Think Like a Specialty Manufacturer

By Gary Smith and Jody Nava

This article is a brief discussion of the history and structure of the automotive parts business, and offers a line of thinking as to why it is financially appropriate to view the operation of an electrical rebuilding business from the point of view of being just another auto parts store.

As an auto electric rebuilder, you are a member of the replacement automotive parts industry, and as such you are to some degree governed by the economic rules and practical realities of the parts distribution business.

As a member of the parts distribution business, some of your largest competitors are parts stores. By the same token, if you position yourself correctly, and the mix of personalities is favorable, some of your largest and most loyal customers can *be* auto parts stores.

Much of the turmoil that currently is afflicting the electrical rebuilding industry is a result of the fact that a "step" in the pricing structure is being eliminated. Economics and "global entrepreneurialism" is not going away, and the reality is that this change will continue to fruition. However, if you think this is difficult, realize that the auto parts industry went through this in the 80s and early 90s, and further, is now going through changes that may well make pricing appear as though a portion of another "step" is being eliminated.

As an auto electric rebuilder, you are what could be accurately described from an economic perspective as a "hybrid" or "specialty" manufacturer, meaning that you don't nicely fit in any one business category. The reality of the situation (with all of the whining and moaning set aside) is that if you position yourself correctly for your individual marketplace, as a specialty manufacturer, you have some distinct advantages that auto parts stores do not.

Parts Distribution Marketplace

The parts distribution marketplace is a rat's nest of competition and cutthroat marketing. If you don't think so, just look around. Parts stores are on every street corner (metaphorically speaking) in many communities. Replacement parts can be bought anywhere, and if you search with any effort, whatever you are looking for in the brand that you wish to purchase can be found somewhere else for less cost.

It is a commodity market: product is readily available, and for many product lines and product groups the major element of differentiation is price. If you want to find a good place to work where it is hard to make a buck, try the auto parts business.

As an auto parts store, you have to purchase your finished goods for resale completely up front and hope that someone walks in the door and wants to purchase them.

As an electrical rebuilder, you do not have this full burden. As an electrical rebuilder, you have to purchase the manufacturing (raw materials) components of the manufacturing or rebuilding process, but you do not have to purchase the finished goods. You produce the finished goods.

It is important to note that the largest parts players (read AutoZone and CarQuest) are trying really hard to pass the flooring cost of product to the manufacturer. Time will tell how successful they will be with this strategy.

Parts Pricing

For more than 40 years, the parts industry has used basically the same pricing format for component pricing. How this pricing is applied has changed, but the nature of the pricing structure has remained intact for a very long period of time.

Specifically, there are five price definitions that are commonly used in the distribution chain: list, user, dealer, jobber and WD (warehouse distributor). Historically, the important price definitions have been dealer, jobber and WD. In today's marketplace, the important price definitions are jobber and WD.

Note that this does not mean everything sells at these prices, but these are the numbers that are most commonly talked about. WD (which is normally defined as a percentage discount below jobber) is the price at which a manufacturer sells product to his volume distributors.

Note that for his largest distributors, a manufacturer may define WD as a larger discount from jobber, and for his smallest distributors, a manufacturer may define WD as a smaller discount from jobber. The reality is that volume always matters.

Jobber price, from a historic perspective, was the price at which a WD sold product to a parts store. While some amount of this practice remains in today's market, jobber price today is normally defined as the price at which a WD sells product to his "preferred" customers. These customers may be parts stores, large installers, small installers or most any other category that someone in marketing may decide to pursue.

JODY'S COMMENT: Jobber price is basically what rebuilders pay for the product. Considering that some WDs are selling direct to the rebuilder's customers at jobber means the rebuilder cannot compete and stands a chance of losing the sale/customer. Also some of the larger truck dealers are selling at jobber to the public.

GARY RESPONDS TO JODY: If a rebuilder is purchasing a finished goods product from a WD, then yes, he will likely be paying jobber price or jobber less a small discount. However, if a rebuilder is *rebuilding* a unit, from a core (that essentially becomes an exchange item or is an additional item billed separately), and he uses sub-component materials appropriate for the quality of product he is trying to compete against, then his cost basis in product (sub-component materials plus his labor) is going to be less than WD, unless he is either using a really dead core (a separate problem) or is building a better product than that of his competition.

Remember, WDs and large truck dealers are purchasing this product from either a rebuilder or as new product. Assuming that it is a rebuilt item, this means that another rebuilding business has already done exactly the same things that our subject "rebuilder" is going to be doing. The only benefit that the large rebuilder has over the small rebuilder is "economy of scale;" in other words, volume.

This large rebuilder's profit markup

to the price (WD) at which he is going to sell this item to his most favored customer is a lot more than the benefits of his additional volume.

There are all sorts of games that go into a printed price list. Some raise prices and fatten margins. These lines are usually heavily discounted. Some lower margins and lower prices to create a "realistic" price structure. In the end, you need to know the line and the pricing philosophy to make sense of the price list.

JODY'S COMMENT: What price sheets are we talking about? I have not seen a printed price sheet from any major manufacturers (Bosch, Denso, etc.) in years. Maybe my WD is just not giving them to me but I think more than likely the manufacturers are no longer producing them like they used to.

GARY RESPONDS TO JODY: All of the major (and most larger minor) rebuilders and OEMs publish a price list. Now, granted, in today's society the "printing" of a price list is often done electronically, but the reality of the existence of this pricing structure is just as real. Also, in today's world, I am aware that a few manufacturers are only quoting a WD price. This really doesn't change anything. The WD is still going to mark up his cost some significant amount, and his customer whether installing or reselling is going to do the same. All of a sudden, you again have a price structure.

I have said before that I would not use the Electrical Rebuilders Association (ERA) seminars or this form of dialogue as a stage for trying to sell the Apptrak program, but I need to use it now as an example. To my knowledge, Apptrak is the only product available in the electrical aftermarket that attempts to provide basic tools to a user that will give them information to be able to see and understand "published industry pricing" and quote prices to their customer accordingly. Regardless of who provides it, this is very important information for the informed rebuilder.

Trust me, no one makes this easy. Most manufacturers and rebuilders have very little interest in having anyone other than their customers being knowledgeable of their pricing policies. But the reality of the parts aftermarket is that sooner or later everything becomes public knowledge. No manufacturer provides us their pricing data. We get the information from wherever we can…but we get it…and we work at it.

In my opinion, this is the most important information that any rebuilder, of any volume, needs to have in order to be able to appropriately and competitively price his product. Without comparative pricing information, anyone in any industry is simply walking around in the dark. Bottom line: If you want to price your product competitively, then you need to know what the competitive price really is.

JODY'S COMMENT: I agree that you must *know what your competition is selling their product for. For those of us that compete with the parts stores on every corner you can access this information on the Internet. AutoZone, Advance Auto and other major parts stores offer online stock and price checking.*

I have not gotten very far on my latest idea but it falls in this area of pricing so I will toss it out here. As we all know most of the auto parts stores offer different levels of pricing based on the quality and warranty that comes with the unit. So if you buy the premium (new) unit it comes with a "lifetime" warranty (what they mean by lifetime is another subject). If you buy a mid range product they offer a one-year warranty, if you buy a discount brand they offer a 30-day warranty.

So why don't we, as rebuilders, offer this type of pricing level? Let's say you sell a Delco CS130 alternator to a cash customer. You normally sell this unit for $95 exchange and your warranty is one year. Let's say the customer wants something cheaper. You know that the parts store down the road sells their discount brand for $85 with a 30-day warranty. Why not offer your units for $75 with a 30-day warranty? Let's say it cost you $30 to build the CS130, you have paid for your production and made $30, at the same time you know your unit will last 30 days and after that you have cut your warranty liability to nothing. We all know the one thing that costs us the most is warranty.

Parts Distribution History

In the 60s and 70s, parts distribution was pretty clean. The sales distribution looked a great deal like the price sheet definition referenced above. Margins were good and most everyone was making money. Small jobbers with enough volume and the correct mindset were already buying direct as WDs and were enjoying very good margins if they were good enough at management to maintain good inventory velocity.

Enterprising individuals had already started the large chain retailers and they were proliferating rapidly, but the structured chain of distribution was not yet broken.

In the 80s the emergence of the two-step WD (meaning a WD who sold to installers) came into full bloom. Traditional parts stores really began to feel the heat (in medium and large sized communities) and many of the marginally profitable parts stores headed for the exits. The large chain retailers continued growing. The traditional chain of parts distribution was now breaking rapidly.

In the 90s, the two-step WD became king, the small jobber continued to wither, and as the two-step WD prospered he was also feeling greatly increasing demands for full customer service. In other words, his customers were now expecting him to behave just like the old fashioned parts store, but keep his prices low.

The large chain retailers were still growing, but not really experiencing market growth, as much as they were experiencing business growth through consolidation and acquisition.

JODY'S COMMENT: This is the prime area that we as local rebuilders should use to grow our business—customer service. Over the past year I have picked up several large accounts in the next town. One of their chief complaints is that the WD that was selling to them could not offer any technical help and were not the best at customer service. Sure they had good prices, but I was still able to compete, and I offered the service they wanted. Even though pricing is important, the customer is still human and they want to be made to feel they are the most important person to you! You give them *that feeling and they will overlook the price difference if it is not outrageous.*

GARY RESPONDS TO JODY: Jody has hit the bullseye! Price may well bring a new customer in the door, but over time (meaning repeat customers) price will seldom (by itself) keep them in the door. In the end, it is people dealing with people…solving problems and finding that middle ground where both parties save face (meaning make a living or make a reasonable profit).

Compared to 99 percent of the parts stores in existence, the automotive rebuilder has so many advantages in this area of the sale (when it involves starter and alternators) that used correctly, this advantage can make the rebuilder a very worthy and overpowering economic competitor.

In my experience, price is seldom the only determining factor in the purchase decision. While some people are only interested in "how much," I have found that most people realize that nothing is free, and that when given the choice many people will choose a higher level of service and be comfortable with an appropriately higher level of price.

As we get our feet firmly in the first decade of the 21st century, the situation has not changed much from the late 90s.

One thing that has changed is there are now fewer two-step WDs, as the weak ones are being culled out just like the weak jobbers were culled out in the 80s. The largest chain retailers are trying to shift the cost of inventory flooring to the product manufacturer, while at the same time the product manufacturers are consolidating or growing through acquisition. It is reasonable to construe (and in fact solid examples of this are already clearly visible in the market) that manufacturers will come up with hybrid solutions to distribute or share the costs of inventory flooring while using this as a tool to protect their market share.

What Does This Mean?

There are two distinct types of rebuilders: volume rebuilders (truly a manufacturer) and specialty rebuilders (a hybrid manufacturer). You decide which category you fit in. The intention of this dialogue is to address the specialty rebuilder.

So…you're just another parts store in a competitive industry. What makes you any different?

Actually, several things make you very different. First of all, on a cost basis you have the ability to be closer to a manufacturer than a WD. Don't kid yourself, this is a big advantage—but only if you use it to your advantage.

Note I said you have the "ability" to have a cost advantage. This does not mean it is necessarily easy, but it does mean it is an attainable advantage if you manage your affairs carefully. Any advantage in business (properly executed) is a benefit.

Secondly, you have an advantage in flooring costs. Your costs of acquisition are generally (not always) limited to the costs of the raw materials and labor in your finished goods. This statement assumes that you appropriately manage your labor costs, but it is still an attainable advantage. In comparison to the typical auto parts store, as a rebuilder, you are already two steps up.

Third, you have the ability to be an on-demand manufacturer. A parts store does not (generally) have this ability in any form. He has to order the part (from somewhere else) and get it shipped to himself or to his customer (a delay in time). One of the oldest axioms of the parts business states that "All other factors being the same, local availability always wins." This statement is as true today as it was 40 years ago. The only thing that has changed is freight delivery is faster. This is a very big advantage for the electrical rebuilder, and is an even bigger advantage if you really use it and effectively market it.

So how do you use these advantages? First, get your priorities straight. You do not get paid for rebuilding! I know this is going to come as a shock to some of you, but it is the truth. You get paid for selling product! Most every person who calls your business or walks in your door is looking for a solution to a problem. That solution, in most cases (those exceptions are another place where you can have an advantage), involves providing a product.

Like it or not, you get paid for exactly the same things that the parts store does. That customer has many places to go to acquire that product. This is where your revenue stream comes from. If you are not clear on this, then this is the first thing you need to figure out. Once you are past this, the rest of it gets easier.

If you are not comfortable selling things to people; if you are not comfortable asking people to purchase things from you; if you are not comfortable in valuing your services and being able to explain to potential customers why your services are of value to them; then you are putting yourself in a position of disadvantage.

If you have gotten past the above paragraphs with comfort, then the rest is just execution.

In the parts business, you do not sell a profit, you buy a profit. What this means is there is only so much you can charge for a given product, and if you cannot buy it or produce it at reasonable profit based upon your marketing objectives, then you cannot make a profit on this item, and you may want to question under what circumstances you wish to pursue selling this item.

The idea that "there is only so much you can charge for a given product," strongly infers that you need to have a clearly defined and structured plan for product pricing. Further, this pricing plan needs to give appropriate consideration for the pricing strategies of your local competitors. If you have not done this, then you are only guessing at what to charge for your product.

It is far wiser to quote prices to your customers that position your product in line with your marketing wishes...and consistently project that image. If you quote prices that are too high, you drive customers away and your revenue stream suffers; if you quote prices that are too low, you get the sale but your revenue stream again suffers. This may seem like a daunting task, but there are tools available to help.

JODY'S COMMENT: In some respects you may want to consider NOT competing with the local discount houses, I don't, although as noted above I have started thinking about it. I think that most of us are of the same mindset that the product we make is better than the *product from a discount house (although this mindset could be a problem). With that in mind though you have to learn to "sell" your product when price is a consideration to your customer. Sell your service, your knowledge, yourself. In the same respect a lot of times I hear from my customers that I have better prices than the parts store, I have found that you never know what they are selling their stuff for.*

GARY RESPONDS TO JODY: Jody is absolutely correct, though I might phrase it slightly differently. Auto parts stores do *not* sell everything in their store to every customer at their lowest possible price. Volume matters. I agree regarding the necessity of projecting an image of "knowledgeable professionalism," and of taking advantage of the market opportunity of selling a "better quality product." I agree that it is necessary to "sell" a better product.

But with all of that said, any business operator also needs to be "pricing aware." If you offer a clearly superior product to a knowledgeable or caring consumer, then you may well be able to add another 30 percent to the price tag. But there is a point of diminishing returns, beyond which a product simply will not sell…and you can't know that point of diminishing returns without knowing pricing and your market.

Once you have a pricing plan in place, consider your "cost of manufacture" in relationship to your "manufacturing capacity." If you need to price 3510s in your market at a price point where it is difficult for you to build them profitably, then consider not building them. Note that I did not say *not* to sell them. I suggested not building them.

Note that I did not say not to sell them. I suggested not building them. Find a source for this product (with sufficient economies of scale) that suits your quality desires and purchase/resell the product. For popular high volume product, there is a world of choices and options. If you are a small shop, then by nature you will have limited "manufacturing capacity." It makes little sense to build low profit units if you are struggling to keep up with demand for higher margin (read industrial and low selling volume) units.

JODY'S COMMENT: When you are a one or two-person shop as we are you have to know what makes the money and what doesn't. In our case one of those things was Lucas starters. I have never built one and Robert doesn't like to build them so I buy them. In most cases I can buy them for a fair price and sell them and make a nice profit. Everyone is happy.

From a marketing point of view, your intrinsic advantages over a parts store are that you can move quickly with greater knowledge over a wider range of product. If you are diminishing your ability to market these advantages by allocating limited time to the manufacture of low margin product, you are hurting your own business.

A last important tenet of the parts business is inventory velocity. In short, finished goods inventory (or to some degree manufacturing components) that sit endlessly on your shelf are not paying their way. If you view inventory as you would fresh fruit and vegetables, you will get the idea. If fruit sits too long it spoils. In the case of inventory, stagnant product produces no return, and in a world of limited resources you would likely be much better off to position your inventory dollars elsewhere. There are various methods of resolution, but the act of keeping your inventory fresh and clean is paramount to successful business operation.

JODY'S COMMENT: Eighteen months ago we moved our shop. Prior to moving I went through our completed units and pulled everything that had not sold in over a year and put it aside. When we moved, that product went to a special place in the shop—not on the shelving where moving product went. We made a list of all this and took it out of our inventory. It was a very eye-opening experience to see the amount of "dead" stock we had.

Now every six months or so I try and do the same thing. I evaluate what is not moving and remove it, or if I do sell it I don't rebuild the core. Why build a core when that unit had sat on my shelf for over a year to begin with. Build what sells.

This also goes for parts. We culled out dead parts as well and boxed them up and put the list on the top of the box and made a master list. It only takes a second to cross it off the list when you get lucky enough to sell something. I try to do a stock return at least once a year, twice if I can. I am currently in the middle of this task and must say that we have kept up rather well and do not have that much dead stock.

When you do a mass culling of inventory ask your accountant about writing this off on your taxes and removing it from you financial statements in order to reflect a more accurate inventory figure.

My last thought: I am sure that most readers have been in business a lot longer than me, but over the past 15 years I have been doing this, and the 10 years my dad did it before me, we have acquired several very loyal customers as I am sure you have. I have found that those customers (and these are special customers, not just any customer, you have to trust them) are willing to help you; they want to see you succeed and they would rather buy from you than some large parts house.

In the past I have asked a customer or two to help me with price checking, application books, etc. They are very useful sources of information because they have their finger on a much larger picture of the parts world than we do. We just see what's going on in our end of the pond, and they have their feet in the whole pond. They are also your peers. I find they are great sources for business information, advice, and advertising ideas, or just to sit and have a chat with.

Earlier I made the remark "if you position yourself correctly and the mix of personalities is favorable, some of your largest and most loyal customers can *be* auto parts stores." Your local parts stores see a lot of people in their day that they have to turn away because they do not have the part on the shelf. Therein lies your opportunity. Nurturing a relationship here may well be to your benefit and may be a source of ongoing monthly revenue.

Yes, you will need to "share the profits" because you will need to offer him enough room to make a small profit for his time. But in a healthy relationship, you can see business from him month after month. He may even refer business to you, perceiving you will treat him similarly. You may already know these people well. This makes it all the easier to make a sales call. Ask the manager or owner out for lunch. As my father taught me: “Half of something is often a whole lot better than 100 percent of nothing.”

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