

Closing the Execution Gap

How Wholesale Distributors Can Apply Profit Intelligence to Achieve New Levels of Performance

CAVALLO

DISTRIBUTION STRATEGY GROUP

Executive Summary

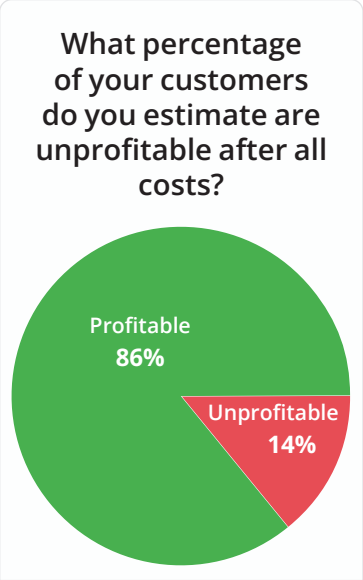
Wholesale distributors face an overlooked profitability crisis. A recent survey commissioned by Distribution Strategy Group and Cavallo, the leader in AI-powered Profit Maximization software, compiled survey data from interviews with 84 industry participants. The survey reveals that while 69% of distributors measure customer profitability, only 34% provide sales teams with real-time access to this data.

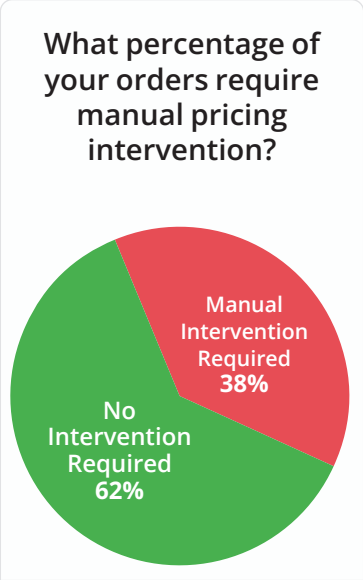
The result: an execution gap that costs the industry an estimated 3-5% of revenue annually or 150-200 basis points in margin improvement opportunity. For a $50 million distributor, this translates to $750,000 to $1 million in recoverable annual margin.

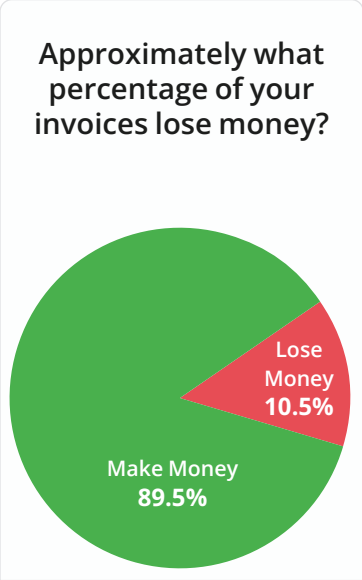
Four sources drive this accumulated margin erosion:

- **Incomplete supplier price pass-through**
- **Manual pricing errors**
- **Small order losses**
- **Unasked-for discounts**

The underlying problem: 41% of distributors cite order-level profit intelligence as their top technology priority revealing that most cannot see profitability at the transaction level where all margin leakage actually occurs. Without transaction-level visibility, customer profitability averages mask individual order losses, pricing discipline remains theoretical, and cost-to-serve analysis cannot inform real-time decisions.







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This research identifies four critical profit leakage points.

- Half of distributors pass through less than 90% of supplier price increases, and nearly 30% pass through less than 75%, resulting in margin that disappears before it ever reaches the P&L. (DSG Distributor Profitability Intelligence Survey, n=69)
- 37.8% of orders require manual pricing intervention, creating unnecessary costs and errors that compound across thousands of daily transactions. (DSG Distributor Profitability Intelligence Survey, n=68)
- On average, 10.5% of invoices lose money at the transaction level, concentrated in small orders under $100 where cost-to-serve exceeds gross profit.
- Unasked-for discounts erode margin when salespeople lack visibility into customer profitability was rated a persistent profit leakage source by survey respondents (2.53/5 severity) giving away profit unnecessarily on a routine basis.

The cumulative result: 14% of customers are unprofitable, one in seven relationships destroys value after all costs. Yet only 10% of distributors use profitability-based segmentation to identify and address these losses.

Technology plays an enabling role: 66% prioritized competitive price monitoring, 46% wanted real-time customer profitability dashboards, and 41% sought order-level profit intelligence. Yet 63% still rely on Excel, reflecting a maturity gap where disciplined processes must be established before technology can amplify results.

Distributors have a 12-18-month window to gain competitive advantage before these practices become industry standard. Early movers addressing all four leakage points simultaneously will not only achieve higher profitability but will also establish ongoing margin discipline before these practices become baseline expectations. This report provides a practical framework with immediate actions deliverable in 30-90 days.

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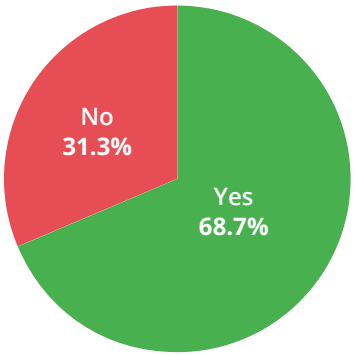
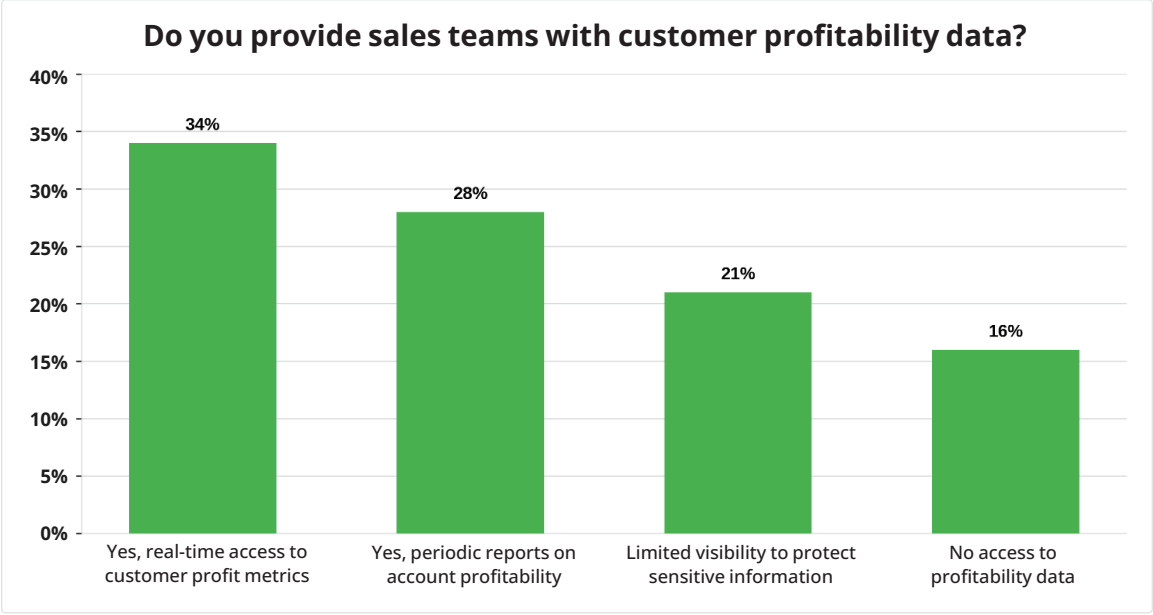
The Profitability Paradox: Why Measurement Isn't Enough

Most distributors measure profitability. Few act on what they learn.

Do you measure customer profitability?



Survey data shows 68.7% of distributors measure customer profitability yet most measure only at the customer level, not the transaction level where pricing decisions occur and margin leakage happens. But measurement without action creates the illusion of control while profits leak away. The issue isn't data availability; it's how and if distributors act on it.



Only 34% of distributors provide sales teams with real-time access to profitability data. Another 28% offer periodic reports that arrive too late to influence pricing conversations. The remaining 38% provide limited visibility or no access at all, treating profitability as sensitive information too valuable to share with the people who influence it the most.

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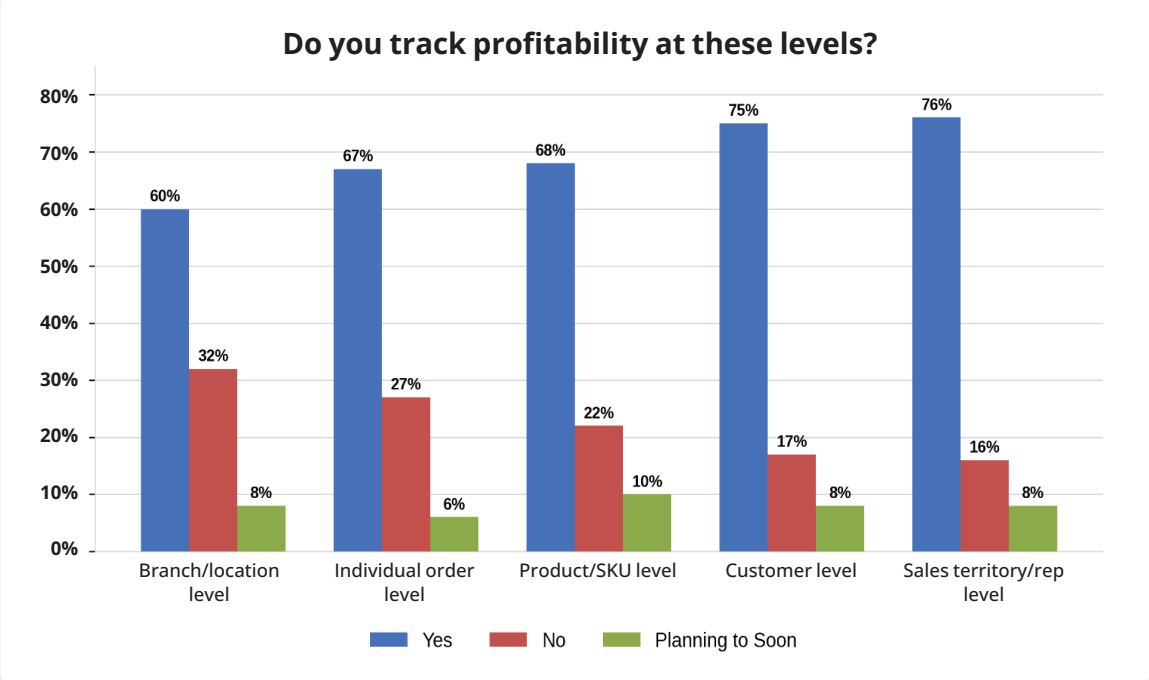

This creates a predictable pattern. Finance teams analyze profitability monthly or quarterly, identifying problem accounts and margin pressure. They present findings to executives who mandate improvement. But sales teams enter their next customer conversation with the same information they had before: last quarter's sales volume, historical discount patterns, and competitive pressure from the customer.

A distribution consultant interviewed for this research observed: "Sales teams quote based on recent experience rather than aggregate company data. Customer service representatives routinely give unasked-for discounts, viewing price as 'another nice thing you give away' rather than how the company gets paid."

When profitability data lives in spreadsheets inaccessible during quoting, pricing discipline becomes a function of individual judgment and memory, neither reliable nor scalable. The CEO of a food ingredients distributor managing 14,000 SKUs described the challenge: "Human error in pricing is our primary profit leakage point due to SKU complexity and multiple pricing arrangements. With nine distinct price points and thousands of SKUs, manual management guarantees inconsistency."

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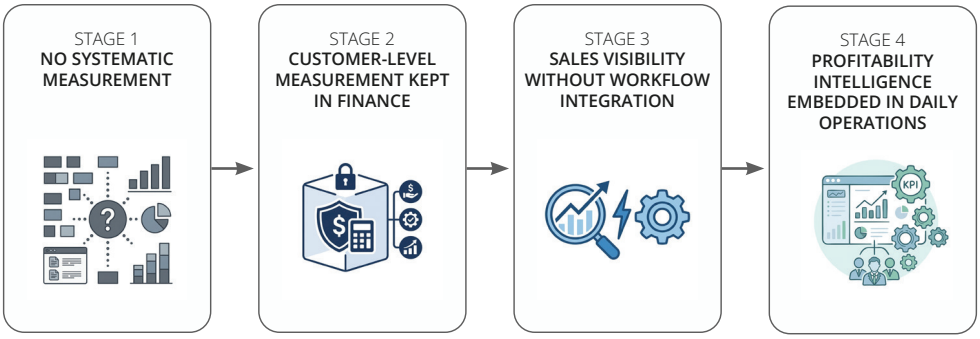
Maturity Gap in Profit Intelligence



The four stages of Profit Intelligence maturity typically begin with limited or ad hoc measurement of profitability, followed by basic reporting that lacks actionable insights. As organizations progress, they develop more integrated systems and processes that enable real-time visibility and analytics.

The final stage is characterized by a data-driven culture where profitability information is embedded in daily decision-making, empowering teams across the enterprise to proactively address margin leakage.

Solutions like Cavallo's AI-powered platform are specifically designed to accelerate this progression by using ERP data to uncover actionable profit intelligence, providing distributors real time insights for decision making. Most distributors, however, are still in the early phases, underscoring the need for both cultural and technological transformation to unlock sustained margin gains.

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Customer Segmentation Redefined: From Volume To Value

Most distributors segment customers by how much they buy. The best segment by how much profit they generate.



Only 10% of distributors segment customers by profitability. More than a quarter (28%) have no segmentation at all, and the remaining majority rely on crude size-based groupings that ignore the single factor that matters most: whether the customer actually makes them money.

A manufacturer who works with multiple distributors confirmed this pattern: "My conversations with distributors show 50% do some sort of customer segmentation, very rudimentary, just strictly based on volume, no other criteria, no other dimension. The other 50% don't do anything. I've talked to some folks that are half a billion dollars that still don't have customer segmentation that makes sense."

Volume based segmentation creates three problems:

1. It rewards large customers regardless of profitability.
2. It treats all small customers identically, missing the distinction between profitable small accounts and money-losing ones.
3. It fails to account for cost-to-serve variations that can exceed margin differences.

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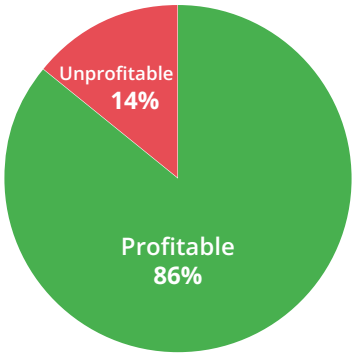
A distribution consultant explains: "They end up giving bigger discounts to the larger customer, creating cross subsidies. They're losing on the big customers and making it up on the small. But when they're making it up on the small, they're not competitive."

What percentage of your customers do you estimate are unprofitable after all costs?



Survey respondents estimate that 14% of customers are unprofitable on average, with individual responses ranging from under 5% to as high as 50% or more. But outright unprofitability is only the most visible symptom. Most companies cannot answer the deeper question: what percentage of their accounts could be significantly more profitable than they are today? Only 10% segment customers by profitability tiers, and 31% don't measure customer profitability at all. Once you factor in cost-to-serve, pricing exceptions, and order patterns, the number of underperforming accounts likely dwarfs the 14% that are explicitly unprofitable.

The Profit-Based Framework

Profit-based segmentation classifies customers into tiers based on their contribution after all costs:

- **A-Tier: High-margin, low-cost to serve** - strong margins with reasonable service costs, order in economical quantities, pay promptly.
- **B-Tier: Solid margin, moderate cost to serve** - acceptable margins but require more support, could move to A-tier through order consolidation.
- **C-Tier: Break-even or minimal profit** - minimal contribution after cost-to-serve, need correction through pricing adjustments or service fees.
- **D-Tier: Value destroyers** - lose money after all costs, combine poor margins with high service costs, require correction or exit.

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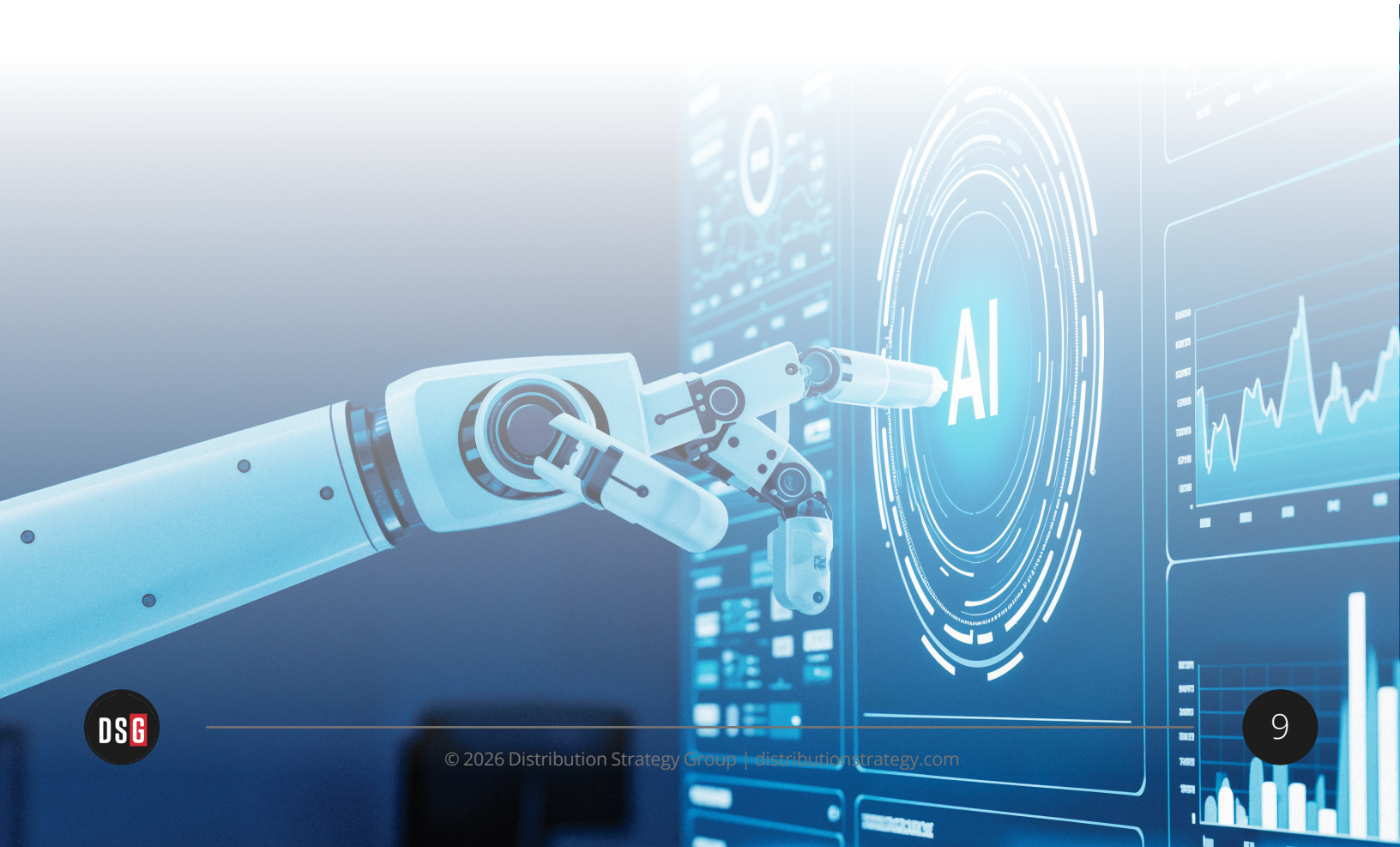
The segmentation process requires three inputs: accurate cost-to-serve data measuring actual expenses (68% of distributors don't systematically measure this); customer profitability analysis incorporating all freight costs, handling, payment terms, returns, and sales support - and ongoing monitoring to account for tier shift as customer behavior changes.

Customer communication matters. Rather than "you're unprofitable, so we're raising prices," successful distributors say, "we've analyzed our cost to serve different order patterns, and we need to adjust our approach to ensure we can continue providing the service you expect." They offer solutions such as order consolidation and electronic ordering that reduce both parties' costs.

Distribution Strategy Group's experience shows distributors who address customer segmentation early achieve 150-200 basis points (1.5-2.0 percentage points) in margin improvement within 12-18 months. For a $50 million distributor, this improvement translates to $750,000 to $1 million in annual margin recovery, often with minimal capital investment beyond the analytics and process changes required to implement the framework. The framework provides the foundation for nearly every other improvement; pricing discipline becomes easier when tiers define appropriate margins.



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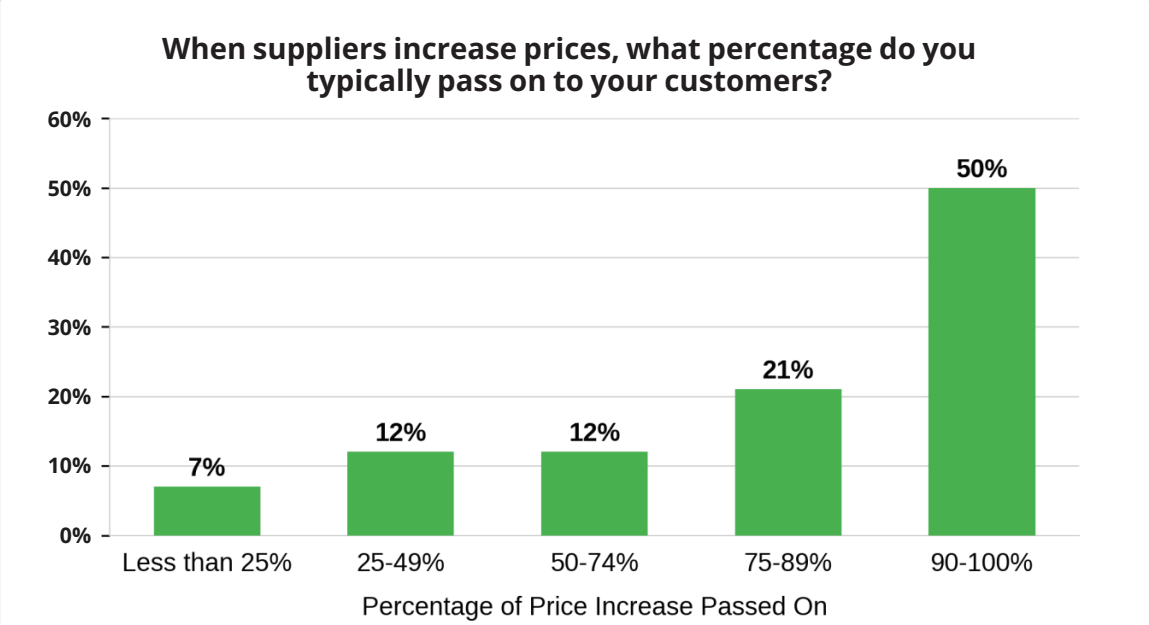
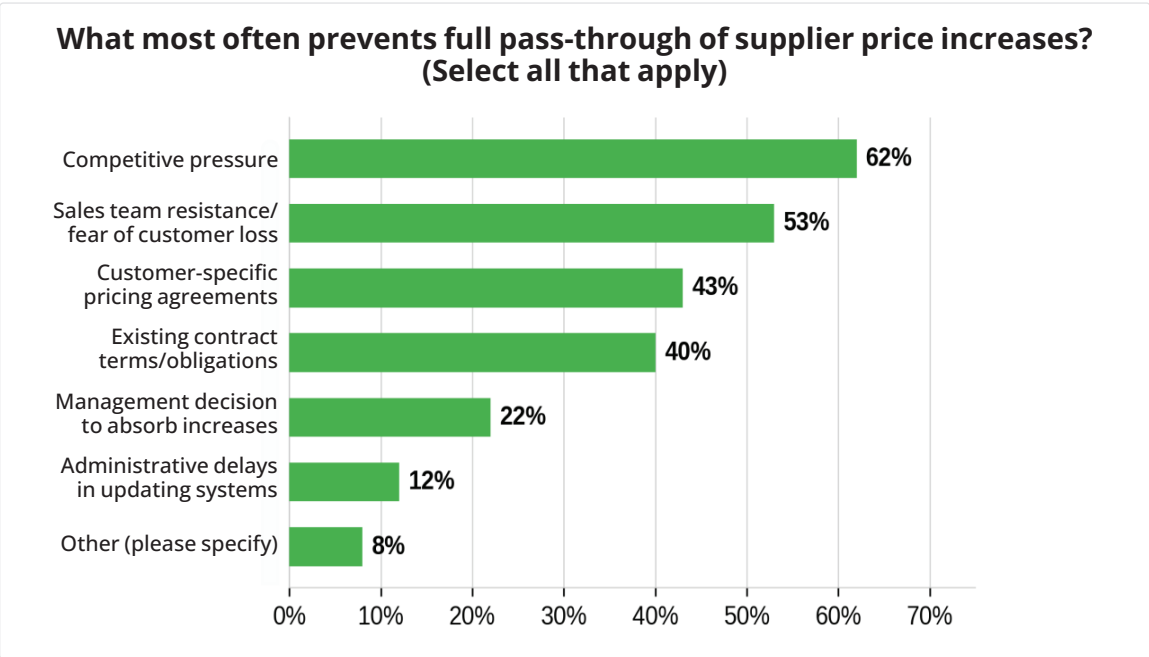
Pricing And Margin Integrity

The Suplier Pass-Through Gap

Supplier price increases should flow through to customers. They don't.



Half of the distributors surveyed pass through less than 90% of supplier price increases. Industry experts suspect actual performance is worse due to normative bias causing people to report how they should perform, not how they do.



Erosion follows a pattern. Competitive pressure prevents 62% of distributors from full pass-through. Sales resistance blocks 53%. The combination creates a predictable pattern. Suppliers announce increases with 30-60 days' notice. Distributors prepare their responses, but execution ultimately fails through sales team exceptions, customer negotiations, and competitive intelligence suggesting rivals aren't passing through fully.

An executive from a motion control distributor described the challenge: "Manufacturer uncertainty about tariff impacts created operational challenges with minimal advance notice, three days in some cases, and no backlog protection. We were forced to implement price changes immediately or absorb costs. Distributors with strong governance handled volatility better."

The Manual Pricing Burden

Survey data shows 38% of orders require manual pricing intervention. For a $50 million distributor, this translates to 2-3 full-time employees dedicated to pricing, annual costs of $150,000-$225,000, error rates three times higher than automated systems, and processing time of 5-10 minutes per order versus 30 seconds automated.



On a severity scale of 1 (minimal impact) to 5 (critical impact), human error in pricing ranked 2.72 among profit leakage points. Sales reps giving unasked-for discounts rated 2.53. While neither tops the scale individually, their combined and compounding effect across thousands of transactions creates significant margin erosion.

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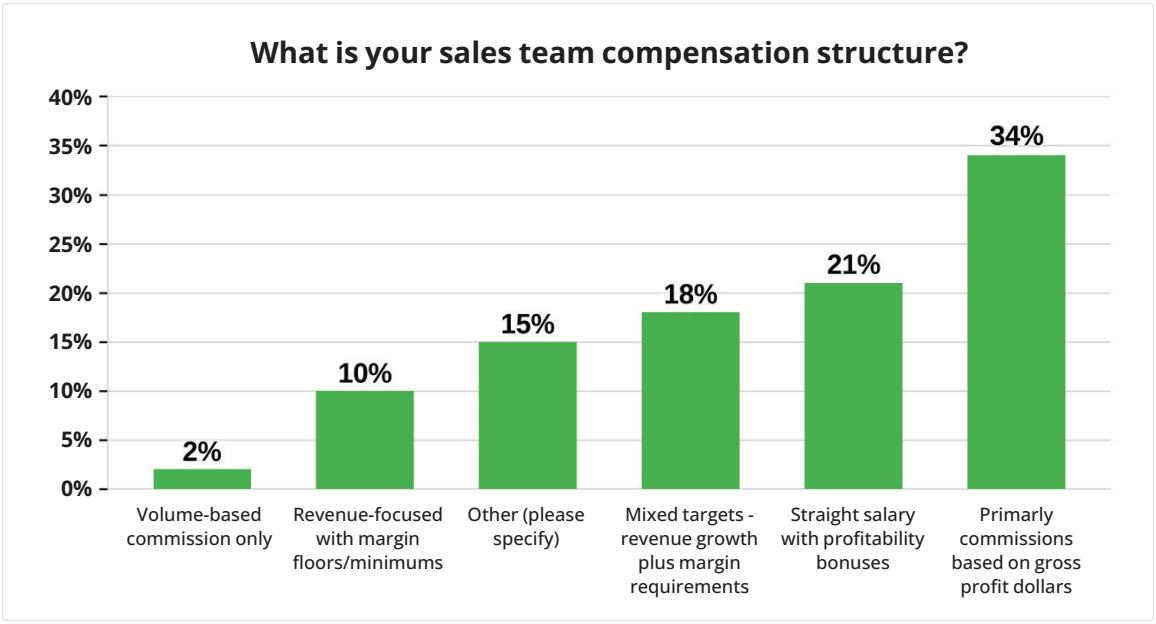

Misaligned Sales Incentives

Only 34% of distributors compensate sales teams based on margin. Distributors that use revenue-based compensation directly incentivize volume over profitability. When a sales rep faces customer price objections, revenue-based compensation encourages discounting to close the deal. The distributor loses margin, the rep hits quota. Notably, the 15% of respondents selecting "Other" overwhelmingly described hybrid base-salary-plus-bonus structures blending revenue and margin targets suggesting the industry is already experimenting with more nuanced compensation models, though few have formalized them into consistent, margin-first frameworks.



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The Four-Part Architecture for Margin Integrity

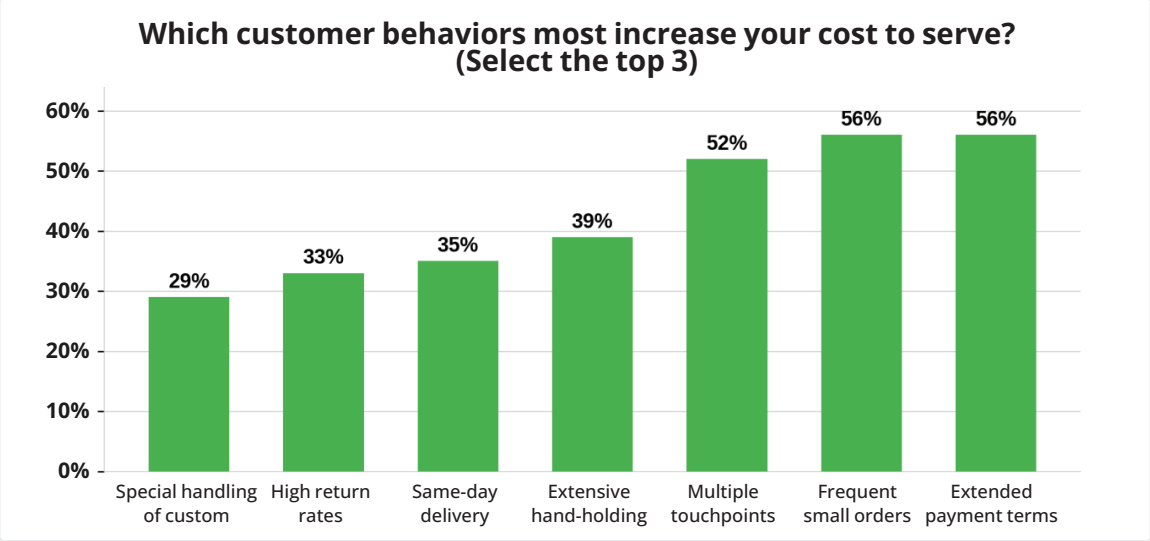
The solution requires four components working together:

- **Automated Pricing for Standard Orders:** Reduce manual intervention from 38% toward 15%, reserving manual pricing for genuinely complex situations.
- **Real-Time Margin Visibility:** Provide immediate margin feedback during quoting, for example, when a rep enters a price, display resulting margin and tier-appropriate range.
- **Exception Management Workflows:** Create approval workflows for discounts beyond defined thresholds, generating reports showing patterns by rep, customer, and product.
- **Supplier Pass-Through Governance:** Establish clear policies for timing, percentage, and communication of supplier cost increases with contract provisions.

The financial impact of pass-through failure compounds over time and often multiplies. A distributor failing to pass through 10% supplier increases, perhaps absorbing 50 basis points per increase over two cycles annually, loses 100 basis points of gross margin. Across a $100 million distributor operating at 25% gross margin, this represents $1 million in annual margin erosion. Platforms like Cavallo automate pass-through governance by flagging gaps between supplier cost changes and customer price updates in real time, ensuring that margin protection is systematic rather than dependent on individual vigilance.

The Hidden Cost Of Small Orders

Small orders don't just reduce margin–they destroy it.



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Survey data identifies frequent small orders under $100 as a primary cost-to-serve driver, cited by 56% of respondents. Extended payment terms (56%) and multiple sales touchpoints (52%) follow closely. Small order frequency stands out because the costs are invisible to most customers and many distributors.

The economics are stark. A typical small order costs $25-50 to process, pick, pack, and deliver. An order with $75 in product at 25% gross margin generates $18.75 in gross profit. After subtracting processing costs, the transaction loses $6-30. This helps explain why 10.5% of invoices across the industry lose money at the transaction level.

Yet 68% of surveyed distributors don't systematically measure cost-to-serve. Without measurement, the problem stays hidden and often multiplies. Finance teams see gross margin pressure but can't identify root causes. Operations teams feel the burden but lack data to quantify impact.

A distribution consultant explained: "Many distributors acknowledge losing money on small orders. The solution benefits both distributor and customer: to encourage order consolidation to two or three weekly deliveries. This reduces processing costs for both parties while maintaining supply reliability."

Consider a customer placing five orders weekly averaging $60 each, $300 weekly. Each order requires invoice processing, delivery coordination, and payment. Consolidating two weekly orders of $150 each delivers the same products with 60% fewer transactions. Both parties save money.

Implementation requires:

- **Measurement:** Quantify actual cost to process different order sizes; calculate breakeven thresholds; share data with sales teams.
- **Minimum Order Policies:** Establish thresholds ($150-250) with fees ($25-50) below minimum; build A-tier exemptions.
- **Customer Solutions:** Provide blanket purchase orders, standing orders, electronic ordering, vendor-managed inventory.

Customer communication matters. Rather than framing small order fees as penalties, successful distributors position them as necessary to maintain service quality. Most customers respond positively when the rationale is clear and alternatives are offered. Distributors capturing margin improvement from small order policies typically achieve 50-100 basis points of benefit in the first year.

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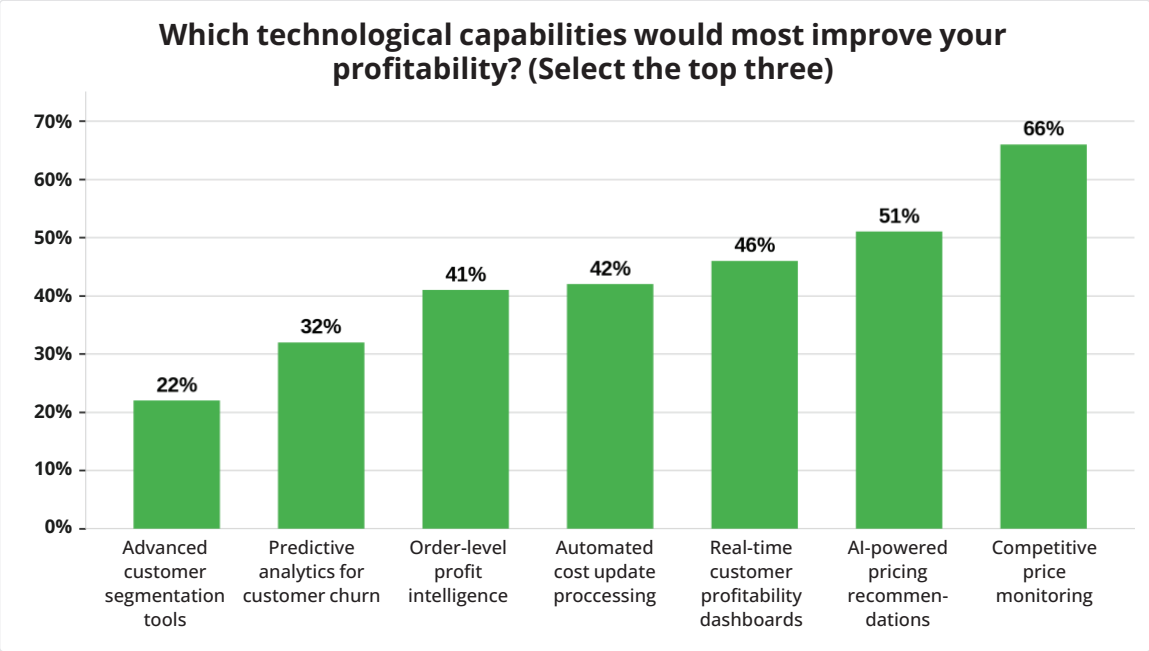
Technology Priorities And The Readiness Gap

Technology enables execution. It does not replace it.



Survey data reveals strong distributor interest in profit optimization technology. Yet 63% still rely on Excel, a diagnostic tool, for profitability analysis vs technology that provides actionable intelligence. This contrast is striking: while over 40% identified real-time profitability and order level profit intelligence as priorities, the overwhelming reliance on Excel suggests that most distributors lack the data quality, process standardization, and organizational capabilities required to deploy advanced analytics successfully.

Why Traditional Tools Fall Short

Excel provides diagnostic insight but cannot integrate into decision workflows. ERP systems generate retrospective reports that arrive after pricing conversations conclude. Purpose-built profit intelligence platforms address this gap by delivering real-time, transaction-level margin visibility directly into quoting workflows. Cavallo, for example, integrates with leading ERP systems to surface profit insights and predictive intelligence at the point of decision, enabling distributors to see exactly where profit is made or lost and act on it immediately.

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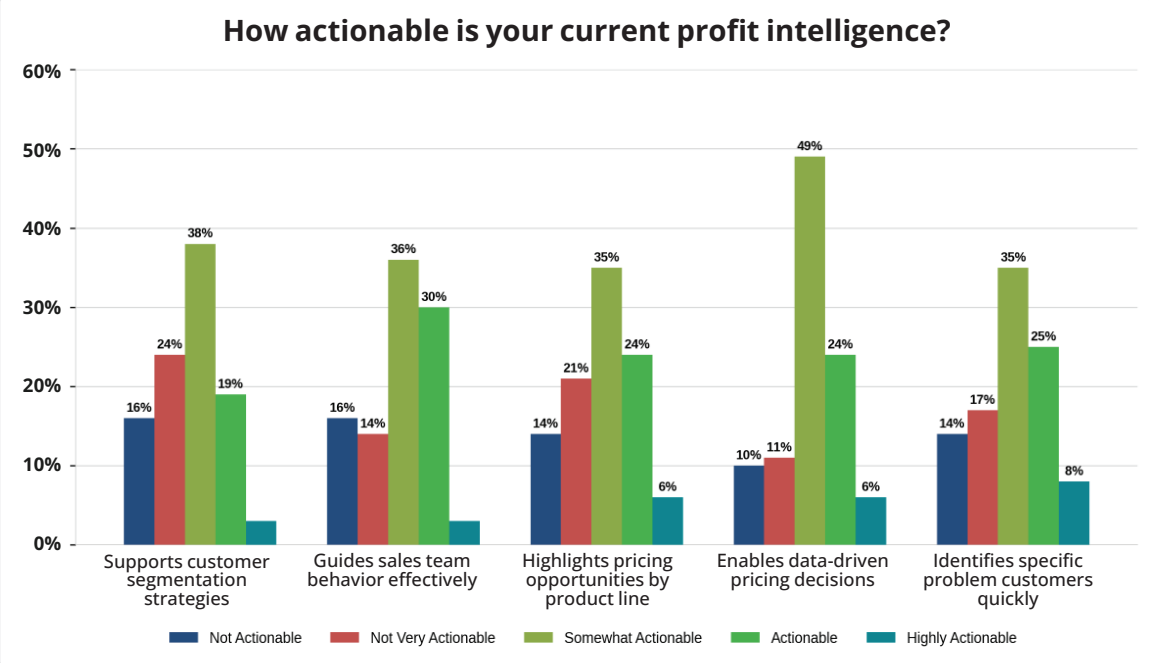
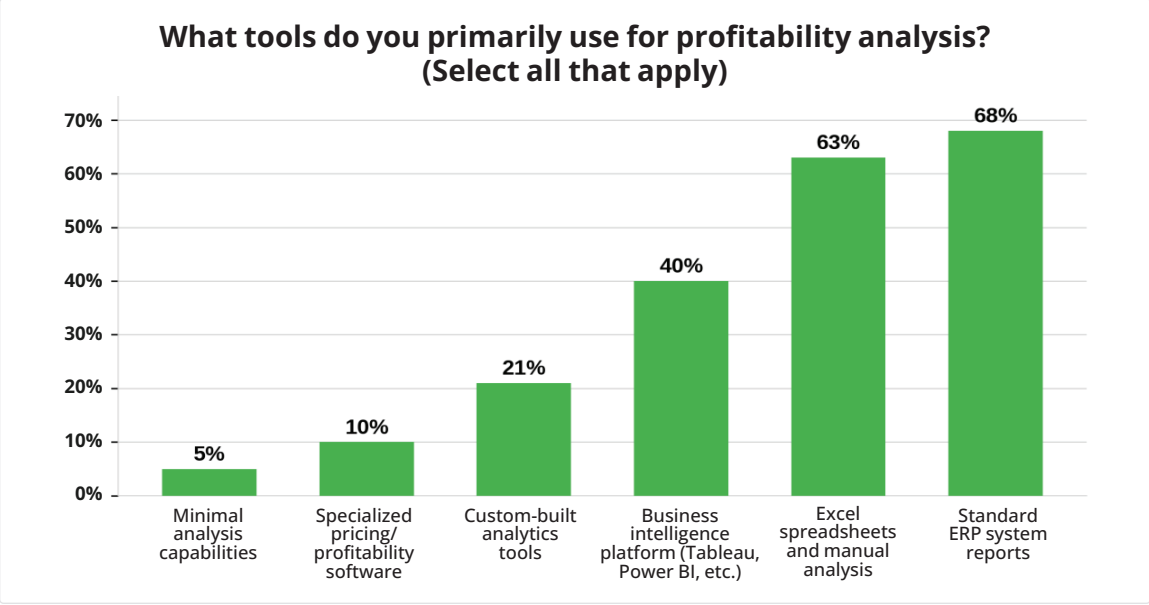


The survey measured actionability across five dimensions. Only 3-8% of distributors rated their current profit intelligence as "Highly Actionable" for any use case. A full 40% rated their profit intelligence "Not Actionable" or "Not Very Actionable" for customer segmentation. Worse, 30% felt the same about their ability to use profit intelligence to guide sales team behavior.



The readiness gap appears in three ways. First, many lack clean foundational data, for example, pricing rules remain in sales team heads rather than systems. Second, process discipline must precede technology; implementing dashboards without standardized pricing processes simply automates chaos. Third, change management drives adoption–sales teams resist tools perceived as constraints rather than enablers.

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The Staged Technology Path

- **Stage 1 (Foundation):** Augment Excel with automated data extraction from ERP systems; add simple dashboards that present analysis visually; implement basic pricing rules that prevent obvious errors.
- **Stage 2 (Visibility Tools):** Deploy profitability dashboards that answer specific questions: Is this customer profitable? What margin should I quote? Integrate visibility into quoting workflows.
- **Stage 3 (Intelligent Automation):** Implement AI-powered pricing with human oversight: system suggests prices with explanations; sales reps can accept, adjust, or override; system learns.
- **Stage 4 (Predictive Intelligence):** Use predictive models to identify customers at risk of churning, accounts likely to accept price increases, and profitable growth opportunities.

A distribution consultant cautioned: "A distributor with manual pricing errors trying to implement AI pricing solves the wrong problem. The issue isn't prediction sophistication; it's basic process execution." Fix foundational problems first, then layer on intelligence.

Action Framework For Distributors

The execution gap closes through systematic action, not heroic effort. Distributors who focus on five areas simultaneously achieve 150-200 basis points (1.5-2.0 percentage points) in margin improvement within 12-18 months: pricing discipline, customer segmentation, small order policy, pass-through governance, and sales team visibility.

If You Do One Thing First

Put transaction-level profit insights in the hands of the people quoting orders. Not monthly reports. Not quarterly customer profitability summaries. Real-time visibility into whether the specific order being priced right now will make or lose money, incorporating current costs, customer tier, order size, and delivery requirements.

This single action enables everything else. You cannot segment customers by profitability without seeing which transactions drive the average. You cannot enforce pricing discipline without showing sales teams what margin they're giving away. You cannot address small order losses without identifying which orders lose money. Transaction-level visibility and analysis to see where and why profit

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is slipping away is the prerequisite. This is precisely the capability that Cavallo delivers: real-time, order-level profit intelligence integrated into the quoting process. Start there.

Immediate Actions (30-90 Days)

- **Audit Your Top 20 Unprofitable Customers:** Calculate true profitability including all costs; develop corrective action plans, including price increases, service adjustments, or exits.
- **Implement Small Order Charges:** Establish minimum thresholds ($150-250) and fees ($25-50); build A-tier exemptions.
- **Set Up Pricing Validation:** Create approval workflows for discounts beyond thresholds; generate exception reports by rep, customer, product.
- **Begin Dashboard Development:** Customer profitability distribution, margin by tier, rep-level margin performance.

Foundation Building (3-6 Months)

- **Deploy Profitability Dashboards:** Integrate into quoting workflows; enable real-time "Is this customer profitable?" answers.
- **Implement Cost-to-Serve Analysis:** Move from estimates to activity-based costing by customer type and order profile.
- **Establish Pricing Governance:** Clear policies for supplier pass-through timing; contract language with escalation clauses.
- **Formalize ABCD Segmentation Based on Profitability:** Define tier criteria, service levels, pricing parameters, payment terms, minimum orders.
- **Automate Standard Pricing:** Reduce manual intervention from 38% toward 15%; integrate logic into ERP.
- **Consider Sales Compensation Redesign:** Shift to hybrid model (50% margin, 30% revenue, 20% strategic); implement over two quarters.

Advanced Capabilities (6-18 Months)

- **Predictive Analytics:** Model for customers at risk of churning, price acceptance likelihood, and profitable growth opportunities.
- **Real-Time Margin Intelligence:** Integrate into quoting with margin comparison and recent comparable transactions.
- **Competitive Intelligence:** Monitor prices for key product lines to inform strategy and justify premiums.
- **Behavior Monitoring:** Track profitability trends; alert on declining A-tier margins; identify upward-trending B-tier.

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Critical Success Factors

Executive Sponsorship: Margin improvement initiatives fail without CEO/COO level commitment. Executives must communicate that profit discipline is non-negotiable.

Change Management: Budget 2-3x software costs for training and organizational change. For a $50 million distributor investing $100,000 in pricing technology, this means allocating $200,000-$300,000 for change management, training, and process redesign. The investment pays for itself: distributors who properly manage the transition typically recover costs within 6-9 months through margin improvement. Frame changes as enablers that help sales teams sell more profitably, not constraints that limit their flexibility.

Process Before Technology: Define processes first, then select technology. Begin with pricing governance and segmentation frameworks; technology amplifies discipline but cannot create it. Early movers establishing these foundations now will capture the 12–18-month advantage window.

Measurement Discipline: Track orders manually priced, pass-through rate, un-profitable customers, margin by tier, cost-to-serve by segment. Review monthly.

The Competitive Advantage Window

Early movers can capture 150-200 basis points (1.5-2.0 percentage points) in margin improvement before competitors respond. For a $50 million distributor, the difference between acting now and waiting is stark: early movers recovering $750,000 to $1 million annually in margin gain compound that advantage over time, funding reinvestment in technology, talent, and customer experience while lagging competitors continue absorbing preventable losses. During this 12–18-month window, profit intelligence becomes embedded in organizational culture, sales teams develop margin-focused selling proficiency, and technology investments deliver ROI before becoming standard practice. The downstream benefits extend beyond the P&L: improved pricing discipline strengthens customer trust, reduced manual intervention frees sales teams for higher-value selling, and data-driven decision-making creates a culture of accountability that drives performance across the entire organization.

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Profitability As Process Discipline

The execution gap is not mysterious. The solution is systematic. This research reveals a fundamental truth: Most companies know more than they act on. They measure customer profitability but don't share it with sales teams. They identify unprofitable accounts but don't correct them.

The four leakage sources, incomplete pass-through, manual pricing errors, small order losses, and unasked-for discounts, share a common root cause: the gap between measurement and action. Only 3-8% rated their profit intelligence as "highly actionable" across any use case.

Closing this gap requires five interdependent actions: real-time profitability visibility at the decision point; profit-based customer segmentation; pricing discipline through automated validation and pass-through governance; small order economics through minimum thresholds; and technology that reinforces and improves thoughtful processes. The compound effect comes from addressing all five simultaneously.

This research confirms that profitability improvement is fundamentally an execution challenge, not a knowledge gap. Most distributors know what to do. The best actually do it. And the rewards extend well beyond the margin line: distributors who close the execution gap report stronger customer relationships, more confident sales teams, faster decision-making, and a competitive resilience that compounds over time.

The data is clear.
Intelligence informs the strategy.
Execution defines the leader.

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About Cavallo

Cavallo is a leader in AI-driven Profit Maximization and Decision Intelligence. Its platform integrates with top ERP systems to ensure flawless orders and deliver actionable insights to optimize revenue streams for distributors, manufacturers, and product-centric brands. Its real-time analytics and advanced workflows also help businesses enhance customer retention and align sales and marketing initiatives. Cavallo's mission is to help customers maximize profits at scale.

For more information, visit cavallo.com.

About Distribution Strategy Group

Distribution Strategy Group is an industry research and consulting firm specializing in wholesale distribution operations, strategy, and technology adoption. The firm provides research-based insights, strategic advisory services, and implementation support to distribution companies and technology providers serving the wholesale distribution market.

For more information: research@distributionstrategy.com

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