

SMB FRONTIERS

Solving the Small Customer Dilemma in the Chemical Industry

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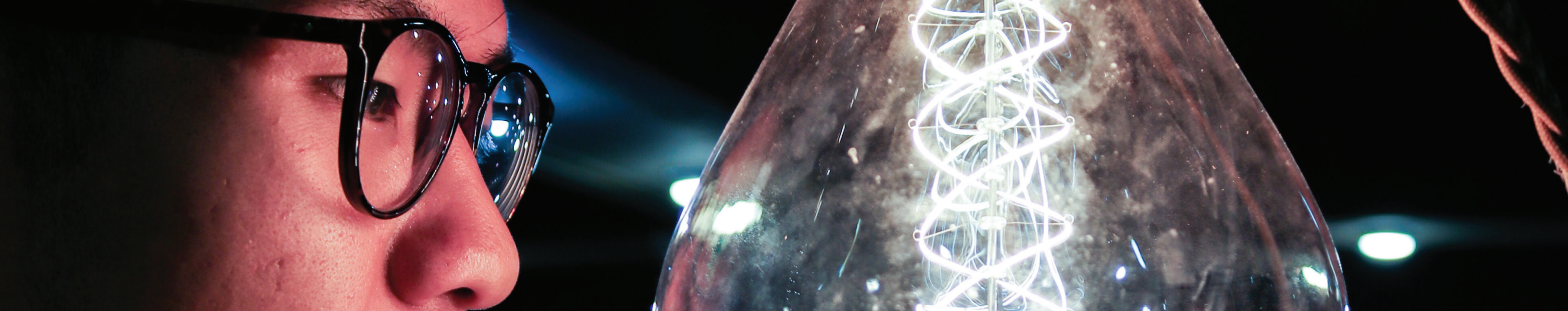
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The chemical industry finds itself at an extraordinary moment in time. Facing challenging logistics and customer expectations that are drastically different from just 5-10 years ago, manufacturers of specialty chemicals must continue to search for innovative ways to advance performance. As budgets tighten and tensions rise, there's tremendous pressure on management teams around the world to dramatically re-think and re-shape their operations in order to recoup lost sales and profits while enhancing their competitive position.

Today's uniquely competitive environment is compounded by China's global leadership position in manufacturing, with output that continues to ascend the value-chain, setting the stage for an uphill battle for years to come for U.S. companies. End-use customers now have access to a broad spectrum of tech tools for product and price discovery, and access to vast amounts of competitive and market information. This is especially true in highly innovative industries, such as food ingredients, where fragmentation is occurring due to rapidly shifting consumer preferences.





A Light In The Dark

It might seem counter-intuitive, but it's the perfect time to pay careful attention to the Small-to-Mid-Sized Businesses (SMB) customer. Agile and swift, these young upstarts are helping manufacturers bring uniquely differentiated products into the marketplace, or are filling special roles that their larger counterparts cannot. According to industry sources, global consumption of chemical products now exceeds \$2 trillion. In most of the chemical products sub-groups, the proportion of sales derived from SMBs generally varies between 10%-30%, translating into an aggregated addressable market opportunity of approximately \$200-300 billion with attractive above average GDP growth characteristics.

However, the opportunity for these companies can be significant. Enough to move the dial for a multi-billion dollar manufacturer? Initially: likely not. But over time, the next Tesla (\$120 billion market capitalization), Annie's (acquired by General Mills for \$820 million) or another high-growth household or trade brand will emerge. The concept of "lifetime value" quickly changes to "opportunity cost" – the cost of trying to 'win' the business from a competitor after the fact, or potentially missing out on being a supplier partner altogether.

"Historically, most senior executives in the chemical industry spend little to no time thinking about their small customers", said Mick Slattery, CEO of Xenon arc, "However, we see incredible value in this segment. We commissioned this research to help everyone unlock the great value that we believe is central to the long-term growth of this industry."

The Small Customer Dilemma

In many industries, SMB's represent a significant proportion of revenue and a unique profit opportunity, helping to catalyze innovation throughout an industry while serving as test-bed for new offerings. Despite their size, they're often willing to pay a premium over larger customers, should the relationship generate value over the long term.

But SMB's come with their own share of pain points, to—they're notoriously demanding, expecting considerable attention from their suppliers; and if expectations aren't met, they might leave for a competitor.

Traditional strategies to serve these customers fall in two categories, each with their own unique set of problems:

- 1. The direct model – employing a direct sales force.** While offering a personal touch, manufacturers report higher sales and customer service rep turnover; higher administrative costs; and increased complexity, leaving the SMB to deal with service gaps, inflexible commercial terms and a host of other frustrations which typically end in poor experiences and decreased brand loyalty.
- 2. The Indirect, distributor solution.** Though rich with efficiencies, manufacturers lose command and control of the customer experience; lose visibility into customer and market dynamics, opening the door to channel conflict, all while relinquishing brand intimacy.

The most common outcome of either strategy is low to no growth of the segment. In fact, often an unintended third strategic option materializes by default: abandonment of the segment altogether.

The Path

Research

Is there a viable way for manufacturers to form intimate relationships with these non-core, end-use customers? In a world that's changing very quickly, what are their specific needs?

To find out, Xenon arc commissioned ERDM, an award-winning pioneer of Voice of the Customer (VoC) research, to gain an in-depth understanding of how SMB customers and prospects in the materials industry define meaningful customer engagement.

From 2019-2020, ERDM conducted over 149 hours of interviews across 108 companies, spanning a wide array of customers, seeking to define how they would prefer to engage materials producers and then ranking their priorities.

Big Picture: A Frustrated Category

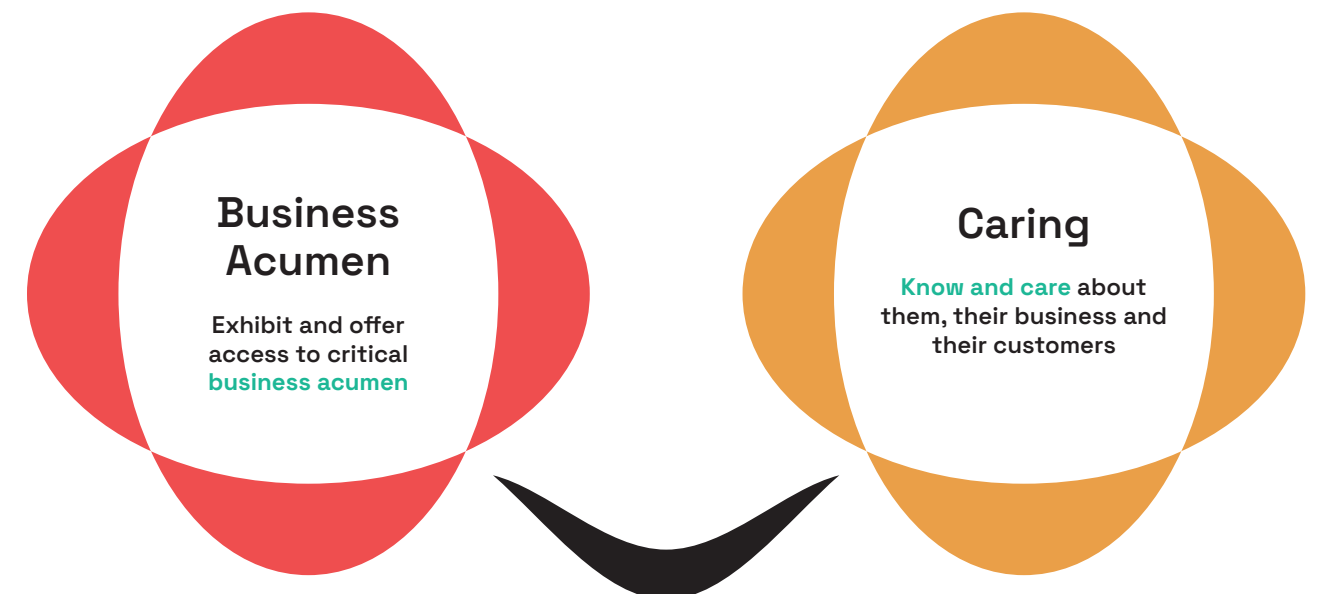
Though ERDM has been conducting VoC research for decades, their top takeaway was that this was “the most problem intensive group of customers” they'd ever seen—now that's saying something! The dissatisfaction was widespread and agnostic with regards to channel type, whether producers, distributors, or marketplaces.

SMBs tend to be a highly cynical customer base. In fact, some defined success as vendors who simply achieve basic service commitments with no perceived upside and significant downside risk.

On a brighter note, the research project itself speaks to an opportunity as it generated significant positive goodwill with customers, with many citing their appreciation for the process and the opportunity to voice their needs and preferences. This highlighted the desire of SMBs to improve their vendor relationships and the opportunity for producers who choose to focus on them.



These were essential **needs** for customers, and not meeting expectations means providers don't get their business. Price was such a close second in importance that is moved in this “need” category.



These are customer **wants**—while they don't expect providers to offer them, these are the qualities that when exhibited on a regular basis, set premier providers apart from the rest.



Key Insights For Producers

In the context of the overarching themes above, four clear insights emerged for producers:

Insight 1: *Small customers have clearly articulated criteria, expectations that must be met—and ultimately, exceeded.* In this regard, the SMBs who participated in the study identified four categories of criteria that are critical to success—Operational Reliability, Price, Business Acumen and Caring.

Insight 2: *The prioritization of criteria can appear counter intuitive.* For example, it is widely assumed that small customers value bundling or the ‘one-stop-shops’ provided by traditional distributors. But the research clearly indicates that SMB’s would prefer a deeper, direct relationship with the manufacturer—so long as key service criteria are met.

Looking deeper, the research identified 18 underlying criteria required to exceed customer expectations and achieve that “best-in-class” level with customers. The first 10 criteria do the heavy lifting needed to win and, ultimately keep, a customer. The other 8 were identified as necessary to take the customer relationship to the next level and become a top performing vendor, garnering the loyalty and resulting lifetime value needed to extract value from this segment. Atop the list were the operational criteria – creating table stakes for earning customer loyalty.

“[Our Suppliers] are the biggest contributors to our success! But, if they drop the ball, it hurts the company and its customers.”

Each of these 18 Criteria are defined in more detail as follows, ranked by customer priority:

- 1. Quality Product:** Quality was clearly rated as the most important criteria – the product must perform, consistently, in order for vendors to win and keep business with SMBs.
- 2. Competitive Pricing:** Pricing was defined as having 3 key mechanisms critical to the foundation of building trust and ease of doing business: Overall pricing, value and cost of doing business.
- 3. Responsive Service:** Responsiveness has multiple facets which are all important to customers, including promptness of response, turnaround time (of information requests) and speed of troubleshooting.
- 4. Availability:** If managed well, availability of products/materials/ingredients can prove to customers how much you care about them and their business.
- 5. On-Time-In-Full (OTIF) delivery:** How consistently the product is delivered to INITIAL expectations.
- 6. Reasonable Lead Time:** SMB customers are willing to wait longer for highly differentiated, rare products than they are for readily available, basic products.
- 7. Technical Expertise:** SMBs generally don't have access to the caliber of technical expertise they need to independently problem solve, and many have questions about the product/material/ingredient they wish to incorporate it into their process or formula.
- 8. Timely Documentation:** Among food ingredient SMBs, this was cited as one of their highest areas of dissatisfaction and strain. Delays with documentation and general information are common, and SMBs named this as a major influencer on loyalty.
- 9. Appropriate MOQs:** Most study participants reported that minimum order quantities were generally appropriate for their purchasing needs; however, when MOQs are out of reach, SMBs find this highly disruptive to their overall relationship with a vendor.
- 10. Product Stewardship:** This was highlighted as a key attribute when selecting vendors. While this was voiced as an important point across almost all companies in the study, it is especially critical to those doing business in heavily regulated industries who are often audited.
- 11. Ethical Company:** Among the criteria necessary for companies to excel with customers, being an ethical company rated the highest (For most, knowing their supplier is acting ethically relative to their products/materials/ingredients lessens their overall risk and legal exposure).

“It’s one of the biggest problems with being a small company. We could probably use, even more than our bigger competitors, help with some of the more technical aspects of the ingredients we buy. And to do that we need access to the manufacturer’s resources.”

- 12. Product Portfolio:** Customers WANT their best vendors to bring them options, alternatives, new products/materials/ingredients, and have a look at their full product suite because it makes their job easier, especially if they consider you a good supplier.
- 13. Know my Business:** Study participants identified three areas for proactivity: “The vendors we use most actually care about us and our business. That’s probably the biggest difference.” Communications, business recommendations and problem-solving.
- 14. Trust:** This unique criteria is vital to create strong partnerships. Some of the key areas that were highlighted as eroding trust were: not being transparent about price increases; document delays or inaccuracies; and getting incomplete or inaccurate data.
- 15. Partnership View:** Many respondents want suppliers to be invested in their success and offer resources and help that can impact the growth of their business, outside of just product-related resources and advice.
- 16. Good Sales Rep:** As long as the overall relationship is going well, most customers will suffer through a bad or absent sales rep; the caveat, however, is that if any of these areas start to suffer, the customer will be quicker to replace a vendor.
- 17. Right level interaction:** Most SMBs valued the quality of their interactions over the quantity of interactions.
- 18. Market Leader:** Finally, it was important to respondents that they work with a market leader, whether the ‘biggest’ or ‘best’ company in the industry, or the one with highest quality or unique products/materials/ingredients, or the one with the shortest and most efficient supply chain.

Insight 3: Mismatch of Account Categorization. Traditionally, materials producers have viewed their customer segments through a matrix based on customer size and end use market (e.g. core versus non-core), customer size and margin, or customer size and service needs. The result is a tiered system of accounts, with Strategic Accounts or “A” customers in the top tier that are served through a customer-intimate, high touch, relationship-focused model. Below that first tier may be two or more categories of less strategic customers, with diminishing importance and focus.

These traditional frameworks differ meaningfully from how SMB customers view themselves and their desired relationship with vendors. Seen through this lens, the critical dimensions are: (1) The importance of the product to their business (e.g. a critical ingredient for a small food company); and (2) The proportion of spend the vendor represents. Based on where they are on these two dimensions, their expectations of service and the prioritization of the criteria discussed above shift. In some cases, certain requirements completely disappeared, while others were more highly valued, based on the nature of the vendor’s importance to the customer. In all cases, operational reliability is a critical component of how SMBs want to be serviced and should never be overlooked.

Strategic (*High importance of product/High proportion of spend*): For these vendors, customers expect operational reliability, competitive pricing, business acumen, and demonstrating a high level of care from the providers that everything is being delivered to the highest standard. Of these criteria, caring is the most highly valued.

Transactional (*Low importance of product/High proportion of spend*): Vendors that fall into this category are still expected to deliver a high level of service in all four areas. Of these, operational reliability is the most important.

Reactive (*Low importance of product/Low proportion of spend*): Companies that fall into this category are still expected to deliver solid operational reliability and may have less room for error. To companies in this category, price competitiveness is most important.

Important (*High importance of product/low proportion of spend*): Vendors in this category are expected to reliably deliver in all three areas except caring, because of the lower investment. Operational reliability is most important to this category.

What becomes critical, as we view customer preferences through this lens, is understanding how to adapt and adjust service and support models to better address customer priorities and needs. When we approach SMBs traditionally, we

may be missing the mark on two fronts: first, we may be over-servicing accounts who don’t need or want it, and second, we may under-servicing accounts that need more attention – putting the business at risk of churn.

In addition, price elasticity and margin opportunity vary significantly by quadrant. Customers in the “Important” quadrant are likely to be more willing to accept price increases than customers in the “Transactional” quadrant. Anchoring segment-specific pricing strategy in this analysis will yield significant margin expansion from the SMB customers.





Insight 4: Digital technologies provide an opportunity for vendors to fundamentally upgrade their relationship with SMBs. Digitization is on the agenda for every senior executive in the materials industry. Start-ups and corporate initiatives are proliferating, and at a conceptual level, the potential for SMBs is clear. That said, the current landscape of digital tools is fragmented. Most materials producers are left with a sub-optimal and confusing patchwork of different options as entrepreneurs and investors rush to fill the digital gaps. For the most part, materials producers have been focused on digitizing internal operations, leaving the industry well behind in the development of customer-facing digital platforms. Add to that the siloed nature of materials businesses, the rigidity of enterprise software programs, the technical and scientific nature of the products, the risk profile, regulatory requirements, and the decision of how and when to act becomes a major challenge. Finally, the expectations of SMBs have been highly influenced by their experiences as consumers, meaning a standard of performance and ease of use has already been established in the minds of the target audience.

This rise of digital platforms in the industry will ultimately lead to a shake-out of winners and losers. Critical considerations for producers as they navigate in-house and external options include: Who will own your customer data? Who will manage

“Most of the [providers] we’re working with don’t have [online platforms], though all the larger ones do. We use the ones that are good, so maybe 25% of those.”

the transactional complexity? How is your brand represented? As those questions are being answered and options navigated, it is critical for producers to not lose sight of perhaps an even more fundamental question: What do SMBs want from their digital engagement with vendors?

Most fundamentally, customers want digital to be a *fully integrated element of a holistic service engagement with producers*. A simple concept, but difficult to execute well. More specifically, customers pointed to four priorities regarding their digital interactions:

1. Clear access to a live, technically competent person on demand via the online commerce site.
2. Easy access to live and accurate information, shaped by expectations from B2C platforms.
3. eCommerce should be clearly intended to be additive to their experience and not, in any way, representative of a cost-reduction initiative.
4. Most importantly, the platform must meet all expectations for operational reliability, most specifically the same top 10 criteria identified in the earlier part of this paper.

Customers in the study echoed what has been proven across thousands of B2C online commerce platforms—that a seamless customer experience will make or break the success of your offering. It is the integration of each piece of the customer journey, and the operational performance coming together, that foster trust in the site and, ultimately, the producer’s brand.

Customers were clear that no vendor initiatives (yet) met these requirements. Others, like marketplaces and aggregators, are structurally limited from ever meeting one or more of these criteria.

Our Commitment To SMBS

For producers of products in the materials industry, there clearly exist strong, long-term benefits to deploying a service model that understands the unique needs of SMB customers.

Decades of experience, deep analytics, supported by unbiased, third party research has given Xenon arc unparalleled expertise in the evolving service requirements of SMB customers in the materials industry. We have developed a unique, technology-enabled solution for the industry based on actual data versus perception. It creates the opportunity for win-win outcomes for on both sides: For producers seeking to drive greater effectiveness and efficiency from this segment, and for SMB customers seeking to compete in an ever increasingly challenging environment.

The solution has already been adopted by leading producers in the industry including DuPont, Cargill, Kerry, Tate & Lyle, Quaker-Houghton and others.

Results are compelling.

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