One Consulting Firm

# Evolving Channel & Distribution Landscape & Implications for Brands and D2C companies

# Table of Contents

CONTENTS

INTRODUCTION

## Evolving Channel & Distribution Landscape and Implications for Brands and D2C companies

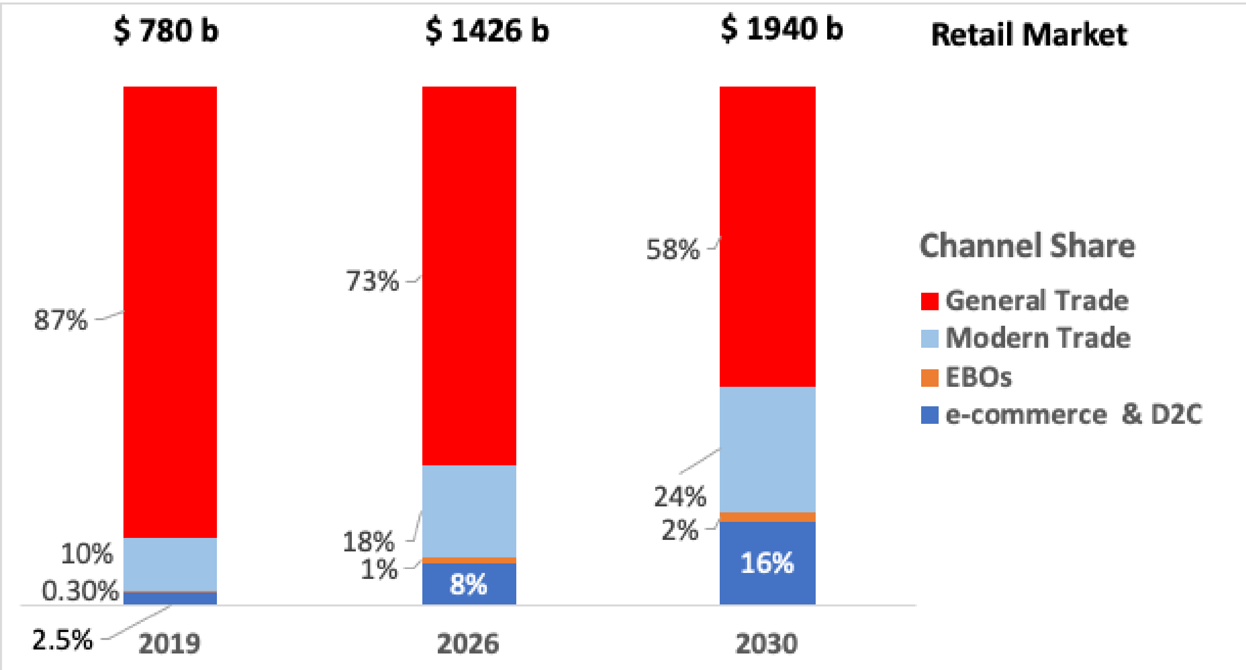
India's retail channels and the distribution landscape are likely to undergo rapid changes. There are several compelling drivers behind this.

Indian consumption has traditionally taken place through the general trade (13 mn kiranas) which are served by thousands of distributors spread across the country, serving local markets. These distributors have built deep relationships with retailers over several years, serving them through thick and thin, offering them credit, the flexibility of smaller orders, and doorstep deliveries to make their life more convenient.

Things are changing, however. This quote from Sunil Kataria – CEO Godrej Consumer Product, India & SAARC, best summarizes the speed of this change

“One thing I want to put on the table for all people in the industry is this is going to be a piece which all have to navigate very fluidly because it is evolving like crazy right now”.

# The shape of Channel & Distribution in 2030




Source : OCF analysis based on secondary research

Key points of transformation

- The general trades' share is likely to decline from 87% to 58%, but in absolute terms, it would increase by US$ 450 billion. As explained below, many developments in the distribution front would help Kiranas to modernize and do well. The challenge would be post year 2026, once the share of other channels rises in comparison to the overall growth of the retail market. If other channels continue to take more market share from Kiranas, the channel can face stagnation.

- There will be a major shift in how brands serve them. The B2B aggregators such as Udaan, Jio Mart, and Flipkart Wholesale may capture 5-25% of the market depending on the scenario. The implications for brands, distributors, and Kirana stores are significant. Going forward, we'll discuss them.

- E-commerce and direct-to-consumer (D2C) brands will grow at a CAGR of 28% to take 16% of the market by 2030. Even though this share is small compared to China (>50%), it is still US $230 billion (six times the 2021 level of US $38 billion). With technology evolving rapidly, the percentage share may increase.

- With its strong foundation, modern trade would continue to grow at 18% per year to reach above the US $ 450 billion by 2030.

# CHANGE DRIVERS

## 1. GROWTH OF E-COMMERCE AND D2C BUSINESSES

E-commerce and D2C players would continue to grow and gain channel share. This can even accelerate with several promising new technologies in the pipeline. Already there are 4,000 D2C brands. This space is seeing a lot of action from the brands, investors, and enablers like Mensa and GOAT. We think that this trend would accelerate.

In almost all cases, FMCG companies are strengthening their e-commerce businesses and are generating 5-10% of sales and many are profitable. They are also acquiring direct-to-consumer brands.

In light of the horizontal and vertical marketplaces solidly in place and the commitment of the promoters and investors, e-commerce will continue to grow.

## 2. THE MODERN TRADE WOULD CONTINUE TO EXPAND

Modern retail formats are now firmly established and are expected to continue to grow across all categories. Existing players like Tata, Amazon, Reliance, Landmark and Shoppers Stop are committed to making large investments and growing the sector. If FDI regulations are relaxed further, international players may join them.

## 3. UPGRADATION OF KIRANA STORES

For the first time, Kiranas are in a great position to upgrade themselves. With the support of the aggregators, CPG companies and other ecosystem players, Kirana stores can stay relevant in a changing world of the biggies.

# 4. ADVENT OF B2B E-COMMERCE (ALSO CALLED AGGREGATORS)

- The biggest disruption is likely to come from B2B e-commerce players like Udaan, Reliance Jio Mart, Flipkart Wholesale, and others who use technology to take orders from lacs of Kirana patrons.

- 8-12 players are vying for a share of this US$ 680 billion market. It will be interesting to see how these players evolve. Some players plan to focus on rural parts of the country, while others will focus on urban areas. As things stand today most of the players are focusing on the urban market. Similarly, some players might occupy the horizontal space while others might specialize in one or two industries.

- China is well-positioned in B2B e-commerce, with firms like Alibaba well established as a horizontal marketplace and firms like Meicai and Yijiupi specializing in agriculture and alcohol, respectively.

- If India were to go through this evolution and at that pace, aggregators could take a sizeable share and across many of the categories. Most of these players are big, well-funded, and know how to operate in the business.

- The fact that both Walmart and Metro Cash & Carry are ramping up their distribution through sales force and technology platforms is not surprising given these trends.

- The aggregators have certain advantages over traditional distributors, such as better pricing, credit, frequent deliveries, better efficiencies due to full truckload, access to funds & talent, and technology. It will be interesting to see how traditional distributors respond. The traditional distributors can leverage their relationship with retailers, knowledge of the products they specialize in, and their ability to pick up smaller orders.

Here is a glance at the key players

| PLAYER | REACH & GMV | STRENGTH | FUNDING (US $ B) | PRODUCTS |
|---|---|---|---|---|
| udaan 2016 | **Reach:** 3 million customers , 900+ cities, 12,000 pin codes 25-30,000 sellers **GMV:** US$ 3Bn | • First mover advantage – most likely would continue its lead • Vision to have US $100 b of transactions in 7-8 years • Good coverage and high satisfaction among retailers • Lending, sourcing and fulfilment capabilities • Strong private labels in several categories & well funded | $1.2b Lightspeed, Venture Partners, Octahedron Capital, Moonstone Capital Partners and others | 2,500 brands across multiple categories electronics, F&G clothing, fashion accessories, home furnishing products, pharmaceuticals/medicines |
| Flipkart Wholesale 2020 | **Reach:** 1.5 m customers; Fashion -23 cities; Grocery- NCR region; 29,000 fashion retailers **GMV:** Best Price business US$ 0.6Bn | • Pivoted its cash & carry business • Flipkarts' technology is an advantage complemented by Walmart strengths in wholesale business | Parent Funded | Fashion, grocery and general merchandise |
| JioMart 2020 | **Reach:** 0.2 m retailers,120 cities 50 Reliance Market Stores | • Strong presence in B2C space, experience in B2B space • Well funded & Very strong B2B proposition • Aggressive plans • Can leverage WhatsApp | Parent Funded | Multi categories |
| ElasticRun 2016 | **Reach:** 1.2 lacs kirana; Plans to reach to 1m in 2 years | • Rural focused | $132.1M; Prosus Ventures, Avataar Ventures, Kalaari Capital | |
| METRO Cash & Carry 2003 | **Reach:** 3.5 m registered users, 0.8 m are kirana; 30 stores-plans to open smaller stores **GMV:** US$ 1 Bn(revenue in 2019) | • Kirana centricity • Smart Kirana program s -2000 outlets • Profitable operation | Parent Funded | Own brand |
| Jumbotail 2020 | **Reach:** 30,000 kirana stores | • Data Centricity | | Food & grocery |
| ninjacart 2015 | **Reach:** Present in 11 cities, 60,000 customers, 20,000 farmers | • Elimination of middleman, relationship with farmers | Tiger Global, Accel, Syngenta Ventures, STIC | Fruits & Vegetables |
| bigbasket | | • Technology and B2C retail • Part of Tata group & Relationships with brands & suppliers | | |

Source survey by One Consulting team:
Pharma Outlets in Gurugram and Mumbai. A few retailers preferred to stay with their distributors and valued relationships over the price and other benefits offered by aggregators. Some of these retailers may eventually work with aggregators once they hear from their peers and overcome their technology inhibitions

As many as 40% of the retailers mentioned that they are working with the aggregators and are willing to order anywhere from 20-60% of their merchandise from them. Aside from better prices and credit, they felt so relieved that a substantial portion of their workload had been removed.

# IMPLICATIONS ON STAKEHOLDERS

# IMPACT ON ECONOMY

## Indian retail industry is one of the most dynamic and fast-paced industries contributing a significant portion of the country's GDP and around 8% of employment.

Kiranas contribute a good portion to India's GDP. Studies have found that modernization can be of great benefit to Kiranas. This can have a significant impact on India's growth prospects. The incremental gains to Kirana's topline could result in an increase of 1.25% in India's GDP growth

In addition, the Ministry of MSME has taken a landmark decision to include Retail and Wholesale Trades as MSMEs. Retail and wholesale trade will now get the benefit of priority sector lending under the RBI guidelines. This will have a positive structural impact, helping the industry to formalize, get structured, & the much-needed support to revive and thrive.

# IMPACT ON BRANDS

## Several FMCG brands have dominated the country with their extensive distribution networks.

Until now, this network was unassailable and this was one of the reasons FMCG companies got high returns on their investments.

With the arrival of aggregators, this distribution network could come under threat, as would be their control of Kirana stores, which had so far only one source to purchase from. Also, the entry barriers for new entrants and existing smaller brands will be removed, since they can directly tie-up with a national distributor and reach out to lakhs of Kiranas. In parallel, D2C brands have discovered low-cost ways to build their brands-another competitive advantage that CPG companies may find under threat.

Currently, GTM costs are 30-40% of sales and are plagued by many inefficiencies, including partial truckloads - especially the last mile to service retail - manual processes, a lower service frequency, and not being as agile as the aggregators.

The key questions facing brands are:

- Is it possible to modernize, make more agile and efficient the distribution network without losing its relationship with retailers?
- How will traditional distributors be impacted? What new capabilities will be needed?
- How should they approach aggregators?
- How can they manage the channel conflict?
- How can technology be used to achieve the above? What new capabilities must be developed or outsourced?

The answers will differ from company to company.

Brands may want to follow this two-fold strategy:
1. Hold and modernize their distribution network
2. Collaborate with the aggregators.

Since both distribution models will coexist, it is imperative to follow this two-pronged approach. Companies are attempting various ways for modernization - for instance, Unilever with a 5.0 million direct retailers reach is building a marketplace where they can sell their brand as well as non-competing brands to expand the range of products they offer. - to take a larger share of Kirana (so they don't have to have multiple apps for different brands) and secondly to counter the problem of partial truck loads when supplying retailers. Another example is that of the WABI digital ecosystem from Coke. The challenge however is how many of these applications retailers can keep on their phones.

Although these changes won't be easy, they can prove beneficial in the long run if the brands can take advantage of them. Increasingly, brands realize that change is inevitable and it is better to embrace it and make it work for themselves and partners.

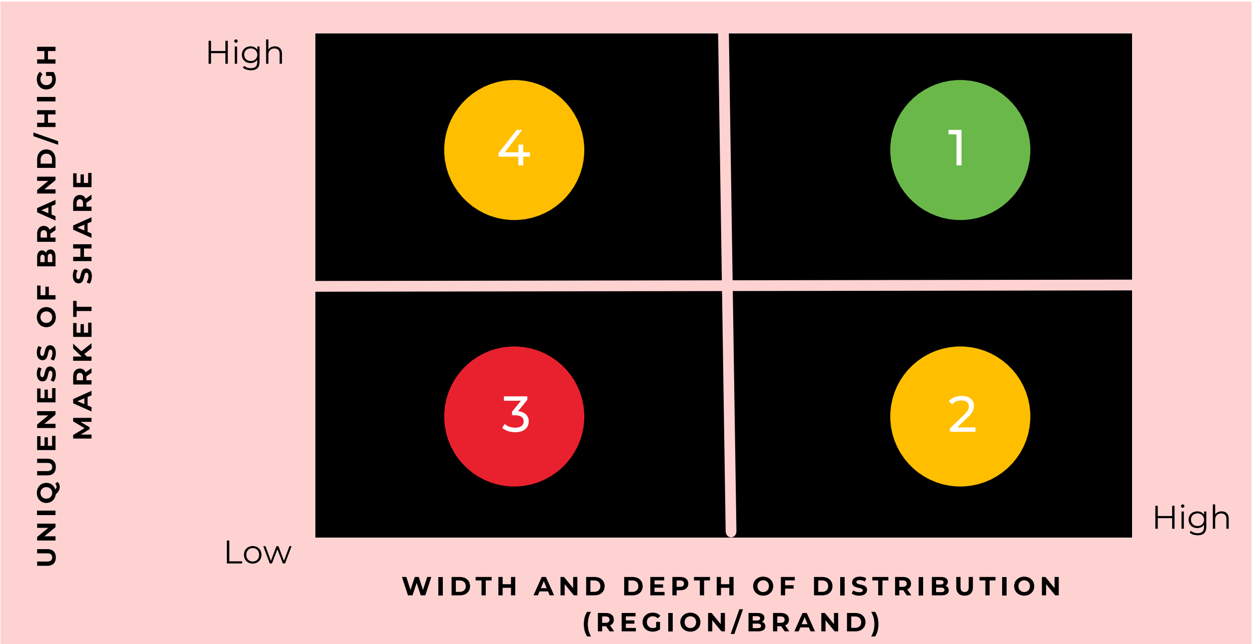
## The following are key imperatives for brands

# 1. Brands need to redefine their GTM strategy and the role of Channel Partners

Brands are not new to channel conflict. Through proactively defining the channel partner's role, offering different prices/products to different channels, and being transparent with all parties, they have managed conflict in the past. These are the best practices for managing channel conflicts and would continue to be guiding principles even when the storm is bigger.

The first step in dealing with the aggregators is to identify the strengths on parameters like reach, market share, hold on to the kiranas compared to the aggregators. By doing this, they can determine where they should hold back on their distribution network and where they can leverage the B2B aggregators' network/capabilities. The roles of the aggregators and partners, as well as brands and distributors, can be defined on this basis.

For instance, the following chart can offer some insight into where brands can hold on to their distribution network and where they can leverage aggregators' networks. As an example, brands in quadrant 1 are well-positioned to negotiate terms of trade.



Consider various scenarios of market shares by aggregators for the addressable market for the categories & geographies served by them

| Scenario | Coverage (A) | Market Share (B) | Net Market Share (A*B) |
|---|---|---|---|
| Conservative | 30% | 20% | 6% |
| Realistic | 40% | 30% | 12% |
| Aggresive | 60% | 50% | 30% |

This means that distributors could lose 6-30% of the market depending on region to region, category to category.

**What would be the new role of distributors in the new scenario?**
The new role might be based on the geography they cover, the services they provide, or the products they sell, as well as the strength of their relationships with retailers.

Is it possible for these distributors to specialize in products that require specific training that might not be available from aggregators such as Udaan, Jio Mart, etc. since they would be dealing with multiple brands & categories and are unlikely to have the time and skills to explain these features to their retailers? In the future, most aggregators plan to use a minimal salesforce and maximize technology for order taking. In this area, traditional distributors can establish their competencies and create niche markets for themselves.

Answers vary from company to company, product to product, and region to region. Under extreme scenarios, CPG companies might completely exit the distribution channel and focus exclusively on store visibility, shopper experiences at retail outlets, product innovation, sales, and marketing. These are a new set of strengths that brands may like to build and provide a new set of competitive advantages.

## 2. Help kiranas transform into their modern avatars

Several brands have provided retailers with order-taking apps. For instance, HUL has reached 3,00,000 retailers. This is an effective way of maintaining a hold over kiranas and a direct to retail (DTR) distribution model. Distribution to these outlets can be handled by existing distribution partners.

## 3. Build nimble supply chain

The leading aggregators are providing delivery twice a day and fulfilling orders in a matter of hours against twice in a week by most brands. Brands would need to meet or surpass the new service standards and for this, they would need to invest in the supply chain and technology.

Once the supply chain is driven by the orders from the retailers and not from the brand push, the supply chain is likely to become more agile and efficient..

## 4. Develop Personalized Assortments

Being partially free from distribution load allows brands to create bespoke assortments for each Kirana. One way to do this is by investing in AI and analytics. This could be a win-win for both parties.

Currently, many brands do not have a view of secondary sales, let alone visibility of sales in retail stores. We were working with a leading brand that had POS data coming in, but it was never used to make any actionable decisions.

It is time to develop those capabilities that will support sharp offerings with the right promotions. Currently, sales are mainly derived from trade promotions (10-20% of the sale) - many of these are ineffective and there is a huge savings potential.

# IMPACT ON KIRANAS

## We believe the kiranas are the key beneficiaries of the disruption in the distribution world.

On almost all parameters, they have the potential to gain: service levels, credit availability, lower prices, and the appearance of the store. An Accenture study showed that Kiranas could increase sales by 40-60% if they were transformed and supported throughout the business.

The share of Kiranas will drop to around 73% by 2026, but they will continue to grow as the Indian retail market grows. However, after 2026, Kiranas will likely face stagnation because e-commerce and modern trade will take away a large portion of the growth. This is likely to happen more in urban areas than in rural areas.

# IMPACT ON DISTRIBUTORS

## The distributors have been serving kiranas for a long time and have developed strong relationships.

The distributors have been serving Kiranas for a long time and have developed strong relationships. Several retailers we spoke with wanted to continue their relationship despite attractive offers from the aggregators.

The distributors may want to build on these strengths: their better understanding of products and their ability to give personal attention to retailers. CPG companies should support them in becoming more professional and help them upgrade technology. The disruption might be more pronounced in some geographies with strong aggregator presences.

# IMPACT ON D2C COMPANIES

## Though e-commerce is growing significantly, the majority share of retail is still offline.

The D2C players would like to consider off-line distribution sooner rather than later for several reasons, including scale, touch and feel, brand visibility, and several others. For them, offline distribution is new and will require effort and skills to establish a presence. They don't have an existing distribution network, so either they create their network, ride on B2B aggregators or a hybrid model. They might also do this region by region. Aggregators can offer a ready network.

Additionally, premium D2C brands can also consider building their direct-to-retail networks. Many of these brands have innovative products that need to be explained to retailers. An aggregator with multiple products may not have the skills and time to explain the features and benefits of these new products.

# CONCLUSION

- With trillions of dollars on the line, India has already begun yet another disruptive story in channel and distribution.
- Kiranas and the economy stand to benefit. Although the kiranas may face stagnation post-2026 as more share is taken by modern trade and e-commerce players.
- To play this game to their advantage, brands must rediscover themselves, redefine their GTM strategies, and redefine the role of distributors.

# ABOUT ONE CONSULTING FIRM (OCF)

- One Consulting Firm (https://oneconsultingfirm.com/index.php) was founded to provide exponential value to its clients through strategy & performance improvement advisory and implementation work.
- Our team has worked on more than 150 strategy and implementation engagements. We bring a difference to our clients through – experienced consultants, faster turnaround time and a commitment to deliver results.

# ABOUT AUTHORS

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# THANK YOU

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