The Amazon Effect & Your B2B Supply Chain

A summary of how you can adapt and thrive

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It is important to understand Amazon's effect on your supply chain, your operations and your customers, and more importantly how you can adapt and thrive.

The Amazon Effect

Amazon earns 37% of all ecommerce sales in the USA. What is even more incredible is their ecommerce market share is growing, and ecommerce is a fast growing market. In 2016, Amazon was responsible for 53% of all ecommerce growth. This is all remarkable… or frightening. However, what is getting our attention (and should get yours) is Amazon's inevitable march into industrial product distribution. Most Supply Velocity Clients are involved in industrial markets. Before 2016 Amazon was a consumer business. Not any more. Their incredible distribution footprint is quickly being used to serve industrial markets.

Increasing complexity of supply chains

Ecommerce in general has created changes to how companies process products. What used to move in pallet quantities is moving in single unit parcel boxes. Customers that used to accept 7 days leadtime demand products in 2 hours. What used to be returned at below 10% rate to stores is now being returned at almost a 30% rate, which requires handling by special processing centers. Supply chains are getting more complicated; customers and consumers are requiring, and getting used to better performance.

Manufacturers are becoming distributors

For manufacturers, the world is changing. In the past, lean manufacturers with less than 2 week leadtimes could produce-to-order. Now even industrial customers are requiring 2 day leadtimes on commonly purchased items. The result is manufacturing companies are having to build warehouses and become distributors, with efficient pick-pack-ship operations of pallet quantities, mixed pallets and single unit parcels. If you think you can be a manufacturer, focused on production, with an inefficient warehousing operation, it is time to think again and realize you are actually a distributor with a dedicated supplier (your manufacturing operations).

Distributors are becoming retailers

The bad news for distributors is they will find themselves competing with Amazon… a company that is great at supply chain management and uses advanced mathematics and software to minimize costs and can succeed earning razor-thin margins. The good news is Amazon is forcing distributors to become online retailers, selling via their web site or opening stores on Amazon and being part of Amazon's marketing machine. If you are not augmenting your wholesale business with direct-to-consumer retail business, you risk being cut out of the supply chain in the future. You must develop a relationship with the customer, whether it is a repair-person, a construction firm or property manager.

Online store – link to Amazon's platform (Marketplace)
If you can't beat them (and no one seems able to beat Amazon) then join them. Putting a store up on Amazon allows you to participate in their marketing efforts. You can do this while building your own online store which can be promoted in parallel to your sales through the Amazon marketplace. The key is to start selling online as soon as possible, even if it means giving a portion of the profit to a company that is competing with you for sales. Note, make sure you do the fulfillment to make sure Amazon does not gain power over your pricing.

Competitors sharing assets
If you have been fighting it out with your competitors, it is time to evaluate them as potential collaborators. If you and a competitor can jointly reduce costs and create (legal) barriers to Amazon entering your market, do it. This can be transportation assets, joint-warehousing or even sharing manufacturing.

Inventory management / optimization
Few companies think of their inventory as a strategic weapon. It is a cost they try to minimize. Amazon uses advanced algorithms to set inventory levels, making sure they have inventory near customers who need it, while maximizing profit. You must be smarter and truly optimize your inventory. The days of having "6 weeks on hand" are over. You must calculate safety stock based on service levels, reorder based on target inventory levels and reorder quantities that balance service to customers and investment in inventory.

Inventory / network optimization to minimize delivery time and cost
Amazon has an impossible-to-duplicate warehouse footprint. They are creating a distribution network where every item can be close to every consumer. However, you can still optimize your network. Every item in every location is probably not optimal. You should use your service strategy, and A/B/C/D/F SKU classification to drive your decisions of what item is stocked in which location, at the optimal inventory level. Doing this will balance minimizing costs and maximizing service to customers. You cannot satisfy every customer with every SKU but you can maximize profits and the tradeoff of customer service versus inventory investment.

Be Amazon's supplier
You would think that Amazon, with their incredible purchasing volume, would be buying only from manufacturers. However, in many (for Amazon) smaller product categories it is more cost effective to buy from distributors. Many manufacturing companies are not set up, and therefore will not do the packaging/labeling required by Amazon. (Part of Amazon's very efficient warehouse operations is their receiving processes, which require specialized packaging and labeling by their suppliers.) Therefore, you can and

should actively seek to become a supplier to Amazon and be part of their supply chain. They are not loyal, but it is better to participate in their supply chain then see your customers go to Amazon with no benefit.

Operational flexibility

Even as a smaller company, you can be Amazon's supplier because they require specific packaging and labeling on all shipments inbound to their distribution centers. Large companies are not set up for these special requirements. This allows smaller and midsize companies to fill a gap and participate in Amazon's supply chain. However, some of the productivity-improving automation that Amazon uses so successfully (I mean robots) can actually be problematic because automation is not flexible. You need to be able to quickly change your processes, build new processes, relay-out your warehouse or production operations based on changing product mix and Amazon's requirements. The key to being part of the Amazon supply chain is flexibility, then low-cost. We have Clients whose warehouses may look like the 1980s (when scan guns first came out) but they are flexible and will quickly make changes required by customers.

Omnichannel

While much of our discussion is focused on distributors and manufacturers we must consider how retailers can adapt and thrive in the Amazon era. There are strategies around customer service and having a product that brings your customer into your shop. For example, in the hockey retail business, players will go to the store to get their skates sharpened. From a product fulfillment perspective retailers must embrace omnichannel, which is a set of processes to ensure a seamless buying experience that moves between the physical world (stores) and virtual world (web site, mobile). This includes buying online and shipping from the store, buying online and picking-up in the store, buying in-store and shipping from warehouses, buying online and returning to stores and traditional e-commerce (buying online and shipping from warehouses). In addition, you cannot forget a warehouse's traditional function of supplying product to replenish store inventory.

Demand forecasting

If you have inventory you have been forecasting. Many companies forget this simple truth and believe they are not forecasting when they use the average weekly demand of the last 3 months. Some manufacturing companies using kanban believe forecasting is a push system (the opposite of what they are trying to achieve, pull) but they forget the kanban bin quantity is based on a forecasted demand. Many distributors try to keep "weeks-on-hand" not thinking about what week they are talking about (hint, it should be future weeks!). Here is the reality, if you have inventory you are forecasting, and therefore you should do it as accurately as possible. Because there is no such thing as a 100% accurate forecast, at Supply Velocity we instead seek to minimize forecast error. This requires the use of multiple forecast algorithms. The most advanced, which are used by our sister company, Optimal Velocity, include exponential smoothing, regression and machine learning to predict future demand. If you are forecasting… be great at it.