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Amazon causes angst in the aftermarket parts industry

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CNBC recently noted the 20th anniversary of Amazon going public. Had we invested $10,000 in the company's initial public offering, we would enjoy a holding worth more than $5 million today.

On this anniversary, Amazon has twice the market cap of Walmart and represents more than 1 percent of retail sales in the U.S. It is just finding its footing worldwide, and is ominously eyeballing "specialty" distribution (read vehicle aftermarket distribution). In the automotive aftermarket, only O'Reilly Automotive has a stock record close to Amazon.

Amazon must have loved recently announcing that major traditional aftermarket suppliers have agreed to support their new push. Manufacturers and distributors-to-retailers/jobber/service shops resisted selling Amazon direct for fear of channel retaliation. Now that almost all items are available through Amazon Marketplace, direct selling of most popular SKUs to Amazon is snowballing.

Distribution guru Bruce Merrifield has been looking closely at the amazing customer delight machine that Amazon is building and its effects on traditional industrial distribution. We present here our estimates of the Amazon effect on vehicle parts channels.

Amazon, eBay or Alibaba have not missed noticing the multi-billion dollar parts opportunities. With vehicle parts sales through electronic channels reaching $7.5 billion last year, why have legacy channel players (fancy description of traditional distributors) continuously under-rated the Amazon effect for 20 years?

Why didn't we (as an industry) better assess the Amazon threat? Here are some thoughts about that:

• **Consistent under-estimation by channel experts.** One favorite example is Barnes & Noble, which unveiled a website in 1999 that was supposed to crush Amazon. Fast forward to April 27, 2017 and Barnes and Noble announced its fourth CEO in four years. With 645 stores down 9 percent for 2016, we wish him well. Barron's is targeting Amazon shares to hit $1,100 (up 20 percent) in one year.

• **Narrow-frame expert forecasting.** Aftermarket experts (immersed in their studious, unchallenged but comfortable past) extrapolate forward in linear, incremental fashion. They have consistently celebrated, for example, the details of Grainger's 90-year, highly evolved "moats" that Amazon can't imitate yet. But yesterday is rarely tomorrow.

• **Amazon isn't imitating any factory-out, push-product-to-market channel.** They are inventing an entirely new, customer-centric channel that starts with ordering online. Then, they invent whatever is needed backwards to factory sources in China. Amazon bought cargo jets and semi-trailers, for example, to have better, cheaper delivery at peak times and not to compete with FedEx and UPS.

• **Amazon's 500 customer-centric metrics guide their non-stop innovation to create value for digital buyers.** In two years, imagine your 5G bandwidth phone will have merged with the evolving Alexa/Echo business app to instantly retrieve all product information needs, including price and delivery-speed shopping comparisons, while Amazon achieves breakthroughs for 30-minute delivery and cost. A future dream – driverless vehicles to ZIP codes to release drones for last-block delivery.

What's in your customer-centric, value-innovation pipeline? In 2019, more than 50 percent (and climbing) of all purchasing will be by millennials who see traditional reps in their traditional roles as a time waster. Are you reinventing sales force cost/benefit per call proposition?

The good news (kind of) is that Amazon just wants your zero-attention-needing, digital customers/orders. You can keep the unprofitable, high-service-cost, small-order customers.

Your best, most profitable customers want you to match Amazon's web shopping/ordering experience, range of delivery options and prices. How will you keep the 5 percent of your most net-profitable customers and get even more of their total spend?

It's all about Prime time

Amazon Prime customers are typically richer, bigger-buyers, younger, busier, more ambitious and digitally savvy. Does this sound familiar? They know what they want to buy.

Primes are zero-service-cost types. As 24/7 buyers, they see outside and inside reps as a 9-to-5 Monday-to-Friday inconvenience who slow down ordering. For them, traditional distributors' 'service edge' is an un-needed overhead cost. Amazon gives them what they want and the overhead savings in lower prices on commodity staples. Unfortunately, 50 percent of any distributors' smallest, neediest customers stay loyal as net-profit losers.

Note: We have covered ad nauseam how aftermarket distributors can lose 5 percent of its sales from lowest-cost customers on most profitable SKUs and see profits drop by 50 percent. We need honest, new lenses to assess Amazon BIZ's forward innovation effects.

Are parts distributors somehow insulated?

In January 2017 Amazon signed more direct-buy agreements with aftermarket auto parts makers. The Big Four auto parts retailers' stock prices took a hit (Genuine Parts, O'Reilly, AutoZone, Advance Auto Parts). But April stock analyst reports claimed, *"Fears Overblown…. Amazon can't Dent the Big 4s' Moats…. Stocks a Bargain."*

Analysts detailed the powerful supply chain barriers the Big Four have created: Professional mechanics need local, technical advice; high fill-rates; quick deliveries and pick-ups; and easy returns of wrong orders and rebuildable cores. Amazon's better prices aren't enough to win, they said.

Here's why we are calling out these analysts' reports

• Amazon's parts sales for 2016? We found estimates of $3 to 4 billion in sales going to $5 to 6 in 2017 due to January's expansion moves.

• The trend for factories selling Amazon direct is increasingly up (but not well publicized).

• Comparable delivery response time and prices. Amazon has same-day delivery in 40 cities at an average price below the Big 4 of 23 percent. There was no mention of Amazon's 30-minute delivery experiments.

• Customer segment sizes were expressed only in terms of sales. What about the net profitability of the customers who self-select to buy from Amazon who don't need services? The top unmentioned assumption was that Amazon is currently doing what they will still be doing in 2019. That is simply not true.

Some ideas on making your plan

• Be true to your infrastructure and most (historically) profitable customers. Don't try to sell stuff online to the world. Amazon's infrastructure wins. Ask your most profitable customers in your most profitable niches how you can digitally enhance their total buying needs. Then, do it.

• Measure and fix the profit cross-subsidies among your customers and SKUs before Amazon steals your cream customers' purchases on cream SKUs.

• Get line-item, profitability analytics to know and stop the cross-subsidies among customers and SKUs.

• Innovate value for your winners. And stop offering free services to the excessively, unprofitable customers. Think minimum orders, unbundled delivery and restocking fees.

• Finally, don't try to imitate Amazon (like Walmart has so pathetically done). Innovate value for your profit-core customers utilizing specific, localized insights. This is still a relationship business – but not for the old "donut patrol." Don't make one more sales call where you don't bring new supply-chain compression, customer centric ideas.

If you think "my suppliers (or salespeople) won't enthusiastically support a customer-centric innovation idea" – then you cannot possibly be customer-centric. Customer-centricity will reward both suppliers and the best reps who can and are thinking value reinvention.

Editor's note: To get master cloud service Line-Item, Profit Analytics from ***WayPoint Analytics****, contact them for a tutorial at bill.wade@wade-partners.com , bruce@merrifield.com or Randy MacLean, rmaclean@waypointanalytics.com.*
