Choosing the Right Channel Model

Increasing Your Sales and Profits through Strategic Global Business Development.

Consilium
global business advisors
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Buckle Your Seat Belt…Here We Go!

You're moving quickly now. You've decided to export (Still not sure? Read our white paper "Ten Reasons Why You MUST Export") and you've taken the first steps towards that end. (More info in our eBook "Taking Your First Steps") You've selected an initial group of markets (See our eBook "Where to Go First") and have started to prepare some of the legal and administrative footings which your initiative will require. (More details in our eBook "Initial Legal Considerations")

NEWS FLASH! The orders won't automatically roll in. This is going to take some work. You first have to create the demand, identify and nurture projects and then sell, sell, sell! Or rather someone has to, and this becomes the critical question. Who…and with what model? There are numerous "channel model" options that are available and selecting the proper model is an important strategic step which should be tackled as soon as the target market(s) is selected.

Maximizing Opportunity and Minimizing Risk

The thought process involved in selecting a channel model is similar to that of the decisions which you make early in your international business development initiative. It needs to support the company's strategic objectives. Implicit in that requirement is the expectation that an analysis of objectives and thorough planning precede this selection. Additionally, the target market selection step must also be completed before choosing a channel model.

Various factors from that analysis will impact this selection. Margin and pricing; expected and required revenue and profits; expected time to project activity, first order and breakeven; anticipated size of market now and in future; geographical size of market and homo vs. heterogeneity; local barriers and customs; location as a launchpad for other nearby and similar markets; and, plans to assemble, manufacture and source locally are examples of fundamental factors which will impact your decision.

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Other factors to consider in the selection process include, the magnitude of required investment, attractive tax enticements, regulatory advantages and specific local legal considerations pertaining to employee, distributor and agent contracts.

Model selection needs to account for these and optimize the chance for achievement of these goals in addition to rapid market penetration.

A Myriad of Options

Many companies adopt a single model across all regions. That certainly simplifies planning and management, but is it the best way to proceed? In many cases a more nuanced approach and market specific model is preferable. That's not to say that most markets might not have similar models – no doubt distribution is common, effective and economical – but it need not be the same in every case, and depends to some degree on the product and service being offered.

Normally the local channel model takes one of the following forms (ranked below approximately by magnitude of initial investment and ongoing fixed costs, operational control and liability/risk exposure):

- Incorporated local entity – subsidiary (either formed or acquired depending on budget, objectives and time frame)
- Joint Venture
- Employee/Contractors
- Licensing / Franchise
- Distributor
- Agent/Representative (either individual or organization with several Reps)
- Remote sales person/force from a nearby market or home office

Understand that reduced exposure doesn't mean "no" exposure. Particularly in areas of FCPA and export compliance; you may still be held responsible for actions which you should have reasonably anticipated, regardless of any "veil" you assumed your selection of foreign entities provided.

Have Your Cake and Eat It Too

Assuming there are no compelling strategic reasons to have a presence on the ground, (see "Putting Down Roots" below) then your goal is to have as active a presence as possible; maximizing profits and while minimizing risk.

Therefore a model which transfers ownership in the US (ideally FCA or EXW) to a trusted and creditworthy regular foreign trading partner is ideal. This entity is generally a distributor. With this model, local receivables credit risk becomes theirs, as does the cost and risk of transport. (Note that careful understanding of Incoterms 2010 is critical to negotiating an equitable arrangement)

Distribution is often the preferred model. It is relatively quick to establish (although identifying, interviewing and selecting a distributor with aligned focus and interests takes time – read our white paper "Six Critical Phases of Channel Management") and it offers rapid market penetration (distributors already have active customers for related products) with minimal cost (discounts from sales) and exposure.

It is a safe 'default' option for companies new to export and eager to limit downside but still determined to aggressively penetrate new markets.

Putting Down Roots

There are several realistic business situations, however, which would strongly indicate selection of an incorporated local entity. These include:

- **Desire by owner to establish locally held assets (corporate, personal or both) to diversify between jurisdictions**
- **Objective to establish a regional base of operations in a favorable tax jurisdiction**
- **Establish value added assembly in an otherwise high import barrier market, or production for products with distribution constraints (In cases where contract assembly isn't appropriate)**

In all of these cases, however, the previous step of market selection and identification will drive the first two choices and the latter will be integral to corporate strategy.

Beware of transfer cost traps and understand the consequences of repatriating profits vs. not. There is a lot to consider, especially in light of revised FBAR reporting requirements. Involve your domestic legal and financial advisors when developing your plan.

Keep Your Options Open

Business evolves. That's no revelation to you but it's important to keep in mind as you embark on this new pursuit. It is critical to retain flexibility – of model and of partners. One of the unseen hazards of international business is the different and "foreign" legal frameworks which you will confront in different markets.

Particularly complex can be labor and contractual issues. Therefore, it is imperative to seek competent legal counsel, accounting & HR advisory services early in the process. It is not uncommon for casual comments made during initial meetings with potential reps or employees to have long lasting and binding consequences – it's not just the final formal document that needs to be scrutinized. Make sure you understand the minefields that are created by an environment different than that in which you have traditionally carried out your business.

Remember that your goal is to grow aggressively, so be sure to build contingency flexibility into your model and agreements. You may start with distribution and if everything goes smoothly then consider establishing a local subsidiary. So, make sure you don't foreclose that option. Do not enter into a JV with a partner with whom you have, by necessity, only cursory familiarity. Be sure to have clearly defined and reasonable guidelines for extracting yourself from the commitment.

And of course ensure that you are clear on the realistic enforceability of any agreements, as well as what remedies would be available theoretically and practically. Contract stipulations calling for injunctions, that in reality may take 10 years and lots of money to adjudicate, for instance, should not be your focus.

One Part of the Channel Challenge

Please read our white paper "Six Critical Phases of Channel Management" for more information on the details (selection, development and management) of this important aspect.

About Consilium Global Business Advisors

Consilium assists companies in increasing sales and profits through global business development. The Consilium Method uses a selection of advisory services synthesized into a unique export assistance solution, which includes—Marketing Localization, Market Selection, Product Localization, Channel Model Selection, Business Development, Process Management, Government Relations, Commercial Diplomacy and other operational & administrative functions. The Consilium Model is a "big company" export model tailored for SME accessibility. With substantial real-world business experience spanning industries and regions, the Consilium principals deftly guide clients through meticulous strategic planning, comprehensive preparation, and side-by-side market execution. Clients benefit through increased revenue and profit, business stability and survivability. Diversification through carefully selected emerging and established markets also enhances enterprise value through international penetration and growth management.

Consilium is well positioned to help.

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