.6%	1.5%	1.2%	1.5%
Building Repairs and Maintenance	0.2%	0.2%	0.2%	0.2%	0.1%
Rent or Ownership in Real Estate	0.9%	0.9%	0.7%	1.0%	1.0%
Utilities	0.2%	0.2%	0.2%	0.2%	0.2%
Warehouse Expenses	0.3%	0.2%	0.5%	0.2%	0.4%
Insurance Expense	0.6%	0.6%	0.6%	0.7%	0.4%
Auto Expenses	0.5%	0.5%	0.6%	0.5%	0.5%
Telephone	0.2%	0.2%	0.2%	0.2%	0.2%
Depreciation	1.0%	0.6%	1.1%	0.8%	1.1%
Technology Expenses	0.7%	0.6%	0.8%	0.7%	0.6%
All Other Selling, General, & Admin Expenses	2.6%	2.2%	3.0%	2.2%	2.7%
<b>Total Operating Expenses</b>	<b>21.9%</b>	<b>20.5%</b>	<b>23.6%</b>	<b>20.8%</b>	<b>21.7%</b>



# Driving Net Profit

INCOME STATEMENT / PROFIT & LOSS STATEMENT / P&L		
Income	\$1,000	100%
- Cost of Goods Sold	-\$744	74.4%
= Gross Margin	\$256	25.6%
- Operating Expenses	\$219	21.9%
=The Bottom Line		



# Driving Net Profit

INCOME STATEMENT / PROFIT & LOSS STATEMENT / P&L		
Income	\$1,000	100%
- Cost of Goods Sold	-\$744	74.4%
= Gross Margin	\$256	25.6%
- Operating Expenses	\$219	21.9%
= Net Profit Before Taxes	\$37	3.7%

***Less than 4 cents of every sales dollar is profit***



# Cost of Mistakes

What does a \$100 mistake really cost?

$$\frac{\$100}{\text{Net Profit Before Tax\%}}$$

Every time an average distributor makes a **\$100** mistake, they must generate an additional **\$2,700** in sales to pay for it.



# Reducing Mistakes through Setting Expectations

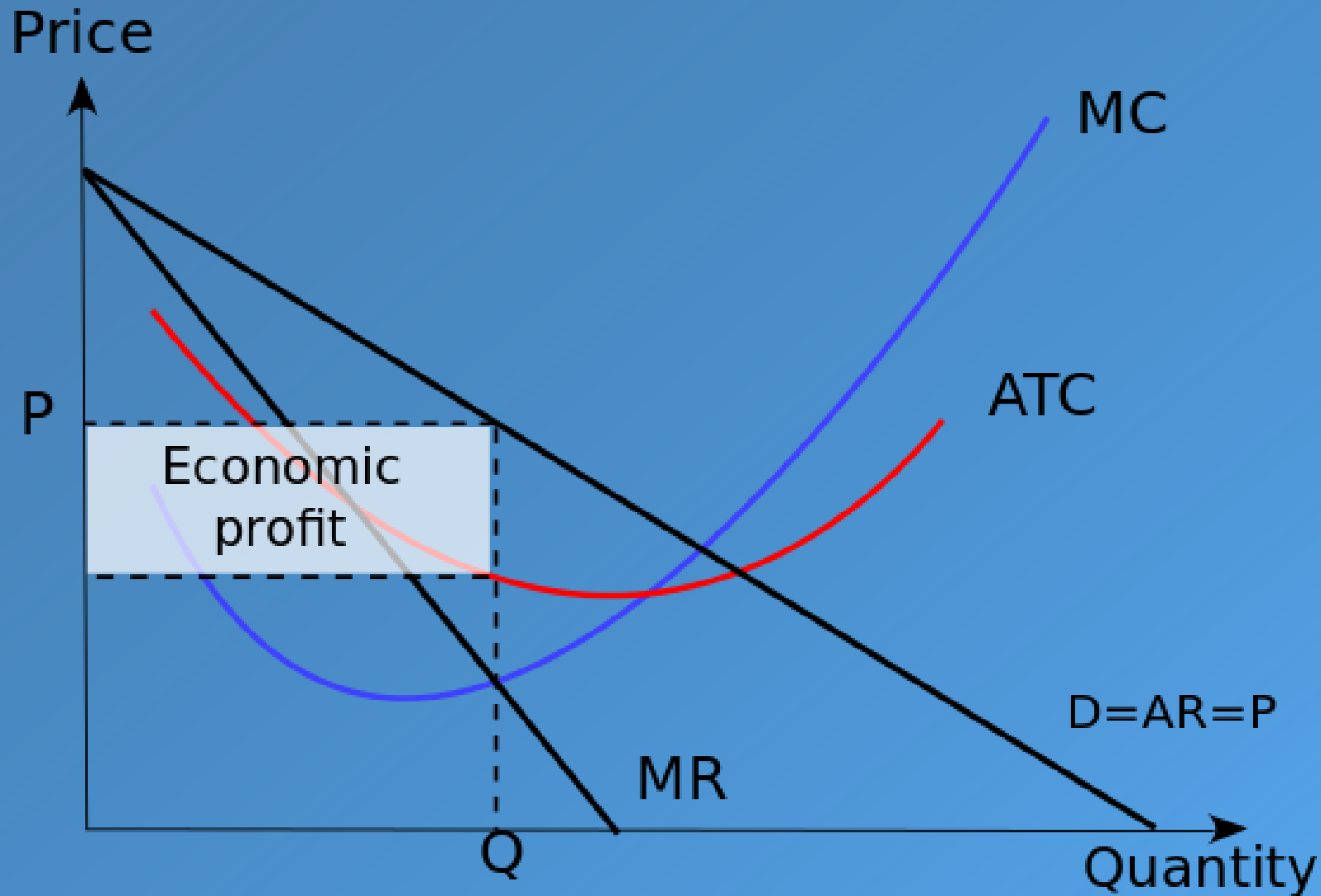
**Is 95% good enough?**

Take order + pick order + pack order + deliver order + send invoice

$$.95 \times .95 \times .95 \times .95 \times .95 = .77$$



# 6 Ways to Increase Profits in Distribution





# 6 Ways to Increase Profits in Distribution

- Sell Higher
- Buy Lower
- Lower Operating Expenses

*Three Cash Driven Ways to Reduce Operating Expenses*

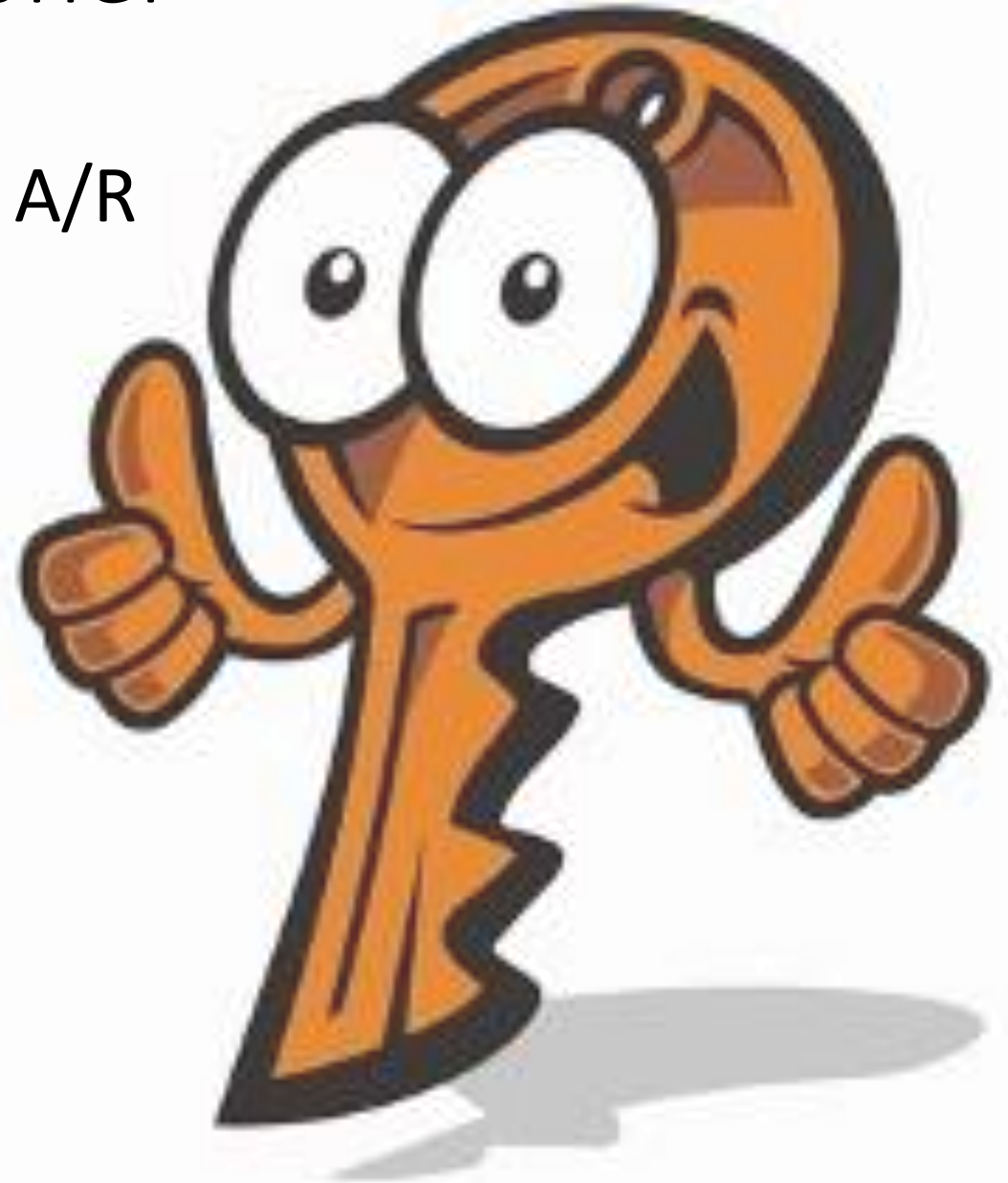
- **Increase Inventory Turns**
- **Collect Sooner**
- **Pay Later**





# Keys to Collecting Sooner

- 3 Primary Costs Associated with A/R
  - Interest Expense
  - Bad Debt
  - Payroll Expense
- Collecting Sooner
  - Reducing Mistakes
  - A/R Automation
  - Interest Charges
  - Cash Discounts





# Profitable Inventory Management





# Changing the Mindset

For a Distributor Inventory is just



in another form.

***The trick is to turn it back to the green stuff!!***



# Keys to Improving Inventory Turns

- 4 Primary Costs of Inventory
  - Facilities
  - Interest Expense
  - Dead Stock
  - Payroll Expense
- Improving Inventory Turns

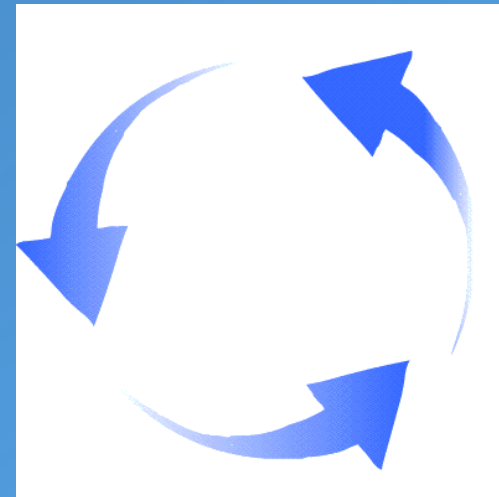




# What is an Inventory Turn

$$\frac{12 \text{ Months Cost of Goods Sold from Stock Sales}}{\text{Average Inventory Value}}$$

- Does not include direct ships
- Does not include special orders
- Should not include transfers





# Keys to Improving Inventory Turns

- 4 Primary Costs of Inventory
  - Facilities
  - Interest Expense
  - Dead Stock
  - Payroll Expense
- Improving Inventory Turns
  - Turn your Purchasing Agent into an Inventory Investor





# An Inventory Investor

- Reduces the hours spent generating purchase orders
- Spends time adjusting system controls
- Studies inventory performance
- Looks for ROI opportunities





# Measuring Inventory Performance

- Inventory Turns
- Customer Service Level

Number of Lines Shipped Complete

Number of Line Items Ordered





# Measuring Inventory Performance

- Inventory Turns
- Customer Service Level
- Gross Margin Return on Inventory (Investment)

Total Margin \$ from Stock Sales for the past 12 months

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Average Inventory Value





# Keys to Improving Inventory Metrics

- 4 Primary Costs of Inventory
  - Facilities
  - Interest Expense
  - Dead Stock
  - Payroll Expense
- Improving Inventory Turns
  - Turn your Purchasing Agent into an Inventory Investor
  - Be Extraordinarily Deliberate in What You Choose to Stock





# Lower Op Exp - *Hunting for Profits*

- Elephant Hunting
  - Much of the big game was eliminated during the Great Recession
  - A lot of it has crept back because of prolonged expansion and supply chain issues
- Cockroach Hunting
  - They are always around





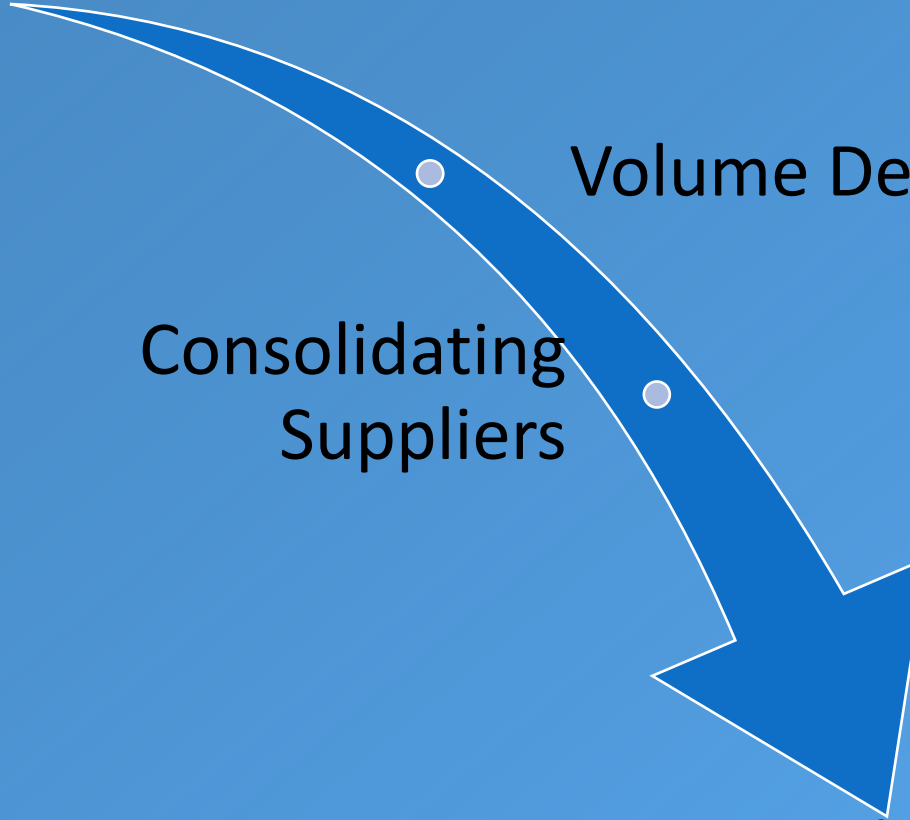
Buy  
Lower

Inventory  
Investor

Volume Deals

Consolidating  
Suppliers

Rebate  
Management





# Sell Higher

## The Hammer or the Scalpel?

- Promote education
- Raise prices across the board
- Adopt a standard cost





# Sell Higher

## The Scalpel?

Adopt sensitivity pricing

Customer Segmentation Based on  
Understanding Your Cost of Processing  
an Order

This Segmentation Creates  
Opportunities for:

Pricing Differentiation

Service Differentiation





# What's Most Important?

- Sell Higher
- Buy Lower
- Lower Operating Expenses
- Improve Inventory Turns
- Collect Sooner





# Finding Marshall

***We want to help distributors!!***

Training / Executive & Next Gen Coaching / Consulting  
Our Monthly E-Newsletter - *Inventory Counts*

*Podcast “Distribution Talk” available at [www.thedistributionteam.com](http://www.thedistributionteam.com)*

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