Disintermediation

In economics, **disintermediation** is the removal of intermediaries in a supply chain, or "cutting out the middleman". Instead of going through traditional distribution channels, which had some type of intermediate (such as a distributor, wholesaler, broker, or agent), companies may now deal with every customer directly, for example via the Internet.[1] One important factor is a drop in the cost of servicing customers directly.

This can also happen in other industries where distributors or resellers operate and the manufacturer wants to increase profit margins, therefore missing out intermediaries to increase their margins.

Disintermediation initiated by consumers is often the result of high market transparency, in that buyers are aware of supply prices direct from the manufacturer. Buyers bypass the middlemen (wholesalers and retailers) to buy directly from the manufacturer, and pay less. Buyers can alternatively elect to purchase from wholesalers. Often, a business-to-consumer electronic commerce (B2C) company functions as the bridge between buyer and manufacturer.

To illustrate, a typical B2C supply chain is composed of four or five entities (in order):

- Supplier
- Manufacturer
- Wholesaler
- Retailer
- Buyer

It has been argued that the Internet modifies the supply chain due to market transparency:

- Supplier
- Manufacturer
- Buyer

History

The term was originally applied to the banking industry in 1967; disintermediation referred to consumers investing directly in securities (government and private bonds, and stocks) rather than leaving their money in savings accounts, then later to borrowers going to the capital markets rather than to banks. The original cause was a U.S. government regulation (Regulation Q) which limited the interest rate paid on interest bearing accounts that were insured by the Federal Deposit Insurance Corporation.

It was later applied more generally to "cutting out the middleman" in commerce, though the financial meaning remained predominant. Only in the late 1990s did it become widely popularized.

Impact of Internet-related disintermediation upon various industries

Strong impact

- Computer hardware and software
- Travel agencies
- Bookstores and music stores
- Stock Purchasing
- Contact lenses

Still in progress (due to legal or structural obstacles)

- Alcoholic beverages
- Real estate
- Recruitment
- Education

A real estate market is social. Buyers and sellers communicate to discover information and negotiate to exchange goods or services. Internet transparency is letting home buyers view Residential and Commercial MLS, FSBO listings on their own. It has reduced home buyers search costs, and given them access to multiple new product options to choose from when entering a real estate transaction. Sellers have found new tools and services to attract home buyers and sell their houses, they can now leverage Internet market tools that are intended to increase the efficacy of transactional requirements.

This transparency has made it difficult for real estate agents, appraisers, and lenders to collect the fees, tipping the balance of power towards the consumers. By opening access to information outside of the Brokers/Lawyers control, buyers and sellers now gain economic benefits that would otherwise go to market intermediaries or be inappropriately distributed among the smart and connected dealmakers of the financial world.

- Prime brokerage for hedge funds
- Health Care - due to developments in eHealth and specifically Consumer Health Informatics
- Video rental and distribution

Failed and became niche ancillary services

- Furniture
- Groceries
- Pet supplies (especially dog food)

Discussion

In the non-Internet world, disintermediation has been an important strategy for many big box retailers like Walmart, which attempt to reduce prices by reducing the number of intermediaries between the supplier and the buyer. Disintermediation is also closely associated with the idea of just in time manufacturing, as the removal of the need for inventory removes one function of an intermediary.

The existence of laws which discourage disintermediation has been cited as a reason for the poor economic performance of Japan and Germany in the 1990s.

However, Internet-related disintermediation occurred less frequently than many expected during the dot com boom. Retailers and wholesalers provide essential functions such as the extension of credit, aggregation of products from different suppliers, and processing of returns. In addition, shipping goods to and from the manufacturer can in many cases be far less efficient than shipping them to a store where the consumer can pick them up (if the consumer's trip to the store is ignored). In response to the threat of disintermediation, some retailers have attempted to integrate a virtual presence and a physical presence in a strategy known as bricks and clicks.

Reintermediation

Reintermediation can be defined as the reintroduction of an intermediary between end users (consumers) and a producer. This term applies especially to instances in which disintermediation has occurred first.[1]

At the start of the Internet revolution, electronic commerce was seen as a tool of disintermediation for cutting operating costs. The concept was that by allowing consumers to purchase products directly from producers via the Internet, the product delivery chain would be drastically shortened, thereby "disintermediating" the standard supply model middlemen. However, what largely happened was that new intermediaries appeared in the digital landscape (e.g., Amazon.com and eBay).[2]

Reintermediation occurred due to many new problems associated with the e-commerce disintermediation concept, largely centered on the issues associated with the direct-to-consumers model. The high cost of shipping many small orders, massive customer service issues, and confronting the wrath of disintermediated retailers and supply channel partners all presented real obstacles. Huge resources are required to accommodate presales and post sales issues of individual consumers. Before disintermediation, supply chain middlemen acted as salespeople for the producers. Without them, the producer itself would have to handle procuring those customers. Selling online has its own associated costs: developing quality websites, maintaining product information, and marketing expenses all add up. Finally, limiting a product's availability to Internet channels forces the producer to compete with the rest of the Internet for customers' attention, a space that is becoming increasingly crowded over time.

Examples of companies

Notable examples of disintermediation include Dell and Apple, which sell many of their systems direct to the consumer—thus bypassing traditional retail chains, having succeeded in creating brands well recognized by customers, profitable and with continuous growth.

See also

- Outlet store
- Flat fee MLS — An example of disintermediation in the Real Estate industry.
- Laiki agora - an example of disintermediation of agricultural foodstuffs in Greece

References

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