



RETAINING SHARE IN AMBIGUOUS MARKET CONDITIONS

A playbook for building
products distributors

WHITEPAPER



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I. AMBIGUOUS MARKET CONDITIONS

Few industries are as visibly indicative of the health of the economy as building products/construction. A glance out the window of your office on a random weekday or car during your commute can tell the story – when times are good, cranes scratch the sky, scaffolds drape commercial buildings and Tyvek is a household name. In a down market, you can't hear the trucks backing up and the hard hats are put away; the inactivity is palpable. Everyone in B2B has painful memories of 2007-09, but the avatar of that recession may well be images of doomed projects on abandoned construction sites. As such, it's unavoidable for leaders of building products distribution companies to experience market-induced anxiety as a matter of course.

The U.S. has currently matched its longest period of economic expansion in the post-World War II era. It's been good to be in the building game for the past decade. But what will the next decade hold and how can you be ready if/when the other shoe drops? 2020 looms as the start of a new decade but many analysts fear it will also mark the end of the building boom. Recent indicators point to a slowdown at the very least. The market as a whole has expanded every year since 2010 but growth has decelerated in 2019. Accordingly, building starts have been flattening out. [The Dodge Momentum Index](#) – a measure of planned nonresidential projects – reached its peak in 2017, dropped off sharply in 2018 and has now leveled off this year.

In Europe, the construction market outlook is similarly mixed. According to [Moody's](#), the outlook for the European steel sector for the coming 12 to 18 months is negative. The key drivers of the negative outlook are a combination of weaker macroeconomic conditions and waning consumer confidence, which are undermining demand and could lead to a forecast 2% contraction in steel consumption into 2020.

The global question of the day becomes: are we at the beginning of a downturn, or have we simply stabilized? The mandatory follow-up: how do building products distributors maintain market share if growth continues to slow or in fact recedes? The existential question: what areas of building products distribution are ripe for reimagination, safeguarding against ambiguous market conditions now and in the future?

In this playbook for building products distributors, we will reveal where margins and revenue leak in most B2B distribution companies and provide reimaged strategies for retaining and growing share. First, a quick look at the unique dynamics in building products distribution that typically hinder growth.

II. COMMON PRICING CHALLENGES



Two formidable forces shape the building industry – the market and the weather. It's a project-driven space with intense seasonal variance, making long-term planning a huge challenge. You can't paint a house when it's 10-below zero, no one's pouring concrete in the rain, and an economic downturn puts the brakes on projects big and small. The high degree of seasonality fosters a decentralized, win-at-all-costs environment where reps are given a high level of autonomy to deviate against system pricing. Too often the default attitude is *"Win the bid, figure out the rest later."*

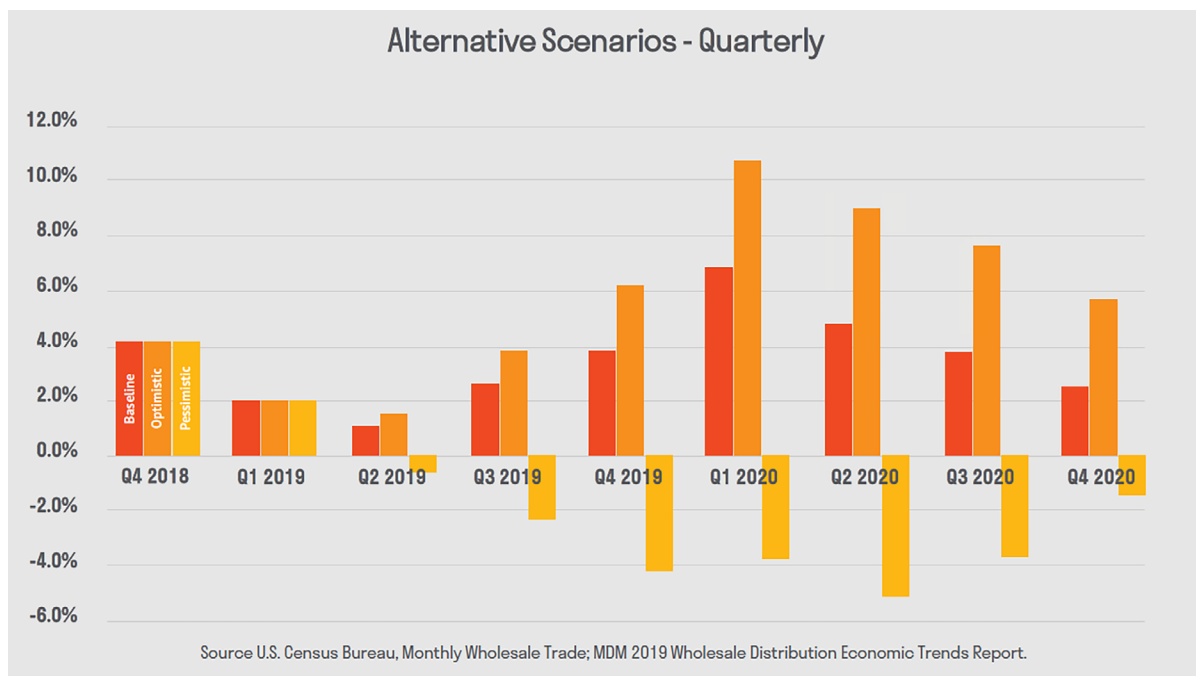
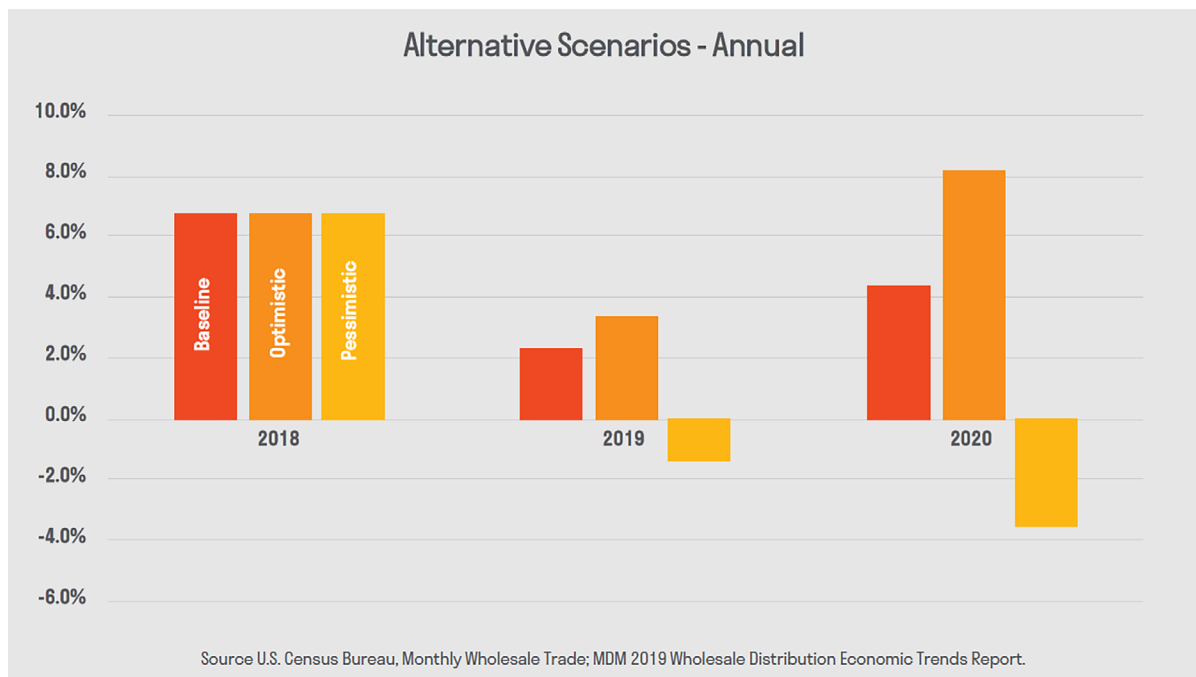
Raw material costs continue to rise, and unpredictably so. Dodge reported a 6.4% increase in material prices in 2018. There was a time in this heavily project-driven industry when supplier cost changes, and all the downstream pricing processes triggered by them, happened once or twice a year. No more. Building products distributors now receive supplier cost changes multiple times per quarter and scramble to keep up. In addition to pricing issues, purchasing is often decentralized, and branch personnel have varying degrees of success when negotiating cost breaks with suppliers.

Both seasonality and rapid cost changes impact the next growth-hindering dynamic: lack of relevant system prices. It is often the case that system prices fail to accurately reflect market prices and are overly general. This leads to only 20 to 30% of a distributor's revenue actually being transacted at the system price level, with the remainder of the revenue occurring at a discounted customer-specific price level or as a one-time deviation or override based on rule-of-thumb discounting behaviors. Furthering the margin leakage, sales reps often lobby to assign nearly all of their customers to the most favorable available price tier or column in the system pricing structure. In other words, every customer gets the best possible system price, regardless of the customer's relationship with the company. This leads to rampant misassignment and additional margin leakage.

Manual pricing methods are insufficient when it comes to accounting for the relevant factors that should drive system price, intelligently assigning customers to the appropriate level or tier, or ensuring that sales reps don't over discount or create unnecessary customer-specific prices.

For example, a sales rep could look at a \$10 price and know it is too high for that particular selling circumstance. He or she may reduce the price for that customer to \$4, not knowing that \$6 would have been an acceptable price for the customer while maintaining an acceptable margin. Typical systems don't make it easy to update these prices later, and as such that customer's price could be \$4 for that item for years, regardless of cost changes, opening wide the opportunity for future margin leakage.

This brings us back to market forecasting. No one can say when the next recession is coming. What will happen in 2020 is anybody's guess – it's an election year in the U.S., trade conflicts are ongoing, uncertainty reigns. A visual representation of this ambiguity is illustrated in Modern Distribution Management's recent Mid-Year Economic Update, which included revenue forecast charts for the distribution industry at large:



That's an incredibly wide swing in the range of anticipated outcomes for 2020. Think about what a 5% drop in revenue would mean for your bottom line or market share. That kind of impact could be coming in Q2 next year. How about a 9% spike in revenue, which represents the optimist's version of Q2? Obviously, the latter would be great, but how do you prepare for divergent realities in any kind of cohesive or coherent way?

III. PLAYS FOR AN UNCERTAIN MARKET ENVIRONMENT



PLAY 1: REIMAGINE PRICING



PLAY 2: REIMAGINE DEAL MANAGEMENT



PLAY 3: REIMAGINE COSTING

Most pricing discussions center on how to maximize margins. While pricing is certainly the biggest lever to improve margins, in a recessionary environment it can also be used to maintain, or even win share, and help distributors balance margin and volume goals. Taking a closer look at how pricing decisions are made in the bid process, how customer-specific price agreements are maintained, and how you can improve margins by focusing on the cost side of the equation as well, may be the keys to weathering the impending market uncertainty.

Consider these plays as you plan for 2020:

Reimagine your price setting process. Take a closer look at how price optimization can produce market relevant prices to drive volume or margin growth, depending on your goal and the market conditions. True price optimization drives the following benefits:

- Optimizes system prices to ensure they accurately reflect the market reality and will be used by the sales team
- Provides override guidance with guardrails to reduce over discounting
- Delivers optimized customer-specific guidance
- Visual analytics to pinpoint and correct where unnecessary price deviations exist
- Passes through cost changes more effectively and granularly across the business

Reimagine deal management with a centralized location for bids and agreements by:

- Providing visibility and means to update customer-specific pricing
- Providing one place for reps to price and managers to price bids to win

Reimagine costing by giving your purchasers predictive guidance on what cost deviations they should be asking suppliers for

Calling these plays – however seemingly complex – is possible. It just requires a reimagining of the legacy methods and systems that have left building products distribution companies in this conundrum. Between years of data and decades of expertise, most companies already have a vast wealth of knowledge within their four walls.

When data science is designed to solve the problems unique to building products distribution, applied to relevant in-house or other data sources, and fine-tuned with the guidance of internal pricing and costing experts, the issues of scale and speed in responding to external forces are mitigated. The technology to achieve this and the streamlined deal management necessary to take control of margin leakage exists today.

IV. CONCLUSION

In conclusion, while ambiguous market conditions are ahead for building products distributors, cutting capital expenditures is not the most advantageous play. Rather, company leaders should look to leverage leading B2B data science approaches to harness the power of their in-house experts and reimagine the speed and scale at which they can respond and adapt to changing market conditions through price.

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