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EXPLOITING DIGITAL DISRUPTION IN THE B2B VALUE CHAIN

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Just as e-commerce and its younger sibling, m-commerce, have transformed B2C retail, the digital revolution now building in the B2B marketplace will permanently alter the way manufacturers and distributors, and their customers, do business. It will leave few participants untouched. Foresighted companies that determine how to exploit the changes under way have an opportunity to establish strong positions in the B2B sales-and-distribution value chain of the future, although doing so may require transforming long-standing practices and business models. Companies that lag in adapting to digital realities will find it hard, and perhaps impossible, to catch up with the leaders—in as soon as a few years' time.

The New Customer Table Stakes

The fundamental dynamics that drive customer decision-making in the B2B and B2C marketplaces are similar. Price, service, and trust are key. B2B customers have learned well from the B2C experience, however, about the impact of digital technology. They are looking to manufacturers and wholesalers to deliver improved speed and convenience, far greater transparency, and much more flexibility of choice. They also understand that they have the ability to choose among multiple shopping channels. B2B customers' expectations are rising. (See Exhibit 1.)

At a minimum, B2B purchasing systems today must be user friendly and offer a high degree of convenience, with features such as prefilled shopping baskets, for example, that are based on a customer's contracts and past record of purchases. Customers are coming to expect near-total information transparency, with respect not only to prices but also to real-time stock availability, order status, and shipment tracking. Customers also increasingly expect a wide range of choice and the ability to shift seamlessly among offline, online, mobile, and personal interactions, filling a shopping basket in the online system, for instance, changing the contents on a smartphone, and placing the final order on the phone for subsequent in-store pickup.

EXHIBIT 1 | The B2C Experience Raises Expectations for B2B E-Commerce

Customers expect B2B e-commerce to match familiar B2C behaviors

Speed and convenience

B2C
- Simple or automated login
- One-click ordering

B2B
- Process optimization tools (for example, facilitated procurement or online IT system links)

Flexibility of choice

B2C
- Disintegration of shopping trips (“cherry-picking”)

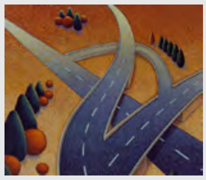
B2B
- Buying across the value chain, adding service where needed
- Disintegrated or optimized baskets

Transparency (preorder and postorder)

B2C
- Price comparison
- Order tracking

B2B
- Price comparison, real-time stock view
- Order tracking

Omnichannel experience



B2C
- Integrated journey across multiple channels

B2B
- Seamless omnichannel usage
- Online catalog systems and expert communities

Sources: IFH Köln Research Experts, *B2B im E-Commerce-Zeitalter—Wohin geht die Reise?* September 2012 (survey of 1,047 B2B online users in Germany, Austria, and Switzerland); Forrester Research, *Thrive by Adopting Proven B2C Principles,* November 2012; Forrester Research, *Key Trends in B2B E-Commerce for 2013*, October 2012; BCG analysis.

These are no longer nifty new features of digital technology; they are fast becoming basic requirements for doing business. Manufacturers and wholesalers need to understand that going digital means reaching new customers and markets and being able to satisfy new ordering behaviors.

The Future Is Taking Shape—Now

Three trends, fueled by digital technology, are turning how customers think about the B2B purchasing process on its head:

- The ability of manufacturers, wholesalers, and new entrants to cross over, or “leapfrog,” traditional value-chain boundaries in sales and distribution.
- Rising demand from customers for seamless cross-channel integration from wholesalers and suppliers alike.
- Acceleration of the ability of both manufacturers and distributors to integrate and automate processes and systems.

Digital technologies enable companies to work more easily across traditional boundaries, often *leapfrogging* entire links in the value chain. The most common example is manufacturers using e-commerce capabilities to bypass wholesalers and distributors by establishing or strengthening direct distribution channels with customers. The risk to traditional wholesalers and distributors is high: in an e-commerce world, customers don’t need a middleman as the matchmaker between supply and demand. Any supplier—anywhere—can make its catalog of goods digitally available to any customer anywhere. Barriers such as geography and national boundaries become less relevant, as do advantages long enjoyed by wholesalers, such as local warehousing. Digital producer-customer matchmaking is easiest for transactions involving commodity products, but even in circumstances involving complex solutions, manufacturers (and others) are increasingly using e-commerce to bypass traditional distribution channels.

One large European manufacturer, for example, has set up the equivalent of an online shopping mall, featuring an interactive catalog of its entire product portfolio (more than 130,000 items). The company offers customers a free Internet-based tool with which they can search the catalog, acquiring information on product specifications and prices (including individual customer discounts); place orders and track orders and shipments; obtain after-sale service and advice, including "webinars" and web-based training modules; and order spare parts or substitutes at any time.

Taking a cue from consumers, B2B customers increasingly look for *cross-channel integration*—the ability to research products, transact business, and interact with suppliers (whether manufacturers or wholesalers), using the channel or channels of their choice: phone, website, mobile app, or branch network. They increasingly expect suppliers to integrate these channels so that they can move seamlessly among them.

Many B2B purchasers today already work across channels. Three-quarters of online sales in Western Europe are preceded by human advice (either in person or on the phone), 41 percent of revenue generated through personal channels is preceded by online research, and about one-third of mobile orders are picked up in a store. Already in 2010, almost $100 billion of B2B purchases in China were researched online before being bought offline. Forward-looking suppliers are offering customers more flexible procurement options and channel-specific value-added services, such as location-based services (for example, the route to, opening times of, and stock availability at the nearest outlet) for customers on the road.

Consider the mobile app offered by a Scandinavian wholesaler that allows customers to search a database of 40,000 products and includes a barcode scanner they can use to obtain product details, pictures, prices, and availability. The app shows the nearest branch, with directions and contact details, and facilitates the ordering of products and the selection of delivery or pickup options. For companies with crews working at remote customer locations, the app also provides a "check-in function" that documents working hours and lets headquarters personnel track the location of individual employees through a GPS-based feature.

Integrating and automating processes and systems can be an effective means of both adding value and making it difficult for customers to change suppliers. Electronically enabled supply-chain processes, including electronic-data-interface capabilities, give customers better control over inventory by, among other things, eliminating excess inventory and stockouts. They can also identify areas for cost reduction. These tools can be major time and money savers for large multisite corporate customers.

For example, a North American distributor of construction and industrial supplies has established an online store with more than 400,000 SKUs that leverages its extensive store network for instant deliveries. It also has installed industrial vending machines at customer locations. The inventory can be tracked online and is refilled automatically.

New Entrants Drive Disruption

While traditional players experiment with digital capabilities, new entrants, unencumbered by legacy business models and relationships, are aggressively seeking to disrupt the B2B marketplace and grab share. These new participants include online marketplaces, metadistributors, online pure players, and third-party configurators. They represent a big threat to distributors and wholesalers, but their rise has major implications for producers as well.

Online marketplaces provide one-stop shops, typically working across categories and industries and offering a wide range of products for multiple third-party vendors. They often enjoy an operating cost advantage, so they can undercut traditional brick-and-mortar wholesalers, reducing switching costs for buyers and making wholesalers exchangeable. They also disrupt producer-customer relationships by offering an alternative procurement channel.

While the B2C market is dominated by a few large marketplaces such as Amazon, eBay, Taobao, and Rakuten, multiple competitors have launched marketplaces or online distributors targeting B2B customers.

One of the most prominent entries in the U.S. is AmazonSupply, which brings Amazon.com's formidable e-commerce and logistics capabilities to the industrial maintenance, repair, and operations (MRO) business. Amazon Marketplace already serves MRO customers with new and used products sold by third parties. In China, Alibaba's Imall and TMall are emerging as B2B trading hubs.

Marketplaces in Asia and Western Europe frequently operate across national borders, breaking down the historical geographic protection of wholesale markets. Marketplaces do have a weakness relative to traditional wholesalers: they typically offer no consultative services to customers—a shortcoming that smart distributors will learn to exploit.

Metadistributors operate like aggregators or meta–search engines in the consumer marketplace, aggregating offers and prices and presenting them to the purchasing public, without taking any product ownership in the process. These are low-cost, commission-based operators, with no need to own distribution or warehouse assets. They increase price transparency—and many wholesale segments historically have had little—allowing buyers to cherry-pick from multiple vendors. Metadistributors put the attractive cross-selling and up-selling margins enjoyed by wholesalers and producers under pressure and threaten the profitability of high-margin, long-tail offerings. Many metadistributors further pressure margins by using a "drop shipping" model, adding the cost of the commission to the sale but leaving the cost of shipping to the producer or wholesalers.

Online pure players attack traditional brick-and-mortar businesses with aggressive online-only economics. With no need to invest in a network of local facilities, they provide a low-cost online shop and look to undercut traditional players' prices. Online pure players have established a base in commodity items and products requiring no sales support or services; they are looking to expand into higher-priced, higher-value inventory.

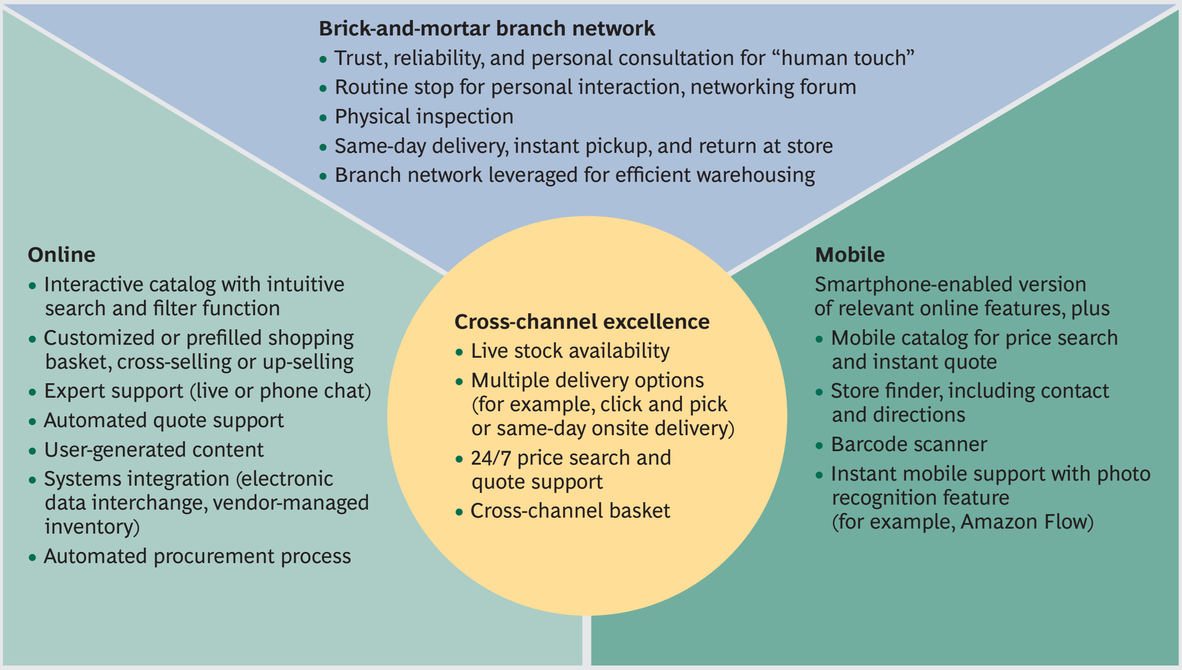
Third-party configurators, another new entrant to the B2B market, aggregate supplier data and ease product selection, helping customers build a basket of products to meet a specific need. Configurators act as independent third parties and can be seen by customers as objective product navigators and selectors. Suppliers and wholesalers risk losing control of the customer relationship and selling process. It is easy to imagine a partnership scenario between a third-party configurator and an online marketplace. The customer specifies a basket of products with the aid of the configurator and then places the order on the marketplace to take advantage of a reverse-auction bidding process.

Indeed, in Europe, online trader Mercateo already operates a multicountry trading platform that enables customers to build a basket of goods—from office supplies and electronics to industrial goods and medical supplies—for which Mercateo then obtains the best price and terms from a multinational network of suppliers and arranges delivery, all through an automated online process. The company actively promotes its ability to provide customers with their "entire business equipping requirements via one trader" and "one platform, one invoice, one contact."

Building a Lead

Many B2B wholesalers—and many manufacturers, too—have established a digital presence. They have built websites with product search and transactional capabilities, they may have a mobile app as well, and they interact with customers to varying degrees across channels, transacting some portion of their business electronically. But at heart, they are brick-and-mortar businesses toying with new technologies. They need to transform themselves into omnichannel distributors that operate with equal comfort and ease in the online, mobile, and brick-and-mortar worlds. (See Exhibit 2.) They also need to take stock of their own advantages—relationships, expertise, and service being key among them—and determine how to employ them in a digitally driven world.

Exhibit 2 | Cross-Channel Excellence Adds Value Along Multiple Dimensions



Source: BCG analysis.

To get ahead of the trends and new players that are reshaping the B2B market, wholesalers and manufacturers need to:

- Develop strategies to pursue or combat leapfrogging, be it from an "offensive" position as a supplier or as a wholesaler needing to defend its turf.
- Invest in the highest-quality product data and support (particularly manufacturers) or risk losing share to competitors with better data and services.
- Evaluate their own potential to sell through online marketplaces and cooperate with metadistributors.
- Unbundle product and service offerings to respond to more specific customer requests.
- Develop a clear strategy to control configurators and protect the customer interface.

In addition, wholesalers, which face a greater risk of disintermediation, should take the following steps:

- Promote their ability to provide service and consultation at a level that manufacturers and new entrants cannot offer.
- Meet expanding customer online expectations by adding digital capabilities under their existing brand while reaching new customers with an e-commerce pure-play operation launched under a new brand.
- Optimize automation processes to add value to customers and retain (and gain new sources of) recurring cash flows.
- Promote value-added services, such as logistics services, face-to-face and consultative selling, and warranty claims handling, which online pure players do not offer.
- Invest in their own online capabilities.

Change comes quickly in the online world, and leaders can suddenly pull far ahead—as a long list of defunct companies in already disrupted industries have discovered. Companies that move quickly to assess the changes under way and adjust their business models to meet shifting market dynamics and customer demands can establish significant leads over both traditional competitors and new entrants. There are plenty of examples to learn from. The retail sector in the U.K. and the U.S. banking industry, to cite two, are both full of traditional players that provide—profitably—advanced levels of customer satisfaction through digital commerce. For thousands of suppliers in China, the e-commerce platforms of Alibaba are the primary means of marketing their products and services, and interacting with customers.

Digital disruption also affects a full range of commercial functions, from sourcing to sales and from marketing to HR. Winners in the B2B e-commerce market that is already taking shape will begin the process of transformation now.

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