

## **What happens to partners and IT end users?**

### **About the Author**

Bruce R. Stuart is the President of ChannelCorp. He is one of the world's foremost experts on vendor channel strategies and channel partner profitability. He has written eight books and authored in excess of 200 articles on the subject of channels and channel strategy. He has educated channel executives from more than 40 countries and has been working with vendors in Asia, Australia and New Zealand for over 15 years.

Mr. Stuart will be leading the Advanced Channels Workshop (11/12 March) and a new program Channel Management: the business dynamic (13/14 March) in Singapore. For more information or to comment on the article, e-mail [info@channelcorp.com](mailto:info@channelcorp.com).

The purpose of this article is to outline what generally happens in economies that display the characteristics outlined in Article 1. As previously noted, what is happening in Asia could certainly happen elsewhere, including North America. In addition, the article focuses on what happens to End Users when economies slow. Experience shows that those vendors whose people have had formal channel strategy and channel management education cope better in slowing economies.

Deflation – too few dollars chasing too many products – occurs when increases in production capacity systematically outstrip the ability of domestic and export markets to absorb the production. This phenomenon last seen in a significant way in the Great Depression, has some nasty side effects. Deflation can be demand-driven, or supply-driven, or in some cases driven by simultaneous drops in demand and increases in supply.

Currencies in deflating countries decline against the currencies of those countries that are not in a deflationary situation. The rapid decline in the value of Asian currencies against the U.S. dollar (in particular) caused a domino effect in the economies of the Asian countries (Figure 4, article 1).

Domestic interest rates shoot upward in order to stem the flow of investment out of the economy. The increase in interest rates affects computer hardware, software and telecommunications product end users, resellers and distributors. Domestic demand falls as the increased rates of interest draw working capital from those businesses that have borrowed. Purchases of products are delayed or postponed until “times are better”

Those companies that are fortunate enough to pay local devalued expenses and sell into U.S. dollar markets enjoy “windfall” profits. Devaluation suppresses expenses while price deflation drives export volumes.

Imported hardware, software and telecommunications products purchased with U.S. dollars become too expensive to sell in local markets. Domestic manufacturers, hungry for cash to pay bills, reduce domestic prices further. Debt with U.S. dollar interest rates becomes overwhelming. Banks, hit hard by devaluation and struggling to clean up battered loan portfolios, reduce the amount of credit that they will grant and in desperation . . . call loans. No new money is lent . . . a classic “liquidity trap” ensues. End users don’t pay resellers. In turn, distributors and resellers can’t pay the banks . . . or their vendors. The cycle repeats itself until businesses, and the economy, come to a grinding halt.

Those members of the channel that are supposed to carry inventory, reduce the size of their investments. Vendor run rates fall. Too much stock of slow moving or obsolete product fills the shelves and warehouses of resellers and distributors. No cash is available for channel partners to purchase fast moving items. The result in the channel is simultaneous stockouts and overstocks. Distributors and reseller that are owned by large, diversified companies are sucked dry of cash to save other cash-starved businesses in the conglomerates.

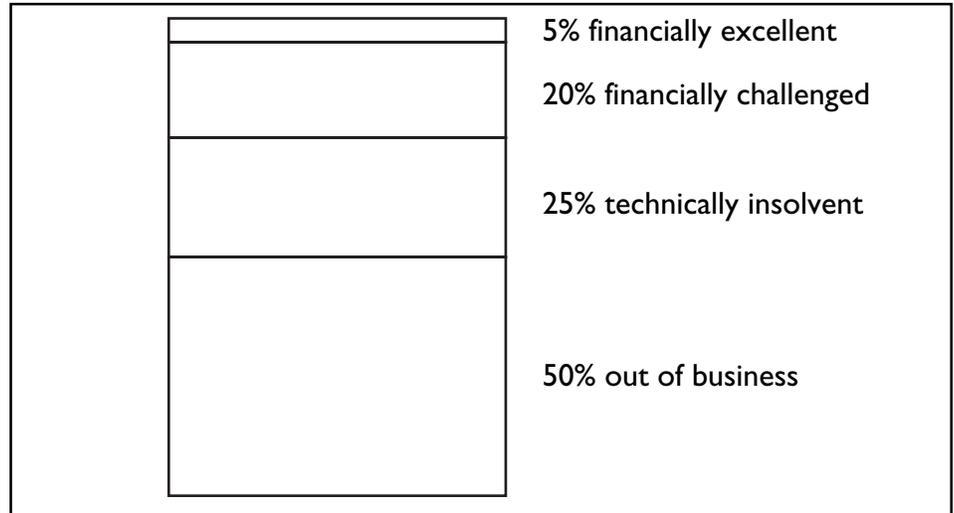
In most countries, the financial situation of many resellers and distributors is not great at the best of times. Figure 1 shows the situation in a typical “stricken” country’s channel.

**Figure 1 – The financial situation . . . on average not great**

<b>Top 10%</b>		<b>The top 10% are financially excellent and have 10% or more of prior year revenue in cash or unutilized lines of credit</b>
<b>Middle 40%</b>		<b>The middle 40% are financially challenged</b> <ul style="list-style-type: none"> <li>• Gross margin/person falling</li> <li>• Revenue/person falling</li> <li>• Cost per order dollar rising</li> <li>• Profit/person falling</li> </ul>
<b>Bottom 50%</b>		<b>The bottom 50% are technically insolvent. They have insufficient cash on hand to meet liabilities as they come in</b>

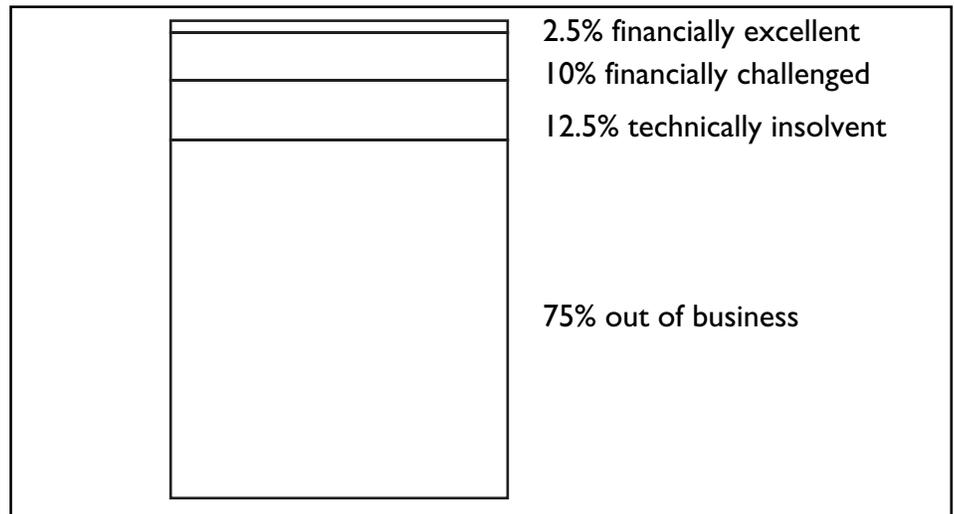
Source: ChannelCorp Management Consultants Inc.

**Figure 2 – The financial situation . . . at 18 months**



Source: ChannelCorp Management Consultants Inc.

**Figure 3 – The financial situation . . . after 18–36 months**



Source: ChannelCorp Management Consultants Inc.

Figures 1–3 outline the economic growth prospects for the various technology distribution channels of the countries in the region. If the deflation lasts 12–18 months, the bottom 50% of the resellers and distributors could go out of business (Figure 2).

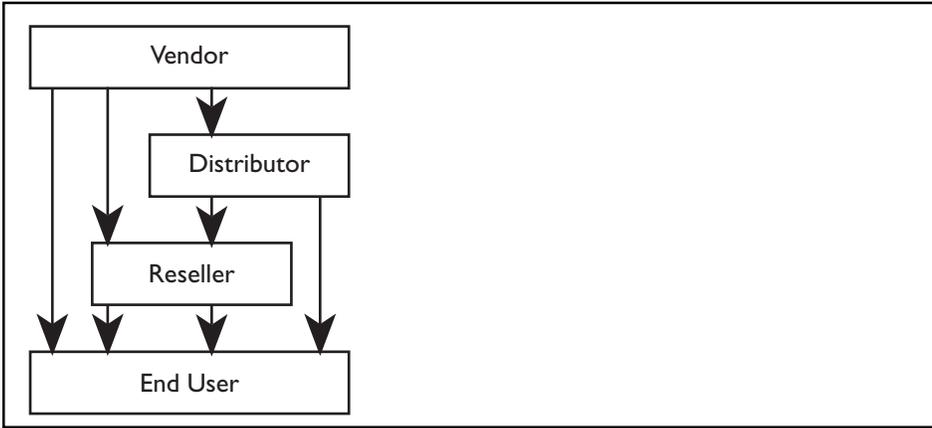
Deflation that lasts 18–36 months could take out the bottom 75% of the resellers and distributors in a country (Figure 3).

The path of deflationary devaluation is very clear. End users, resellers, distributors and vendors that are financially sound and well managed can survive. The rest will not. Financial triage is what happens. Resellers, distributors and vendors will make decisions regarding who will survive . . . and who won't.

## IT end users

The purpose of this section of the article is to outline the impact of deflationary economics on the end users or customers (Figure 4) for computer hardware, software and telecommunications products/services.

Figure 4 – Channel map



Source: ChannelCorp Management Consultants Inc.

End users of hardware, software and telecommunications products and services are themselves players in the industries that are over capacity (Figure 4). What will happen to end users of vendors, distributors and resellers in deflationary times is clear:

*domestic markets will slow and export markets will become more competitive as other Asian economies attempt to export themselves out of slumps*

*revenues measured in domestic currency will fall. Valued in \$U.S., revenues will fall dramatically*

*prices and profit will fall – margins will fall faster than expenses can be reduced  
working capital will be reduced – customers of the end users will be slow to pay their bills, profit from operations will be down, interest expenses will rise sharply and bank credit will be cut back*

*End users, as a result of weakened cash flow, will slow the payment of bills to their own creditors*

*People will be laid off in order to reduce expenses*

*Major corporations will be restructured and downsized, resulting in more layoffs*

When times become tough, end users attempt to reduce or delay their expenditures on new information technology (IT). As a result of IT expenditure cuts and project delays, end users attempt to extend the lives of their existing technology expenditures. Expenditures on outside service, support, training and consulting (SSTC) rise as might expenditures on contract people. Outsourcing becomes a consideration in order to backfill laid off IT people. On the other hand, big IT projects will vie for monies previously budgeted for hardware and software purchases.

Faced with a lack of cash for capital expenditures and severely curtailed availability of debt financing, end users turn to leasing as a source of capital to finance operations.

## **Article summary**

The channel organizations of vendors must be staffed by people who clearly understand the business dynamics of channel partners and their clients. The *Advanced Channels Workshop* and *Channel management: the business dynamic* provide the required skills. For any purchases/leases of any IT products or services, end users become very careful of which channel partners or vendors that they purchase from. Financial due diligence of potential suppliers becomes a key component of the vendor/channel partner capability analysis. No end user wants to be halfway through a project only to have the reseller go out of business or the vendor pull out support for a reseller . . . . or even a whole country.

### **ChannelCorp Education Programs in Singapore – March 2002**

We are pleased to announce that two ChannelCorp workshops will be delivered in Singapore March 11–14, 2002. This is ChannelCorp's sixth year of delivering world-class channel education to channel executives in South East Asia.

In 2002 we are offering an important new program. Channel Management: the business dynamic (13/14 March) is unique in the world. It will dramatically increase the business skills and improve performance of quota-carrying personnel such as channel managers, account managers and business development managers. This program will provide two years worth of knowledge and experience in two days.

The ChannelCorp Advanced Channels Workshop (11/12 March) is well known to channel executives in South East Asia. The 2002 Advanced Channels Workshop has been updated to reflect new eChannels findings and the new role of influence channels in the IT industry. This program has SOLD OUT for six straight years.

For more information on either program, go to [http://www.channelcorp.com/workshops\\_01.htm](http://www.channelcorp.com/workshops_01.htm). We can also provide detailed outlines and group pricing details. Simply send a return e-mail requesting data. We hope to see you and your people in Singapore in March.