

# UNLOCKING HIDDEN PROFITS

SECRETS TO GENERATING NEW DEMAND



“WHEN YOU DISCOVER A  
PROBLEM, YOU DISCOVER  
A BUSINESS.”

– HENK KWAKMAN, FORMER CEO OF NESPRESSO

# WHERE WILL SIGNIFICANT, SUSTAINABLE NEW GROWTH COME FROM?

In today's competitive market, most companies are struggling to drive profitable growth in their core customer base. Generating and harnessing demand for new propositions is critical to driving breakaway performance in this environment.

Driving profitable growth is tough. Once you strip out growth from price increases, mergers and acquisitions, and international expansion to look at a business's "core growth", you often find that this growth has been sluggish or even negative over recent years (see Exhibit 1).

This is not simply a result of the Great Recession, although this has clearly hit some sectors hard. In fact, it has been an issue for many businesses since the end of the 1990s, not just wholesalers and distributors. We regularly talk to CEOs struggling to hold on to their core customer base, let alone profitably grow them.

Yet, despite this weak background, some businesses have managed to generate outstanding growth of 6–10 times that of their market. They have done this by innovating: new propositions, new services and game-changing products that have found pools of untapped customer demand. This paper looks at the five key lessons to be learned from these "demand creators" and how they are being applied today by the more innovative distribution companies<sup>1</sup>.

1. **Customer and supplier hassles are the source of untapped demand**
2. **New propositions need a team, processes, and the right culture to incubate**
3. **Don't stop innovating and iterating until it's magnetic**
4. **Identify techniques to get around the inevitable customer inertia**
5. **Don't launch before you are ready – then scale, fast**

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## Exhibit 1: Demonstration of sluggish core growth in many distribution and wholesale sectors

Our analysis found that, after stripping away growth from acquisitions and international expansion, core growth has been meager at best

DISTRIBUTION SECTOR <sup>1</sup>	2008–2013	INTERNATIONAL GROWTH <sup>2</sup>	ACQUISITIONS <sup>3</sup>	PRICE INCREASES <sup>4</sup>	ESTIMATED CORE GROWTH				
Electronics	9.4%	–	1.8%	–	3.9%	+	0.0%	=	3.7%
Food	6.0%	–	0.4%	–	1.2%	–	0.4%	=	4.0%
Building materials	5.3%	–	1.5%	–	0.9%	–	0.9%	=	1.9%
Pharmaceuticals	3.1%	–	0.2%	–	0.3%	–	1.2%	=	1.4%
Industrial chemicals	2.0%	–	2.5%	+	1.0%	–	3.0%	=	-2.3%
Industrial parts	2.0%	–	2.2%	–	0.4%	–	0.2%	=	-0.8%
Electricals	0.2%	–	1.4%	–	0.9%	–	0.7%	=	-2.8%
					<b>Average = 0.8%</b>				

Source: Company 10-Ks, annual reports, and US Bureau of Labor Statistics

1. Each sector is comprised of three leading publicly listed multibillion-dollar distribution companies, primarily based in the US
  2. Growth from base international revenues in 2008, along with international acquisitions
  3. Net change in revenue caused by domestic acquisitions and disposals
  4. Estimated from the change in Producer Price Index for the associated industry
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<sup>1</sup> Several of the lessons and examples are drawn from research published by Oliver Wyman in *Demand: Creating what people love before they know they want it* by Adrian Slywotzky and Karl Weber

## Lesson 1

# CUSTOMER AND SUPPLIER HASSLES ARE THE SOURCE OF UNTAPPED DEMAND

Exhibit 2: Procedure packs – sterile, sealed packages containing all single-use equipment for a specific operation



Multiple surgical items need to be gathered, sterilized, and disposed of

To



A pre-sterilized, single-use procedure pack solves hassles in the operating theatre

Managerial attention is first and foremost on the products and services you deliver today. To generate breakthrough demand, companies need to spot unmet client needs before competitors. This is easier said than done. It requires you to look beyond your current business into the wider “business system” in which your products are sold and look for hassles that you could solve for your customers, or suppliers.

Take surgical equipment distribution as an example. In the past, surgical teams sourced protective equipment, gowns, and surgical instruments from multiple manufacturers, sterilized them, and brought these different parts together for each operation. Distributors focused on getting the right range of equipment at the lowest price, delivered on time when the customer ordered them. Yet, this left the surgical team with some significant hassles:

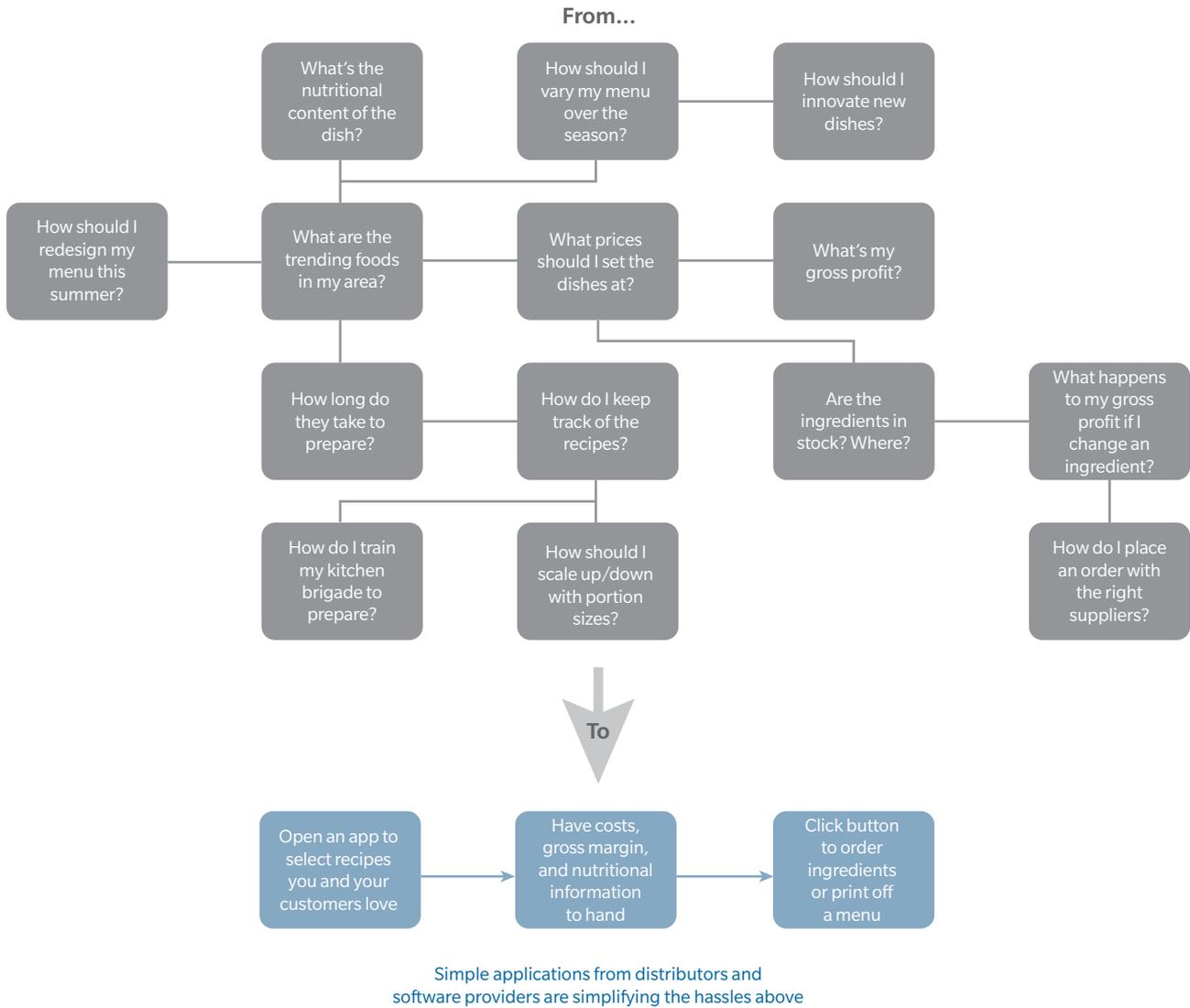
- Missing protective wear or tools for the operation
- Incorrect instruments
- Incomplete sanitization of instruments before use
- Accounting for individual surgeon brand preferences
- Post-operation disposal and recycling

Each of these issues could increase operation set-up times, increase risk of infection to the patient, add to costs in the hospital, or even jeopardize patient safety.

These hassles, however, also presented a major opportunity. Innovative equipment suppliers have become “value added distributors” by providing custom procedure trays (see Exhibit 2). These trays contain in one pre-sealed pack all the single-use medical devices needed for a specific procedure. The value proposition to the hospital is clear: shorter set-up times, less unused equipment, less packaging waste, and reduced costs. For the distributor, the trays offer a significantly higher margin than selling the constituent products, and a broader product range than before.

This lesson applies equally to your suppliers who may also experience hassles that reduce their margin or increase their risk. **Mapping hassles systematically using a “hassle map” (see Exhibit 3), can often be the first and richest source of ideas to identify next-generation demand.**

Exhibit 3: A hassle map for chefs planning their menus



## Lesson 2

# NEW PROPOSITIONS NEED A TEAM, PROCESSES, AND THE RIGHT CULTURE TO INCUBATE

Exhibit 4: Contrasting efforts seen by Oliver Wyman by businesses keen to generate the next \$1BN in sales

GOAL: \$1BN+ IN NEW REVENUE	INVESTMENT
 New product R&D	<ul style="list-style-type: none"> <li>Dedicated brand or product development team</li> <li>\$300MM on each new product</li> <li>System to track and ensure success</li> </ul>
 New car platform	<ul style="list-style-type: none"> <li>1,000+ specialized employees and best suppliers</li> <li>\$500MM of investment</li> <li>Gated process with senior executive review focused on fine-tuning, not pass/fail</li> </ul>
 Entrepreneurial start-up	<ul style="list-style-type: none"> <li>10–30 people</li> <li>100-hour work weeks</li> <li>The best talent</li> <li>\$MM of venture capital investment</li> </ul>
 Growth initiative	<ul style="list-style-type: none"> <li>10s of staff, often B-players</li> <li>Minimal investment</li> <li>Presumption of failure, mindset is to “poke holes”</li> </ul>

Demand innovation is as challenging as new product innovation and requires the right level of resourcing: consider the contrast between efforts we have seen in one business to generate the next \$1BN, shown in Exhibit 4.

Too often companies default into the “growth initiative” mode, unwilling to free up their best teams to work on new propositions. New propositions are also often threatening to the core business itself and risk being killed-off by managers.

The best demand innovators address these issues head on. Take Amazon’s creation of the Kindle as an example. Amazon realised that, if the Kindle team were based in Seattle sitting next to the teams selling traditional media, the Kindle would be seen as too big a threat to the core business and quietly killed. In addition, Silicon Valley was home to the resources required to move away from logistics and distribution and towards becoming a great device manufacturer. For these reasons, Amazon’s Lab126 was set up near to Apple’s headquarters in California as an entrepreneurial start-up, with Amazon providing the investment dollars.

Or take Nalco, originally a chemicals business focused on water treatment and hygiene, which branched out from chemical sales to technical services. Nalco developed a technical solution that both monitored water quality and added the appropriate amount of Nalco’s chemicals. The benefits to the customer were less downtime of their plants and less chemical use. While this service was clearly valuable to customers it posed a threat to Nalco’s core chemical revenue streams. So the company decided to incubate this new service in a completely separate team and developed specialist sales forces. The result: a unique service built up over 20 years and counting, with overall sales linked to customers using the solution being 2–3 times more profitable than what had been sold before.

**Thinking now to your business, once you have identified the customer hassles behind next-generation demand, consider the structure of your innovation team:**

- **Is it well-resourced with your best talent?**
- **Do they have a clear stage-gate process for assessing and accelerating/prioritizing/dropping innovation concepts?**
- **Are they appropriately incentivised for success?**
- **Are you really willing to provide sufficient investment for it to launch, improve, and scale its offers?**

## Lesson 3

# DON'T STOP INNOVATING AND ITERATING UNTIL IT'S MAGNETIC

The list of functionally useful but fundamentally unsuccessful new propositions is long. Propositions that appear to be great on paper fall at the first hurdle and don't get the expected customer traction. At this stage, managers often conclude that to invest further would be to pour "good money after bad" and decide to call time.

**Truly innovative new propositions require extreme patience, careful risk management, and a combination of emotional customer appeal as well as functional excellence. There is no substitute for testing prototype propositions with customers, be it with panels or through friendly relationships (see Exhibit 5).**

Take a client of ours in the electronics manufacturing and sales industry. It is recognised as a leader in innovation, spending over \$300MM a year in R&D with highly qualified PhD-caliber employees. It created a new product, whose functionality was far superior to anything else on the market. This product was patented and the manufacturing process was secret. Yet early versions of the product achieved no traction in the end-market installers and end users.

Further investigation identified that the product's functional requirements were only a small part of a broader proposition needed to make the offer magnetic. For example, customers were uncertain about whether the new product was future proof, how it worked with other products in our client's system, and its interoperability with solutions from leading manufacturers such as Cisco.

We found that our client was able to create a package that became the market standard, containing:

- Branded, interoperable products
- Future-proofing guarantees
- Endorsement from other leading vendors

This system has generated an estimated \$500MM in market value for the business since its launch.

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### Exhibit 5: Proven customer research techniques to make your offer magnetic



#### Customer feedback sessions feature product story boards and solicit input from would-be buyers

Storyboards contain realistic mock-ups of what the offers might look like, feel like, and include. Customer feedback is gathered from there



#### In-market testing puts different prototypes out in the market and tests which does best

Though potentially more time-consuming and expensive, this approach offers the most real-life data on customer impressions



#### Virtual marketplace simulation to quantify likely uptake and optimal offer combinations

Strategic choice analysis that invites respondents to trade off between competing offers and reveal a preference for one versus another

## CASE STUDY

### DEVisING A NEW PROPOSITION IN FOOD SERVICE

Based on trial feedback, the offer resonated with customers, solving ordering hassles and helping them manage their margins. However, when it came to selling the proposition, many customers were either sceptical of the benefits and hassle of signing up, or used it as an opportunity to negotiate prices down to reduce the perceived risk.

The company overcame this inertia by following the four points shown in Lesson 4:

1. **Make it easy:** the company invested significant time in designing sign-up to be quick and efficient, completed in one short sales visit
2. **Provide reassurances:** the company provided customer testimonials and money back guarantees vs. competitor offers
3. **Use early adopters as advocates:** early sign-ups were encouraged to recommend other local businesses to sign up
4. **Provide incentives:** for valuable customers, the company provided time-limited teaser offers to encourage adoption without long-term discounting

### Lesson 4 IDENTIFY TECHNIQUES TO GET AROUND THE INEVITABLE CUSTOMER INERTIA

Once you have a magnetic proposition, you still need to convince customers to adopt it. B2B customers are often reluctant to try something new. Many are naturally distrustful of new offers from suppliers, fearing they may lose out through changes in terms, conditions, or pricing on their core purchases.

Our experience has found that you need to do four things to overcome the inertia:

1. **Make it easy: remove barriers to signing up to the new offer**
2. **Provide reassurances (sometimes financial) that it will work and that downsides will be covered**
3. **Use early adopters as advocates for the proposition**
4. **Provide incentives to customers to use the new proposition**

In our experience, the sales force may need several rounds of training on a new proposition to be able to get customers over this inertia. In the case study on the left, 3–6 months of training, role play, and practice to deliver the pitch got conversion to as high as 90%.

## Lesson 5

# DON'T LAUNCH BEFORE YOU ARE READY – THEN SCALE, FAST

Nothing can kill a good proposition faster than an inability to deliver on your promises to the customer. And nothing will frustrate you more than an inability to scale up your winning proposition. But how can you avoid these issues?

Launching well requires a high degree of discipline and focus on some key areas:

- **Planning:** be rigorous in planning and monitoring all aspects of the launch, including the IT systems you require to support it. Set pilot standards by which you judge readiness to launch – 75% right just isn't good enough here!
- **Piloting:** thoroughly test the launch with dress rehearsals of each element of the proposition and the supporting infrastructure
- **People:** overinvest in people to support planning, training, execution, and assessment

Assuming the pilot is successful versus your standards, you will want to rapidly scale it up. This means having systems and sales approaches that can be scaled up, a roll-out plan, and the resources to do it. All of these things should be considered as part of your pilot so they can be anticipated.

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*“The trick is to ‘swarm’ the pilot... you have to overinvest in people and planning as it has to work when you launch.”*

*– CFO of a European distributor*

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# CONCLUSION

In a competitive environment where most companies are struggling to drive profitable growth in their core customer base, generating and harnessing demand for new propositions is critical to breakaway performance.

However, creating the environment to systematically design and launch winning new propositions is challenging at the same time as running your existing business.

Looking at successful innovators from the wholesale and distribution industry and beyond, we have identified five lessons to follow to institutionalize innovation in a company.

1. The first lesson is to **look for innovative ways to solve customer and supplier hassles to generate demand** for new products or services and build customer loyalty.
2. To turn the idea into reality, your organization needs to **create an environment (culture, people, and process) that helps you systematically develop and refine propositions.**
3. This environment needs to be designed to **keep refining and testing the idea until it is “magnetic”** – functionally good is not enough. You need something customers love.
4. To sell your winning proposition, **you must also make sure you plan how to overcome the natural B2B customer inertia around changing their behavior.** This means making it easy to buy the new proposition and providing appropriate reassurances and incentives to the buyer.
5. Finally, your organization needs to **be skilled at launching well and scaling fast.** This requires rigorous planning, and careful piloting with high standards to measure success.

Generating new demand and unlocking profitable growth can be a reality for any company, but it requires disciplined application of a different approach to managing and incrementally improving your core business.



## ABOUT OLIVER WYMAN

Oliver Wyman is a global leader in management consulting that combines deep industry knowledge with specialized expertise in strategy, operations, risk management, and organization transformation.

In the Distribution and Wholesale practice, we draw on unrivalled customer and strategic insight and state-of-the-art analytical techniques to deliver better results for our clients. We understand what it takes to win in distribution and wholesale: an obsession with attracting, serving, and growing customers, constant dedication to operational excellence, and a relentless drive to improve capabilities. We have a track record of helping clients win in this environment, creating real competitive advantage and driving significant growth. We believe our hands-on approach to making change happen is truly unique – and over the last 25 years, we've built our business by helping distributors and wholesalers build theirs.

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