

The Distribution Advantage In Indian Markets

Contributed by ValueNotes
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Competitive advantage stems from multiple sources. It could be brand, technology or patents, a natural monopoly, access to rare (or cheap) resources or a combination of several factors. Sustaining above normal growth and profitability requires companies to constantly enhance their competitive advantage. Warren Buffet likens this to a "moat" that helps the best stay ahead of the pack.

While brand, patents and such like corner much attention - in a market like India, distribution is one of the most critical competitive advantages (or barriers).

India is a large country. So it's not enough to make a product and then advertise on IPL - one has to get it to the customer. The poor infrastructure (transportation, warehouses, cold-chain, etc.) makes it even more challenging. This is further complicated by language, customs and local regulations. What makes it even more difficult is that the "distribution" industry itself is unorganized and localized for the most part. It's not possible to simply plug into a national network, and if these exist at all - then they will charge a premium.

Hence, distribution has to be built ground up - it cannot be bought off-the-shelf, unless you buy a company. And such companies are often not for sale. If they are, then the premium to be paid is so high that most competitors cannot afford it.

If you look closely at consistent outperformers like ITC, Hindustan Unilever, Asian Paints, Pidilite, etc.; their distribution networks dwarf those of their competitors. Building pan-India distribution is one reason why big brands like Coke and Pepsi are taking so long to reach profitability and scale. On the flip side, gaps in distribution provide opportunities to new entrants. In a recent research study on bottled water, we found that several small companies built strong local businesses, by focusing on small towns where national brands like Bisleri or Kinley were not available easily. Similarly, in mobiles, Micromax gained significant share by targeting customers in tier II and tier III cities.

Given the rapid growth of urbanization (and urban lifestyles) in India, reaching small towns and distant regions is becoming even more critical. Distribution has to be built brick-by-brick, and needs physical visits by sales people, contract negotiation and due diligence. Partners need to be educated about the product, and training for technical products can be significant.

Distribution advantage is not only about FMCG. White goods and electronics manufacturers sell in retail, as do garments and many other categories. Besides there are many B2B businesses like paints, industrial adhesives, building materials, etc., which are sold via retail outlets (even if the customer is not always the final end-user). For most B2B intermediates (chemicals, components, metals, electronic parts, etc.), even if a few large customers can be serviced directly, there are many more small customers, so distribution is crucial.

Building and sustaining this takes time, effort and a deep understanding of what works in each local market. Further, rising competition and emerging customer segments mean that one has to stay updated. Seemingly insignificant local problems can cost dearly. In a recent Voice of customer study on paper products, our client was losing market share in certain locations due to long delivery times - even though their brand was preferred. During a similar exercise to evaluate distribution channels for electronic components, one of the big problems was the lack of technical knowledge of dealers. In another study on air-conditioners, poor after sales service was impacting the brand negatively at select locations.

In the final analysis, you cannot do without a quality distribution network. Since this is not available off-the-shelf, it must be built out (and maintained) slowly and painstakingly. And to do this, an understanding of how it works in each state, district, city or even village is crucial. Of course, this research also requires time and money, but the alternative might be even more unpalatable.

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