WHITEPAPER

5 STEPS HOW TO FIND AND EVALUATE EUROPEAN DISTRIBUTORS

ABSTRACT

This whitepaper explains how to evaluate specifically European distributors. Furthermore, it answers to the questions as how to overcome factors that may influence your choice of distributors in Europe, which particular type of distributor you need, how to introduce and conduct evaluations, how to handle payments for distribution, and safely ship your products to Europe as well as how to deal with good returns.

INTRODUCTION

When expanding businesses to Europe a company can consider several alternatives among which the very popular 'going it alone'. However, many U.S. companies struggle with cultural, economic, political and legal differences, as among others involve HR, regulatory requirements and CE markings. For that reason an expansion to Europe often results in lost opportunities and disappointing sales. Therefore, in case a U.S. company strives for European business presence, the option of allying with a European industrial distributor should be taken under consideration. Having a European industrial distributor provides advantages since it has the knowledge and the ability to deal with these differences. In addition, it probably already has the network and access to distribution channels as required by the U.S. company. This implies that linked activities of the U.S. company and a European industrial distributer most likely result in a cross-border synergy. However, many companies overlook the importance of thorough research and screening of possible distributors. This paper serves to guide companies through the process of finding and evaluating distributors in the European Union.

FINDING AND EVALUATING DISTRIBUTORS

STEP 1: RESEARCH THE MARKET POTENTIAL

The first step for U.S. companies is to identify the following: Current competitors in Europe; where these competitors are concentrated; how its product compares with their competitors' in, among others, quality and cost; whether or not reimbursement is of significance; how well served each of the European markets is already, and what is the future potential in these markets. When having trouble in identifying the previous, one could look into the five forces that shape industry competition as defined by Porter. Thereby should be noticed that there are a lot of differences within the European market as well.

Europe is both a lucrative and challenging market. U.S. products are well respected and innovative products are in high demand. For the last several years the exchange rate has favored U.S. companies, making U.S. products much more attractive to European buyers. In addition, Europe's population of over 490 million people is 60% larger than the United States. There are approximately 67 million people over age 65 in Europe compared with 36 million in the U.S. All of the abovementioned factors contribute to the appeal of the European market; particularly for U.S. companies.

STEP 2: PENETRATE SPECIFIC COUNTRIES

Upon entering the European market, most companies gravitate towards Germany, France and the UK because of their size. In fact, these three countries account for nearly half of the combined population of the European Union. The disadvantage to selecting these markets, however, is that they are very competitive and have fairly stagnant population growth. Depending on the product and the market dynamics, it may be beneficial to look at smaller, second tier markets (e.g. Spain, Poland, Czech Republic). Often, these countries are not as well served and have good growth potential due to rising incomes and other factors. It is of utmost importance to keep in mind the uniqueness of the European market. The European Union is comprised of 27 different countries (plus Switzerland, Norway, Liechtenstein and Iceland which are not part of the EU) and 20+ official languages.

Although the EU has come a long way in harmonizing regulations among member states, and the movement of goods among EU countries is unfettered, each has its own laws, languages and cultural values. Many people do not fully appreciate these differences and sometimes leave the market in frustration.

STEP 3: SELECT A TYPE OF DISTRIBUTOR

After the U.S. company has determined which countries make the most sense for their company, the next step is to determine which type of distributor is best suited to meet their needs. For instance: Is the product relatively simple or complex? Will the product need servicing? Does the company want initially to market in one or two countries? Or is it imperative to have widespread distribution from the outset? Is the product new and unique to the European market; or is it a high volume, low margin item?

Often, companies feel pressured because of time constraints, skip due diligence and enter into an agreement with the first opportunity that presents itself (e.g. meet a distributor at a trade show). Determining which industrial distributor would best serve the U.S. company, however, depends on the answers to the questions above. For example, if the goal is to focus on one to three countries and manufacture a fairly simple product, smaller distributors may make the most sense because they may better cater the company's needs.

In contrast, if the U.S. company wishes to get started in numerous countries and has a fairly complex, high margin product that requires customer and technical servicing, a master distributor with an established pan-European service network may offer the best option. It is important to conduct a thorough due diligence assessment on, among others, market research, developing distributor profiles. This means that one distributor, instead of several national distributors, serves the complete European market. Having such a distributer means all linked activities have to occur once, instead of several times with different distributors. This greatly simplifies the activities and processes involved with the expansion to Europe.

Another common misconception is that a product's success in the U.S. signifies immediate success in the European market. Unless the product is truly revolutionary to the market, the U.S. company must "sell" the product before it will be profitable on the market.

STEP 4: PREPARE FOR INTRODUCTION AND MAKE AN INITIAL CONTACT

Once the type of distributor and which countries the U.S. company wants to target have been determined, the U.S. company will need to make an initial introduction to the selected distributor. Thereby the goal is to introduce the company, outline what goals the company is looking to accomplish and what the benefits of the product are.

In addition, the U.S. company should take this opportunity to request a time to speak in more detail. If the device-related literature is not already translated, it should be done at this time by a specialized professional firm. However, it might also be the case that the contacted distributer not requires a translation (especially in Western-Europe most people are able to communicate in English).

STEP 5: ENSURE THAT THE DISTRIBUTOR IS INTERESTED

Once a dialogue has been established and the distributor has expressed interest, the U.S. company should ask the distributor what types of similar products they sell already, how long they have been selling in the market(s), what are the percent of their sales from the U.S. company's target market, and how they would promote the product. This is a crucial step because it will help the U.S. company ensure that the distributor is interested and excited about their product, and also if the distributor is the best fit for the U.S. company's company and culture. As an example, an important factor to keep in mind during this informal evaluation is the branding image which the company portrays, and how this distributor will maintain that image.

The U.S. company should also be prepared to answer a series of questions by the distributor, who will want to assess that they too are conducting business with a reputable company that makes a quality product and will be able to deliver a reliable supply on time. Finally, customer references should be checked to assess the satisfaction level of their current clients.

BEING AWARE CULTURAL DIFFERENCES

Differences in how business is conducted cross-culturally exist, and are quite profound in certain countries in Europe. Though the U.S. and Canada are very homogenous business environments, in Europe, the French are quite different in their approach to life and business than, say, the Spaniards or the Germans.

In the Netherlands, for example, about 75% of people speak English. In Italy only 28% of people speak English, and in Spain, only 18%. In total, about 47% of people in Europe speak English, at least enough to hold a conversation. Therefore, having someone on staff that is experienced with international business (or calling upon outside resources with business experience in Europe) is critical. Understanding the nuances of the different business cultures can have a big impact in determining whether the U.S. company's business and products will flourish or languish in Europe.

SIGNING A CONTRACT

When it is time to sign a contract with a distributor, U.S. companies should be wary of the issue of exclusivity. The decision to sign a contract for product distribution with an industrial distributor that will only agree to distribute the product with the stipulation that they have exclusivity, is one that requires due diligence. Exclusivity should not immediately raise negative connotations, but again, it is a matter that warrants attention and thorough research.

With terms of an exclusive contract, the distributor may put more focus on pushing the product. However, it is important for the U.S. company to evaluate what will happen in the event that the distributor does not market the product as promised; or if a better, more suitable products distributor is located after the contract has been signed.

Make sure the contracts clearly define the sales regions for distribution of the products. For example, if a U.S. company were to establish products distribution with a new distributor in France that is also strong in southern Germany and the U.S. company already has an exclusive agreement in place with a distributor for Germany, the contract with the French company should specify that the territory covered is France only.

Other important issues to consider are: The conditions under which the contract can be cancelled (e.g. minimum service levels, sales levels); how products will be returned; and what are the conditions of sale, legal governance and other standard issues. To this end, it may behoove the U.S. company to explore the "handshake agreement" and try things out for six months before agreeing on a contract. Sometimes this is the best way to get things moving quickly.

HANDLING PAYMENTS

For purposes of simplicity, three common payment methods are discussed: Payment in Advance, Letter of Credit and Terms. Each represents increasing levels of risk to the exporter. The three methods are described below.

PAYMENT IN ADVANCE

Payment in advance: the distributor pays the U.S. company up front before the shipment leaves the loading dock. Typically, this is done through wire transfer and is generally only done in the early stages of working together, before trust and rapport has been established.

LETTER OF CREDIT

The second option involves a Letter of Credit (LOC), which is often used for larger orders but protects both the exporter and the buyer at the same time. LOCs are letters issued by banks to authorize the seller to collect money from the buyer's bank account only if certain conditions set forth in the letter are met (e.g. proof that the products were shipped).

OPEN CREDIT OR TERMS

The final form of payment is called Open Credit or Terms, typically Net 30. Providing terms to a supplier usually happens after the first shipment. However, it is important not to underestimate the risk of utilizing this method. There are many stories of buyers who place several small orders and prepay to establish trust, and then place a large order, ask for terms and then do not pay or pay very slowly. Again, the U.S. company must perform due diligence.

If a company exports from the United States, they should be aware of currency fluctuations and the impact this can have on their market share. Especially if the company is in a price-sensitive category, this could have a substantial impact on their sales in the market.

SHIPPING PRODUCTS TO EUROPE

Before shipments can be made, companies must ensure that all of the proper documentation is in order and device labeling requirements have been met. Make sure to include a copy of your CE Marking certificate along with your shipping documents to avoid problems with Customs. The distributor or freight forwarder can be used as resources for guidance.

Customs officials have the right to hold a shipment if the necessary paperwork is not attached and may even go so far as to destroy the merchandise. Thus, it is imperative that all of the proper documentation, including CE Marking, is in place prior to shipment.

There are many types of shipping methods and it is important that companies determine which method is best suited to their situation.

HARMONIZED TARIFF SCHEDULE

Every product imported to a country is assigned a code according to the Harmonized Tariff Schedule (HTS). Customs officials in the country where the product first enters the European Union will determine the HTS code. This is relevant because the first classification made by a Customs official in the European Union is used from then on to determine the product's rate of duty. Some devices are not subject to any duties. The different rates of duty can be found in the HTS database.

EUROPEAN VAT

The European VAT[1] is similar to U.S. state sales tax and is levied regardless of whether the goods will eventually be resold in the European Union. The distributor will need to pay the VAT (rates range from 15% to 25%), but are eligible for a refund on the amount paid if the goods are intended for resale. Note that governments are often slow to process refunds, so there is a short-term burden for distributors.

[1] Lear more about European VAT system in EuroDev whitepaper "European VAT Fact Guide"

HANDLING PRODUCT RETURNS AND SERVICING

Product returns and servicing are important considerations: Will the distributor handle returns? How will damaged products be handled? If the product is serviceable, will it be returned to the United States for service? If so, what is (United States International Trade Commission, 2011) the cost?

Shipping between the United States and Europe can cost up to four to eight times more than domestic shipping. This is a salient point because for certain products, the shipping and administrative costs outweigh the value of the product.

If the company manufactures a serviceable product, the cost and time associated with product returns and repairs are important considerations in choosing a distributor. For example, if the product costs $900 wholesale, a decision must be made if it is cost-effective to have the distributor return it to the company in the U.S for servicing if the cost for expedited return shipment is $150 (and this does not include the time to repair it and ship it back to Europe), plus duties.

In the example provided below, it may be best to outsource that task to the distributor or a European device repair facility. These decisions, however, depend on the value of the product, complexity of servicing, frequency of repairs, customer service needs and liability issues. It is extremely important for the U.S. company to consider all of the implications before signing a contract.

CONCLUSION

It can be a challenge for U.S. companies to deal with companies in Europe because of differences in time, culture, business practices and language. Companies often underestimate the amount of work involved in nurturing these relationships and end up disappointed by their distribution arrangements and sales in Europe. Depending on the company, U.S. companies may want to consider the option of outsourcing the distribution of their products to an industrial distributer with a presence in Europe. A carefully chosen and evaluated European industrial distributor can thereby provide great advantages.

SOURCE

This paper is based on the following white paper:

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DISCLAIMER

ABOUT EURODEV

EuroDev, established in 1996 with offices in The Netherlands and France, has a single, defining purpose to help midsized American companies expand their business in Europe. We have developed a proven, successful development model; and since our founding, we have partnered with over 150 US companies to help them define and meet their European business goals.

We have four operating divisions:

- **Business Development** - Sales & Marketing in the Industrial, Retail and Healthcare Markets
- **Business Services** - Financial, Administrative and Human Resources Solutions
- **Mergers and Acquisitions** - International Buy Side and Sell Side Engagements
- **Consultancy** - Consulting Resources for all of our Services and Markets

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CONTACT US

Tel: 0031 (0) 546 660 000
Fax: 0031 (0) 546 660 010

OUR OFFICES

EURODEV BV
Windmolen 22
7609 NN Almelo
The Netherlands

EURODEV SARL
473 route des Dolines
06560 Sophia Antipolis
France