# MARKETING DISTRIBUTION POLICY

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# Marketing distribution policy

Textbook

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The textbook discusses the theoretical and methodological foundations of marketing distribution policy, in particular, the development, management, and control of marketing channels at the enterprises, the establishment of relationships between participants in the marketing channels, the formation of supply chains.

The textbook is intended for top managers of industrial enterprises, specialists, and scientists in the field of sales management and related fields. It will be useful for teachers, graduate students, and students of economic specialties of higher education institutions, also, to a wide range of readers who are interested in the problems of marketing distribution policy.

The textbook contains a large number of examples and factual materials illustrating the theoretical foundations.

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# INTRODUCTION

In the conditions of growing competition, an additional competitive advantage of enterprises becomes their systems of distribution and marketing channels. The environment of marketing channels, modern trends in wholesaling and retailing are factors that already seriously affect the marketing channels development, functioning, and management in the national and world markets.

Therefore, managers and economists must know the theory and methodology of marketing channel development and management, have practical skills in applying appropriate techniques. Omit, the course "Marketing distribution policy" acquires special importance.

The course aims to achieve students' flexible, adaptive thinking and the formation of special knowledge and skills to manage marketing channels and supply chains, organize trade, develop strategies for distribution activities and use them in practice.

The main objectives of the course are:

– to develop professional skills of the organization of the distribution process of the industrial and consumer goods based on the analysis of market indicators and indicators of marketing activity of the concrete enterprise for its activity optimization;

– to develop professional skills of combining in-depth analysis and group work, overcoming conflict situations during the development and presentation of a marketing proposal for the distribution of the products;

– to identify and update skills of interaction with different contractors within marketing channels of different levels.

The textbook consists of 5 sections.

The first section presents the theory of marketing channels: the concept of marketing channels and their role in modern economics; participants and flows in marketing channels, their functions. This section also discusses the types of marketing channels to be used for the distribution of consumer and industrial products. The final part of the section considers the direct and indirect distribution.

The second section covers the relationships in marketing channels. The section comprises the following problems: participants integration in marketing channels; conflict management in marketing channels, and motivation of channel participants.

The third section discusses the purposes and functions of participants in marketing channels. The section also highlights the significance, types, and features of wholesaling and retailing. Particular attention is paid to participants in marketing channels for industrial products.

The fourth section focuses on the marketing channels' structure; marketing channels designing and operating. Part of the section centers on the development of vertical and horizontal marketing systems.

The fifth section explores the link between marketing and logistics in the distribution channels. This section also focuses on supply chains.

The course “Marketing Distribution Policy” is closely related to other courses – “Marketing”, “Marketing Logistics”.

The textbook material focuses on lecturers and students of economic specialties, and practitioners (specialists in the field of management and marketing, etc.). The presented materials form a methodological aid in solving practical problems.

# SECTION 1

# MARKETING CHANNELS: MAIN DEFINITIONS, FUNCTIONS, TYPES AND PARTICIPANTS

## 1.1. Essence of marketing channels

A **marketing channel system** is the particular set of marketing channels a firm employ, and decisions about it are among the most critical one's management faces (Kotler, Keller, 2012).

A marketing channel performs the work of moving goods from producers to consumers. It overcomes the time, place, and possession gaps that separate goods and services from those who need or want them (Kotler, Keller, 2012).

**A channel of distribution or trade channel** is the path or route along which goods move from producers to ultimate consumers or industrial users. In other words, it is the distribution network through which a producer puts his product in the hands of actual users (Channels of Distribution, n.d.).

Marketing channels are, formally, chain of interdependent organizations whose role is to make product and services available for users (Kotler, Keller 2012). Basically, marketing channels are the routes that products and services go through on their way from producers (manufacturers) to final consumers or business users – a link between producers and final users. The main purpose of marketing channel is to have the right product delivered on the shelf of the store when the customer wants it, and at the price customer is willing to pay for it. Marketing channel manager must decide which intermediary, or more of them, are the best suitable to deliver the product to the market the producer wishes to enter. The crucial point of every marketing channel is the customer (whether it is the final customer or business buyer) and all efforts and activities of channel members need to be focused on the end users and their satisfaction.

The essence of marketing channels is consisted of following components (Lovreta, Končar, Petković, 2018 cited in Đurić, Stojiljković, 2018):

– organized system in which participants together undertake integrated and/or coordinated actions;

– agencies and institutions that take place as participants in marketing channels;
– the functions of marketing channel members;
– connections between suppliers and buyers, and
– marketing tasks in the process of connecting producers and consumers.

The channel of distribution includes the original producer, the final buyer and any middlemen – either wholesaler or retailer.

**The term middleman (intermediary)** refers to any institution or individual in the channel which either acquires title to the goods or negotiates or sells in the capacity of an agent or broker. But facilitating agencies who perform or assist in marketing function are not included as middlemen in the channel of distribution. This is because they neither acquire title to the goods nor negotiate purchase or sale. Such facilitating agencies include banks, railways, roadways, warehouses, insurance companies, advertising agencies, etc. (Channels of Distribution, n.d.).

The principal participants in marketing channels are **producers** (manufacturers, originators), **middleman/intermediaries** (wholesalers, retailers and specialized intermediaries) and **final users** (individual consumers or business customers). Other specialized participants, involved in transfer of products and services to the spot of their final utilization are: brokers, manufacturer's representatives, agents and other specialized intermediaries (transport, warehouse, merchandising, delivery, assortment, labeling, financing, crediting, insurance, arrangement, promotion, research etc.) (Đurić, Stojiljković, 2018).

In moving goods to convenient location for the consumer, channels provide form, time, place and ownership utility (Đurić, Stojiljković, 2018):

1. **Form utility** is the want satisfying capability that is created when a good produced.
2. **Time utility** is the want satisfying capability that is created when a product is made available to customers when they want it.
3. **Place utility** is the want satisfying capability that is created when a product is made readily accessible to potential customers. Products have no value to the consumer in the manufacturer's warehouse until it is made available to consumers where they want to buy them.
4. **Possession utility or ownership utility** is the want satisfying capability that is created when title of a product is transferred from the manufacturer to the buyer at the point or time of purchase (retail store).

Possession utility is the want-satisfying capability that is created when a customer buys the product – that is when ownership is transferred to the buyer.

The essential features of marketing channels are the following (Наумов, 2008, p. 9):

– marketing channel is a market-oriented structure consisting of interdependent and interconnected entities aimed at achieving a single result;

– channel participants form communicative interactions that contribute to the growth of the partnerships' value;

– participants coordinate their activities to meet their needs and the needs of end users in the best way;

– due to the high level of interaction, the channel participants organize processes that form “difficult to copy” competencies.

The basic structural elements of the marketing channel (elements of the first level) are the goods/services delivery from producer to consumer and the transfer of ownership. They characterize the main purpose of marketing channel – the movement of products to consumers. In addition, important structural elements of the marketing channel are meeting end users' needs and the implementation of appropriate marketing functions (elements of the second level). Also, the marketing channel forms another structural element – the creation of consumer and marketing value of the product / service (element of the third level).

Important characteristics of marketing channel are length and width. **Channel length** means how many times the product changes hands among middlemen before it reaches the end-user. If the product has to go through a few intermediaries, then the channel is considered long. The channel is short when the manufacturer moves its product through one or two intermediaries. In case the product is sold directly to the end customer, the distribution channel is direct. Generally, the relationship between channel length and size of purchase is inverse: bigger purchase – shorter channel (Cateora & Graham 2007, p, 406 cited in Louckx, 2014).

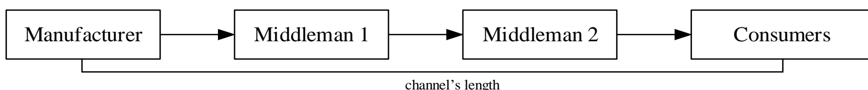


Figure 1.1. Marketing channel length

Where as **channel width** is concerned with the number of intermediaries at a particular phase in distribution channel. More middlemen at a particular point of distribution – wider and more intensive the channel becomes (Onkvisit & Shaw, 2004, 362 cited in Louckx, 2014).

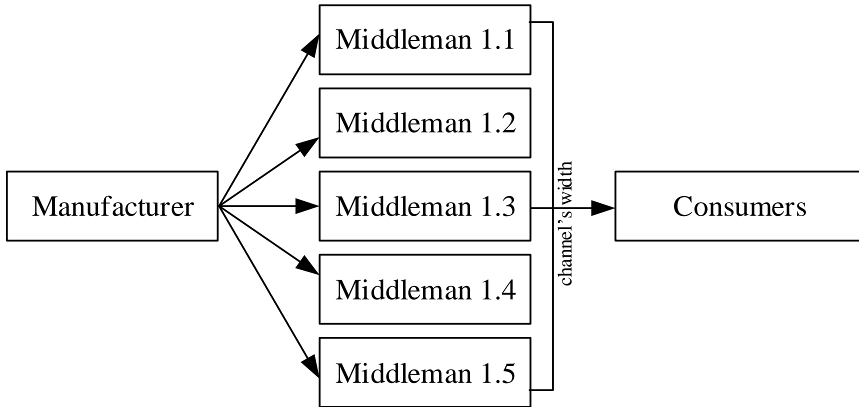


Figure 1.2. Marketing channel's width

Channel objectives will necessarily differ from one company to another, but there are a number of general points that are likely to be relevant to most companies. These should normally be considered by a company in the course of its distribution planning process to ensure that the most appropriate channel structure is developed. The key points that should be addressed are as follows (Rushton, Croucher, Baker, 2014):

1. To make the product readily available to the market consumers at which it is aimed. Perhaps the most important factor here is to ensure that the product is represented in the right buying environment for customers. For a consumer product this might be, for example, retail store and internet. Having identified the correct marketplace for the goods, the company must make certain that the appropriate physical distribution channels are selected to achieve this objective.
2. To enhance the prospect of sales being made. This may be the responsibility of either the sales team or the logistics team. It can be achieved in a number of ways. The most appropriate factors for each product or type of retail outlet will be reflected in the choice of channel. For example, the general aims of delivery to shops/stores might be to get good positions and displays in the store, and to gain the active support of

the retail salesperson, if this is relevant. The product should be "visible, accessible and attractively displayed". In this instance, channel choice might be affected by the following requirements:

– Does the deliverer arrange the merchandise in the shop?
– Are special displays used?
– Does the product need to be installed, demonstrated or explained?
– Is there a special promotion of the product?

3. To achieve cooperation with regard to any relevant distribution factors. These factors may be from the supplier's or the receiver's point of view, and include minimum order sizes, unit load types, product handling characteristics, materials handling aids, delivery access (e.g. vehicle size) and delivery time constraints, amongst others.

4. To achieve a given level of service. Once again, from both the supplier's and the customer's viewpoints, a specified level of service should be established, measured and maintained. The customer normally sees this as crucial. Relative performance in achieving service level requirements is often used to compare suppliers and may be the basis for subsequent buying decisions.

5. To minimize logistics and total costs. As always, cost is very important, as it is reflected in the final price of the product. The selected channel will reflect a certain cost, and this cost must be assessed in relation to the type of product offered and the level of service required.

To receive fast and accurate feedback of information. A good flow of relevant information is essential for the provision and maintenance of an efficient distribution service. It might include sales trends, inventory levels, damage reports, service levels, cost monitoring and EPOS information shared with suppliers.

## 1.2. Functions and flows in marketing channels

According to Profesor Kasturi of Harvard Business School there are eight generic **channel functions** (Kasturi, 1994):

1. Product Information. Customers seek more information on certain kinds of products,particularly products that are new and/or technically complex, and those that have a rapidly changing technological component.

2. Product Customization. Some products inherently need technical modification; they require customization to fit the customer's production

requirements. Many times, however, even a standard product may need to fulfill specificcustomer requirements or factors such as size or grade.

3. Product Quality Assurance. A customer emphasizes product integrity and reliability because of product consequences for the customer's own operations. This is a measure of the application's importance to the customer.

4. Lot Size. This function reflects the customer's dollar outlay for the product. If it has ahigh unit value or is used extensively, it is likely to represent a significant financial decision for the customer and is likely to lead to a concentrated purchasing effort.

5. Assortment. A customer may need a broad range of products and may require one-stopshopping. At other times, assortment needs may simply berelated to the breadth of the product line and availability of complementary products.

6. Availability. Some customer environments require the channel to support a high degree of product availability. These are usually customers whose product-usage rate is difficult to predict, or customerswho will switch to competition rather than wait when the product is unavailable.

7. After Sales Service. Customers need services such as installation, repair, maintenance,and warranty. Often the quality and availability of such post-sales services will influence the initial sale. The nature of this service will obviously differ by industry.

8. Logistics. Transporting, storing, and supplying products to the end user involve levels ofcomplexity. Moreover, once such investments are in place,governing their effective use will involve additional transaction costs.

Additionally, the following are the **additional functions** member of the marketing channel perform (Ilesanmi, 2011):

1. Gathering information on the changing needs in the market and pass them on to the producers. By so doing, they perform part of the research team.

2. Ordering goods, usually in bulk, thereby, reducing the cost of storage by the producers. Ordering is a way of letting the producers know of the demand level in the market.

3. Taking title to the products they help to the market.

4. Bearing risks of storage due to theft, climatic changes and even cost of warehousing.

5. Helping in financing trade through acquisition and allocation of funds required to carry inventory at any level of the marketing channel.

6. Being responsible for negotiating the final price and other terms of the offer for the eventual transfer of ownership.

7. Providing a sales force enabling manufacturers to reach many small customers at a relatively low cost. These intermediaries have more contacts and are often more trusted by the buyers than is the distant manufacturer.

Marketing functions performed in channels of distribution can be grouped as those that are necessary to a transaction, those that are required for the physical exchange of goods and those that facilitate both the transaction and the physical exchange. Channel decision-making involves establishing and maintaining the institutional structure in marketing channels (Louckx, 2014).

The question for marketers is not *whether* various channel functions need to be performed – they must be – but rather, *who* is to perform them. All channel functions have three things in common: they use up scarce resources; they can often be performed better through specialization; and they can be shifted among channel members. Shifting some functions to intermediaries lowers the producer's costs and prices, but the intermediary must add a charge to cover its work (Kotler, Keller, 2012).

An important question in marketing channel theory are types of flows (Fig. 1.3).

1. **Physical flow (material flow):** the flow of goods from the manufacture through middlemen (intermediaries) to end consumers.

2. **Title (ownership) flow** captures the transfer of ownership of goods from one channel participant to another.

3. **Payment flow:** the flow of cash to pay for goods, moving mainly from consumer to manufacture.

4. **Information flow:** the exchange of information between the participants of the channel about the movement of inventory and related activities.

5. **Promotion flow:** the flow of promotional activities, moving from manufacture to consumer.

6. **Ordering flow:** the flow of goods' orders, moving mainly from consumer to manufacture.

7. **Service flow:** the flow of services provided by all members of the channel that serve end users.

8. **Marketing flow:** the flow of marketing communications, due to the need to generate demand for the manufacturer's products at each level of the channel.

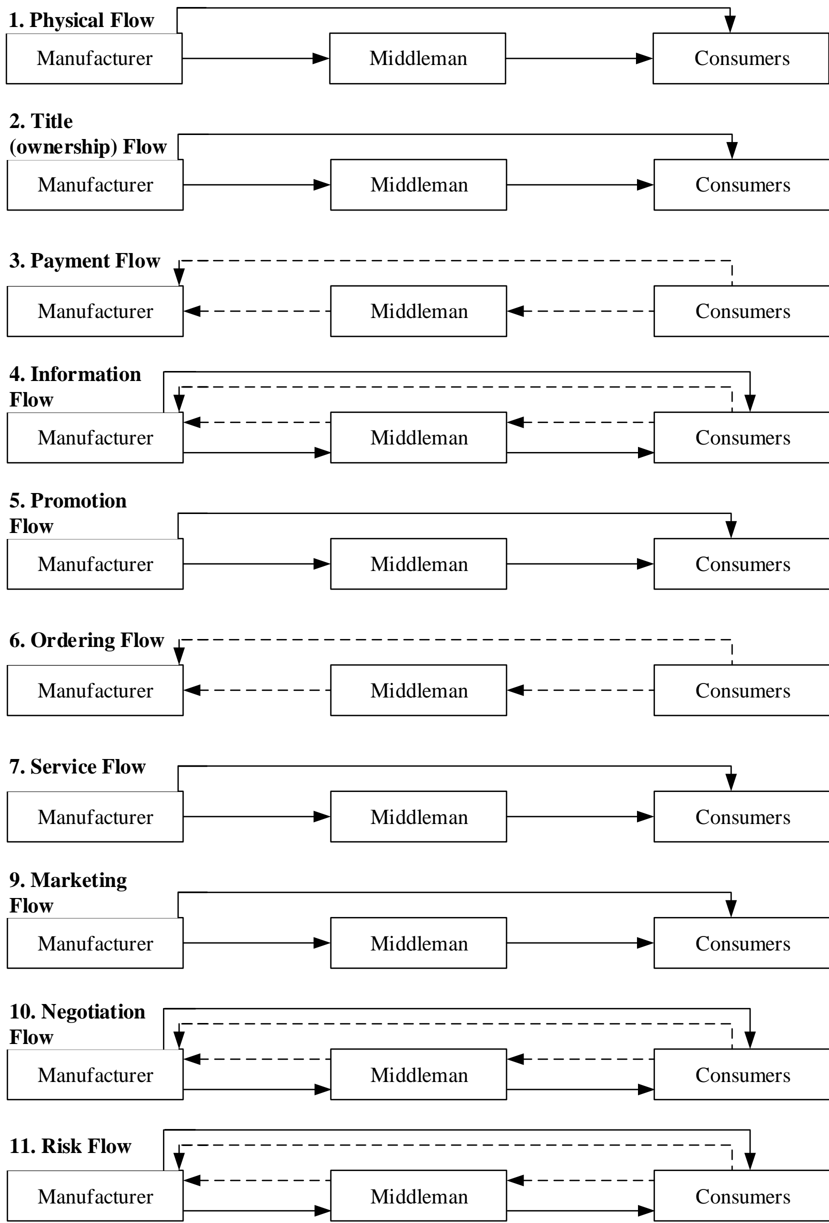


Figure 1.3. Flows in the marketing channel

Physical possession, ownership transfer, promotion, service and marketing flows move forward through the channel, from manufacturer to final consumer. Ordering and payment move upwards the channel, from final consumers to manufacturers. Negotiation, risking and information sharing move in both direction and among different channel members.

Marketing channels produce five service outputs (Kotler, Keller, 2012):

1. **Desired lot size** – the number of units the channel permits a typical customer to purchase on one occasion. In buying cars for its fleet, company prefers a channel from which it can buy a large lot size; a household wants a channel that permits a lot size of one.
2. **Waiting and delivery time** – the average time customers wait for receipt of goods. Customers increasingly prefer faster delivery channels.
3. **Spatial convenience** – the degree to which the marketing channel makes it easy for customers to purchase the product. Toyota offers greater spatial convenience than Lexus because there are more Toyota dealers, helping customers save on transportation and search costs in buying and repairing an automobile.
4. **Product variety** – the assortment provided by the marketing channel. Normally, customers prefer a greater assortment because more choices increase the chance of finding what they need, though too many choices can sometimes create a negative effect.
5. **Service backup** – add-on services (credit, delivery, installation, repairs) provided by the channel.

The more service backup, the greater the benefit provided by the channel. Providing more service outputs also means increasing channel costs and raising prices.

Except channels that are used to transfer goods and services forward, towards the final users, there are reverse channels that are driven in opposite direction, from final consumers towards manufacturers. These channels are used to return unwanted and damaged products (for replacement or reparation) and for recycling (packaging, plastic, glass bottles, organic waste, old and broken technical products etc.). Sometimes the company itself uses reverse channels to withdraw products from the market, when there is the malfunction or damage to the line of products discovered after the product was released to the market (Đurić, Stojiljković, 2018).

**Channel power** is the ability to alter channel members' behavior so they take actions they would not have taken otherwise. Manufacturers can

draw on the following types of power to elicit cooperation (Kotler, Keller, 2012):

1. **Coercive power.** A manufacturer threatens to withdraw a resource or terminate a relationship if intermediaries fail to cooperate. This power can be effective, but its exercise produces resentment and can lead the intermediaries to organize countervailing power.

2. **Reward power.** The manufacturer offers intermediaries an extra benefit for performing specific acts or functions. Reward power typically produces better results than coercive power, but intermediaries may come to expect a reward every time the manufacturer wants a certain behavior to occur.

3. **Legitimate power.** The manufacturer requests a behavior that is warranted under the contract. As long as the intermediaries view the manufacturer as a legitimate leader, legitimate power works.

4. **Expert power.** The manufacturer has special knowledge the intermediaries' value. Once the intermediaries acquire this expertise, however, expert power weakens. The manufacturer must continue to develop new expertise so intermediaries will want to continue cooperating.

5. **Referent power.** The manufacturer is so highly respected that intermediaries are proud to be associated with it. Companies such as IBM, Caterpillar, and Hewlett-Packard have high referent power.

Coercive and reward power are objectively observable; legitimate, expert, and referent power are more subjective and depend on the ability and willingness of parties to recognize them. Most producers see gaining intermediaries' cooperation as a huge challenge. They often use positive motivators, such as higher margins, special deals, premiums, cooperative advertising allowances, display allowances, and sales contests. At times they will apply negative sanctions, such as threatening to reduce margins, slow down delivery, or terminate the relationship. The weakness of this approach is that the producer is using crude, stimulus-response thinking. In many cases, retailers hold the power. One estimate is that manufacturers offer the nation's supermarkets between 150 and 250 new items each week, of which store buyers reject more than 70 percent. Manufacturers need to know the acceptance criteria buyers, buying committees, and store managers use.

Also, each marketing channel member must be treated respectfully and be given the opportunity to be profitable. The main elements in the "trade relations mix" are price policies, conditions of sale, territorial rights, and specific services to be performed by each party (Kotler, Keller, 2012):

1. Price policy calls for the producer to establish a price list and schedule of discounts and allowances that intermediaries see as equitable and sufficient.

2. Conditions of sale refers to payment terms and producer guarantees. Most producers grant cash discounts to distributors for early payment. They might also offer a guarantee against defective merchandise or price declines, creating an incentive to buy larger quantities.

3. Distributors' territorial rights define the distributors' territories and the terms under which the producer will enfranchise other distributors. Distributors normally expect to receive full credit for all sales in their territory, whether or not they did the selling.

4. Mutual services and responsibilities must be carefully spelled out, especially in franchised and exclusive-agency channels.

## 1.3. Types of marketing channels

There are following types of distribution channels for consumers' goods in Fig. 1.4 (Distribution Channels, n.d.; Pahwa, 2019; Kotler, Keller, 2012):

1. **Zero level marketing channels** (Manufacturer to Consumer). Zero-level structure is also known as direct marketing channel. Organizations use direct selling mode to take the products from their production houses to the end users directly. A lot of money has to be spent in order to make this channel structure effective, as there is no or zero intermediaries to take your product to the end user. The major examples are door-to-door sales, home parties, mail order, telemarketing, TV selling, Internet selling, and manufacturer-owned stores.

2. **One level marketing channel** (Manufacturer to Retailer to Consumer). One-level structure is one in which we have one intermediary acting as a link between the manufacturer and the consumer. The retailers procure goods directly from the manufacturer and supply it to the consumers. In some cases, in order to retain profitable and reputed retailers the manufacturers act as wholesalers. One of the advantages for the intermediaries is the customization and the discounts they receive.

3. **Two level marketing channel** (Manufacturer to Wholesaler to Retailer to Consumer). Two-level channel has two people interceding before the product reaches the consumer. There would be a wholesaler and a retailer who takes the efforts for a speedy delivery and this is one of the most commonly used structures for consumer goods. Wholesalers buy the

bulk from the manufacturers, breaks it down into small packages and sells them to retailers who eventually sell it to the end customers. Goods which are durable, standardised and somewhat inexpensive and whose target audience isn't limited to a confined area use two-level channel of distribution.

4. **Three level marketing channel** (Manufacturer to agent/ Wholesaler to retailer to Consumer). Three level structure includes three parties in between the manufacturer and the end user. The third party may be agent, wholesaler, broker or jobber. Even it can be marketers different from manufacturer. These agents come handy when goods need to move quickly into the market soon after the order is placed. They are given the duty to handle the product distribution of a specified area or district in return of a certain percentage commission. Manufacturers opt for three-level marketing channel when the userbase is spread all over the country and the demand of the product is very high.

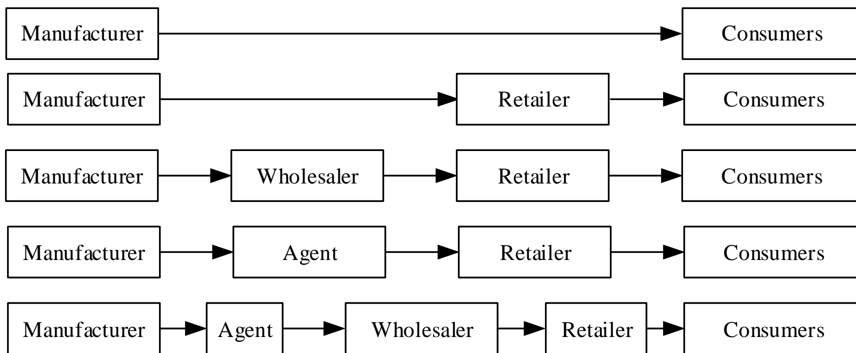


Figure 1.4. Marketing channels for consumers' goods
(Channels of Distribution, n.d.; Kotler, Keller, 2012)

The distribution of industrial goods is significantly different from the distribution of consumer goods (Fig. 1.5). Thus, the following features of the industrial goods distribution are:

– it is important to establish a close business relationship between buyer and seller;

– the need to set high requirements for service;

– specialization of the channel participant on specific industrial goods;

– direct marketing channels are mainly inherent in such industrial goods as basic equipment, facilities and industrial services;

– retail trade is mostly not used in industrial marketing, with the exception of dual-use goods, especially when purchased in small batches (for example, chemical products).

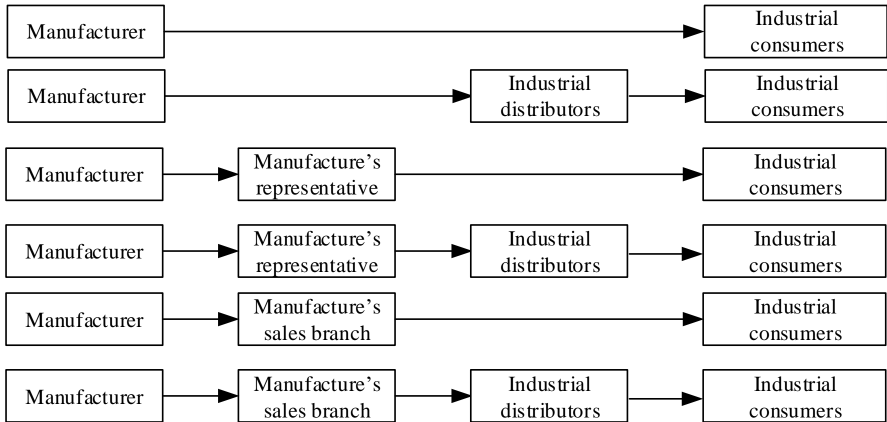


Figure 1.5. Marketing channels for industrial goods (based on Kotler, Keller, 2012)

Taking into account mentioned above, all marketing channels can be divided in two groups – direct and indirect.

## 1.4. Direct and indirect distribution in marketing channels

Direct channels do not use intermediaries. The manufacturer's own sales force deals directly with the customer, and the manufacturer has full responsibility for performing all the necessary channel tasks.

Direct distribution is often required in business marketing because of the nature of the selling situation or the concentrated nature of industry demand.

**The direct sales approach is feasible when** (Hutt, Speh, 2009)**:**

– the customers are large and well defined,

– the customers insist on direct sales,

– sales involve extensive negotiations with upper management, and

–selling has to be controlled to ensure that the total product package is properly implemented and to guarantee a quick response to market conditions.

A direct sales force is best used for the most complex sales opportunities: highly customized solutions, large customers, and complex products. Customized solutions and large customer accounts require professional account management, deep product knowledge, and a high degree of selling skill – all attributes a sales representative must possess. Also, when risk in a purchase decision is perceived as high and significant expertise is required in the sale, customers demand a high level of personal attention and relationship building from the direct sales force as a precondition for doing business.

**Direct channel advantages** (Advantages & Disadvantages, n.d.):

1. Direct channels are owned by the company itself. Control over distribution pricing, ads, display.
2. Skilled workers or professionals develop individual relationships with customers.
3. Companies are able to obtain direct feedback from customers on their existing needs.
4. Greater confidentiality can be maintained with information relating to the customer.
5. Direct channels eliminate the role of middlemen and hence the consequent cost of commission, brokerage etc.

**Direct channel disadvantages** (Advantages & Disadvantages, n.d.):

1. Company must bear all the financial risks.
2. Companies rarely enjoy expertise in local markets.
3. Reduces Distribution Channel Options.
4. Raises Fulfillment Costs.

Indirect channels use at least one type of intermediary, if not more.

**Indirect distribution is generally found where** (Hutt, Speh, 2009)**:**

– markets are fragmented and widely dispersed,

– low transaction amounts prevail, and

– buyers typically purchase a number of items, often different brands, in one transaction..

**Indirect channel advantages** (The pros and cons, n.d.):

1. Share shipping and storage costs.
2. Faster expansion: make it easier for customers to find products.

3. Benefit from third-party's experience, infrastructure and salesforce.
4. Avoid the complexity of managing distribution logistics.
5. Customize product, meet customer needs intermediaries performing functions.
6. Cost saving.

**Indirect channel disadvantages** (The pros and cons, n.d.):

1. Distance between manufacturers and customers: intermediaries increase the amount of time it takes for product to reach the buyer.
2. Hard to establish brand loyalty.
3. Disagree in roles and responsibilities within marketing channel.
4. No product loyalty.
5. Potential conflicts.
6. Long channel – lots of work, complexity.
7. Low level of control.
8. Can be expensive, e.g., slotting, volume return, and promotional allowances.
9. No customer controls.
10. Low margins.

In addition, many important managerial issues relating to the organization and management of channels of distribution have yet to be addressed in empirical channels research. Among the most important of these issues are (Frazier, 1999):

- how resource allocations to channels should be made across global product markets;
- how functions are shared-split between channel members;
- what combi- nation of push and pull strategy is appropriate for firms using indirect channels;
- when and how the Internet should be used as a sales-distribution channel;
- how coordination is achieved among distributors in integrated supply networks;
- how goals are set, plans are developed, and performance is appraised among channel members;
- how distributors should operate their businesses.

Main characteristics of direct and indirect marketing channels are mentioned in the Table below.

Table 1.1. Characteristics of direct and indirect marketing channels (Louckx, 2014)

| Indirect marketing channel | |
|---|---|
| Characteristics | Indirect marketing channel can also be called as the local or domestic channel. It can be applied when a manufacture wants to employ a domestic sales intermediary, which acts as the manufacturer's external export organization and is responsible for export of goods |
| Advantages | The channel is simple and enables reduction of exporting costs. The manufacturer incurs no start-up costs for the channel, and it is not responsible for physical movement of goods overseas |
| Disadvantages | The company has little control over how, when, where and by whom the products are sold. If products stop being profitable, or a competitive product offers a better profit potential, the channel intermediaries can stop the contract |
| **Direct marketing channel** | |
| Characteristics | It is employed when a manufacturer develops an overseas channel. It deals directly with the foreign parties sets the channel, takes care of the international activities, is responsible for physical distribution, exports through its own internal export department |
| Advantages | Direct selling channel enables active marketing exploitation, greater control over the market and elements of marketing mix, improved feedback about the performance of the exported goods, and the manufacturer does not have to agree transaction with middlemen |
| Disadvantages | It is a difficult channel to manage due to unique and unfamiliar foreign market traits. It is an expensive and time-consuming channel, which cannot be affordable without large sale volumes |

The factors influencing the choice of channel levels are the following (Ilesanmi, 2011; Channels of Distribution, n.d.):

1. **Market Considerations.** The nature and type of customers and size of market are important considerations in the choice of a channel of distribution. For example, if the market size is large, there may be long channels, whereas in a small market direct selling may be profitable. The nature and type of consumers include factors such as desire for credit, preference for the stop shopping, demand for personal services, amount of time and effort the customer is willing to spend. It also includes factors like

age, income group, sex, and religion of customers. The main characteristics are:

- type of market;
- number of potential customers;
- geographic concentration of the market;
- order size.

2. **Product Considerations.** The nature and type of product have an important bearing on the choice of distribution channels. For examples, perishable goods need speedy movements and hence shorter channel or route of distribution; For durable goods, longer and diversified channels may be used; Similarly, for technical products requiring specialised selling and serving talents, the shortest channel should be used. The main characteristics are:

- unit value;
- perishability;
- technical nature of a product.

3. **Middlemen Considerations.** The cost and efficiency of distribution depend largely on the nature and type of middlemen. It includes characteristics of middlemen such as availability, attitudes, services, sales potential, costs etc. For example, if the terms and conditions of engaging wholesalers are unfavourable, a manufacturer may like to channelise his products through semi-wholesalers or retailers, thereby, bypassing wholesalers. However, the determining factor would be the differential advantage involved in the choice. The main characteristics are:

- service provided by middlemen;
- availability of desired middlemen;
- producer's and middlemen's policies.

4. **Company Considerations.** The nature, size and objectives of the business firm also play an important role in the selection of distribution channel. It includes financial resources, market standing, volume of production, desire for control of channel, services provided by manufacturers', etc. For example, a company with substantial financial resources need not rely too much on the middlemen and can afford to reduce the levels of distribution. Similarly, a company desiring to exercise greater control over channel will prefer a shorter channel. The main characteristics are:

- desire for channel control;
- services provided by seller;

– ability of management;
– financial resources.

Detailed description of the determinants of channel types is in the Table below.

Table 1.2. Determinants of channel types (Louckx, 2014, P. 26)

| Determinant | Explanation |
|---|---|
| Product | Depending on the product image, the manufacturer may choose to distribute the product in a particular way (e.g. exclusive versus intensive distribution).<br>Product characteristics influence the way goods are distributed (e.g. a low-priced product with high turnover requires an intensive distribution network).<br>Transportation requirements (some products require a special physical distribution, e.g. frozen food, glass).<br>Complexity of a product (for complex products direct selling is preferable) |
| Market | Consumer or industrial market (a product for industrial market is recommended to be distributed through a short channel).<br>Market size and spread from geographic point of view (e.g. if the market is large and widespread, the company has to use a long channel).<br>Shopping habits of buyers.<br>Size of order (e.g. longer distribution channels are preferred if customers buy in smaller quantities and frequently).<br>Local laws can limit choice or forbid some types of channels or middlemen, influence channel width and scope of distribution, force a firm to go through a local agent or distributor |
| Company | Size and financial strength (only large companies can afford own warehouse and transport facilities).<br>Past experience with a particular channel.<br>Reputation.<br>Company's strategic goals |
| Middlemen | Availability in a specific area and experience.<br>Services provided by intermediaries.<br>Increase of number and widening of channels lead to competition among channel members and possibility of conflicts.<br>Channel cost (costs to develop and maintain the channel).<br>Levels of control (price, volumes, promotion, etc.) |

The main factors influencing on choice of direct and indirect channels are mentioned in Table 1.3.

Table 1.3. Factors of direct and indirect channels choice
(based on Channels of Distribution, n.d.)

| Factors | Characteristics of Short Channels (Direct Channel) | Characteristics of Long Channels (Indirect Channel) |
|---|---|---|
| **Market factors** | Business user | Consumers |
| | Geographically concentrated | Markets are fragmented and widely dispersed |
| | Extensive technical knowledge and regular servicing require | Little technical knowledge and regular servicing not required |
| | Large orders | Small orders |
| **Product factors** | Perishable | Durable |
| | Complex | Standardized |
| | Expensive | Inexpensive |
| **Producer factors** | Manufacturer has adequate resources to perform channel functions | Manufacturer lacks adequate resources to perform channel functions |
| | Channel control important (to ensure proper implementation of the total product package and to guarantee a quick response to market conditions) | Channel control not important |
| | Limited product line | Broad product line |
| **Competitive factors** | Manufacturing feels dissatisfied with marketing intermediaries' in promoting products | Manufacturing feels satisfied with marketing intermediaries' in promoting products |

In product characteristics the most important are the following (Rushton, Croucher, Baker, 2014):

1. High-value items are more likely to be sold direct via a short channel, because the high gross profit margins can more easily cover the higher sales and distribution costs that are usual from short channels. In addition, the security aspects of highly priced items (e.g., jewellery, watches) make a short channel much more attractive because there is less opportunity for loss and theft than with a long channel. Short channels also reduce the requirement for carrying inventory of high value goods and the associated poor use of working capital.

2. Complex products often require direct selling because any intermediary may not be able to explain how the product works to potential customers.

3. New products may have to be distributed via a third-party channel because final demand is unknown and supply channels need to be very flexible to respond to both high and low demand levels. Existing own-account operations may find it difficult to deal effectively with the vagaries of new product demand.

4. Time-sensitive products need a “fast” or “short” channel, for shelf-life reasons in the case of food products such as bread and cakes, and relevance in the case of newspapers and tender documents.

5. Products with a handling constraint may require a specialist physical distribution channel, eg frozen food, china and glass, hanging garments and hazardous chemicals.

This chapter has been concerned with marketing channels’ essence, main functions and flows. The main aspects covered were:

– participants in marketing channels: the main participants (producers (manufacturers, originators), middleman/intermediaries (wholesalers, retailers and specialized intermediaries) and final users) in marketing channels were described;

– functions of marketing channels: all marketing channels’ functions were divided into two groups: generic channel functions (product information; product customization; product quality assurance; lot size; assortment; availability; after sales service; logistics) and additional functions;

– flows in marketing channels: types of flows in marketing channels and their directions were introduced – physical flow (material flow); title (ownership) flow; payment flow; information flow; promotion flow; ordering flow; service flow; marketing flow;

– types of marketing channels: types of marketing channels for consumers goods and industrial goods distribution were defined. Characteristics of direct and indirect marketing channels were given. Determinants of marketing channel types were described.

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# SECTION 2

# RELATIONSHIPS IN MARKETING CHANNELS

## 2.1. Multi-channel and omni-channel concepts of marketing channels

In modern conditions consumers want not only buy quality products for good prices but also do it in appropriate place. To satisfy consumers' needs multi-channel and omni-channel conceptions were additionally developed.

To distribute products manufacture can use one of the following concepts: single-channel, cross-channel, multi-channel and omni-channel. Let's explore them in more details.

Manufactures with **single-channel approach** use one (offline or online) marketing channel to distribute product. The price and assortment are determined for the specific channel; the payment method is set up specifically for the channel. The purpose is to make product available for the end consumers.

Manufactures with **cross-channel approach** propose customers' ability to use several channels for the same order. The idea is to mix a brand's channels to smooth the customer experience. "Click & collect" allows clients to order online and get the product in-store, for example. On the opposite, a client tries some clothes in a shop, likes it but isn't 100% sure. He thinks about it later at home and eventually order those clothes online. Another example could be one of a consumer's receiving a coupon via email. He goes to the store to see the product but order it online to take advantage of this voucher. Channels are not in competition anymore, they actually become complementary (Multi-channel, Cross-channel, 2019).

Manufactures with **multi-channel approach propose** customers to use one of the marketing channels to purchase a product: in-store, on mobile, on a tablet, on a computer, etc. Those channels are not connected to one another, it's separate entities among the company, different departments that do not share any data (Multi-channel, Cross-channel, 2019).

Multiple marketing channels are defined as a multi-channel arrangement characterized by the execution of distribution tasks among a combination of distinct channels, direct and/or indirect, resulting in a variety of marketing mix offerings designed to satisfy the needs of diverse target market segments (Fig. 2.1). Two or more of the marketing channels

used by the supplier firm may cover the same target segment(s), although such overlap in the marketplace is not necessarily by design (Goldkuhl, 2005).

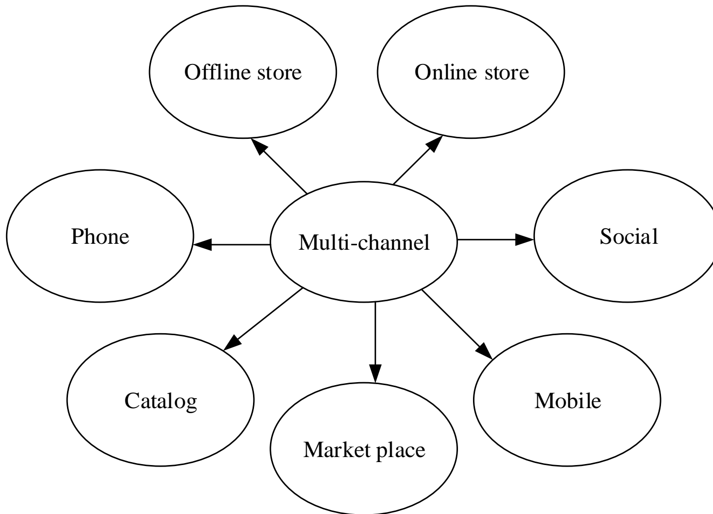


Figure 2.1. Scheme of multi-channel approach

In multichannel marketing, each channel targets a different segment of buyers, or different need states for one buyer, and delivers the right products in the right places in the right way at the least cost (Kotler, Keller, 2012).

So, if a customer is used to order online and goes to the brand's store, other marketing channels won't have access to his purchase history. Channels are in competition with one another, so for multi-channel brands, consumers have to choose one channel and stick to it (Multi-channel, Cross-channel, 2019).

To describe multi-channel approach the term 'click-and-mortar'can be used. The term 'click-and-mortar' denotes an integrated distribution system in which traditional distribution elements (physical stores, warehouses, stocks, information systems for distribution cycle management) are supported by tools made available by the new telecommunication technologies (online shopping, information platforms for distribution management, partnerships to run 'virtual' warehouses). The

expression combines the words click (highlighting the virtual aspect) and mortar (highlighting the physical aspect), thus highlighting the integration of Internet-based (online) business and traditional (onland) elements.

Click-and-mortar businesses are often the combination of a traditional retail business (brick-and-mortar) and an online start-up business. The former can count on market experience, awareness-related assets and brand equity, while the latter contributes knowledge and investments in innovative technology. 'Click' represents the online world: 'dot.com' and 'e-tailer' businesses characterized by innovation, high turnover, potential for development of one-to-one marketing, and ability to reduce the structural and workforce costs that characterize brick-and-mortar businesses to a minimum. 'Mortar' represents the offline world: traditional businesses recognizable by a retail POS sign, customer loyalty, high physical organisation costs, well defined distribution networks, stores and distribution centres or warehouses and customer-handling processes. The concept of click-and-mortar represents the ability to integrate the two worlds (online and offline) and create the ideal combination (Tesser, 2002).

**Advantages** of a multi-channel distribution system are (Tesser, 2002):

1. **Company name.** Businesses already present in traditional markets have a company customer awareness that can be used online without significant additional investments. The trust placed in well-established offline brands also allows consumers to overcome natural suspicion toward the Internet.

2. **Knowledge of demand.** An online distribution channel has specific peculiarities in its approach to customers. However, businesses already operating in other channels possess information about the preferences and habits of their customers that allow the business top concentrate on the true needs of consumers and avoid bad choices and wasted resources.

3. **Reach Same Customers in New Channels**. A multichannel distribution system allows manufacture to provide customers new channels to shop in. Instead of a customer always having to make a trip in-store, they can conveniently buy from you online or another store, like a grocery or department store. Multi-channel allows customer to shop as they want.

4. **Expand Customer Reach.** Selling in multiple channels can lead to new customers. Reaching markets not yet served or complementing an existing market offering. For companies not provided with their own physical distribution network, it might not be considered beneficial to open

points of sale in markets in which the necessary investments and the related cost are not compensated by adequate sales projections. The potential to activate an online presence allows for the overcoming of spatial and temporal barriers through forms of virtual ubiquity and reaching potential customers worldwide at any time, at a limited cost. In markets already served, it becomes possible to supplement what is offered by expanding the range of products (for example, low turn-over products or products not often requested by customers), or time availability (for example seasonal products, that might not be available at certain points of sale).

**5. Grow Sales.** Click-and-mortar companies can tolerate periods of sales below the break-even point on the online channel, since they can count on profits coming from the traditional business. The main advantage of expanding business to new channels is the opportunity to grow sales. New customers and new channels can lead to more opportunities for revenue. Growing sales is a key reason for expanding to new channels.

**6. Well-established infrastructures and distribution logistics.** The delivery cost of digital or digitalizable goods is extremely small, while the delivery of physical goods implies a higher cost exasperated by expectations of ever- shorter delivery times by consumers. Delivery from the physical store closest to the customer could represent the ideal distribution centre, and also the place where the product can be returned.

**Disadvantages** of a multi-channel distribution system are following (Hufford, 2016; Tesser, 2002):

**1. Complexity of multi-channel selling.** It's complicated to sell on multiple channels. Manufacture has inventory to manage, orders to fulfill, and suppliers to work with. All of manufacture's order, items, inventory, and customer data must be exchanged between multiple systems. This complexity can lead to management problems. Online orders can be fulfilled slowly and incorrectly. Inventory levels can be displayed wrong, which can lead to overselling. Product information can be inconsistent across sales channels.

2. **Choosing the right channels to sell on.** First, manufacture needs to be strategic in what channels to choose to sell on. Not every channel is going to be best. Manufactures must think strategically about where customers are, what type of products they sell, and how they run your business.

3. **Invest in a multichannel integration platform.** As multi-channel business plan comes together, manufactures need to think about

how to connect the business. It's too complex to manage multiple systems and processes in their own silos. As each channel can have its own processes, different from other channels, it becomes too difficult to manage.

4. **Distribution costs related to multiple channels.** Usually, the net is introduced instead as an additional channel, complementing the existing ones. The use of technology has the potential benefit of reducing costs, even if it initially implies an increase in the resources employed, and produces benefits only in the medium to long term. Cost containment can be achieved by using the net to sell new products and services, for which no established sale processes exist. The use of Internet-based distribution channels would thus be justified by the progressive coverage of new markets, and a possible change to the existing organisation could be delayed into the future, when suitable financial equilibrium conditions have been reached.

5. **Different channel margins.** A multi-channel distribution strategy usually requires the adoption of different sales prices. The needs expressed by markets can differ depending on the modes in which products and/or services are made available to purchasers. Various reasons can suggest decreasing the price of products sold through Internet-based distribution channels. The development and success of Internet-based electronic commerce is restrained by the prudent and fearful attitudes held by the demand, as is often the case for new technologies. The abandonment of well-tested distribution systems must be motivated by immediately verifiable benefits. A price cut is the simplest way to overcome many fears. On the other hand, a reduction in sales prices does not necessarily have a negative influence on the total net income, since the costs related to the Internet-based selling channel can be significantly lower than traditional distribution channels costs. The impact of such a development leads to a change in the whole cost structure for an industry, with effects to all distribution channels.

6. **Establishment of channels with hybrid features.** The use of Internet in distribution produces competitive advantages easily implemented by the various parties, with limited investment, thus allowing for the expansion of businesses into functions and services previously the exclusive domain of other types of commercial intermediaries. For example, a retailer can continue its traditional sales activity, and at the same time add services that were previously under the exclusive control of

wholesale dealers (such as making a larger selection of products available through an Internet site). In the same way a wholesale dealer can continue its business while complementing it with online retail sales. This is made possible by the fact that final purchasers can easily identify and contact the dealer. Distribution intermediaries could also take up functions previously belonging to manufacturers, such as advice and support on the products sold. Besides the potential for expanding the typical characteristics of specific distribution channels, new organizations also have the opportunity to enter traditional channels and introduce service innovation.

7. **Channel fragmentation.** Channel fragmentation derives from the inability of companies to change their organizational structure and work processes to respond to changes emerging from the introduction of Internet. An example of these difficulties is the inability to integrate the communication flow represented by e-mail into existing processes. Instead of the establishment of a unified, integrated communication channel, fragmentation can ensue due to the inability of marketing managers to coordinate their network business activities. Lack of coordination can be the source of significant problems for a company's business. For example, prices left unchanged on the Internet site when they instead have been modified offline can create confusion among customers and substantially damage brand image. The introduction of a new channel creates new channel management problems, if existing distribution channels have to be reconciled with the new electronic channel. The progressive replacement of traditional with electronic channels can be assumed for digitalizable products, while for the products for which pre- and post-sale services and logistics are of importance, situations of complementary coexistence should be assumed.

There is medium degree of interaction between multi-channels. While using multi-channel approach the price is determined for each channel separately; often the price in an online channel is lower than the one on offline channel; the form of payment is determined for each channel. Also, the assortment can differ depending on the channel; restrictions may be imposed on the sale of some product categories.

Today, consumers tend to use two channels at the same time: using a phone in-store, browsing a tablet when watching TV, etc. So, customers can compare prices or read reviews on their mobile when they are in a store, before purchasing a product for example. And omni-channel approach can customers in it.

Manufactures with **omni-channel** approach allow customers to access real-time information, wherever and whenever they want, no matter the channel used (Fig. 2.2). On the other hand, it empowers brands to break the gap between online and offline (Multi-channel, Cross-channel, 2019). The channels operate independently and often in competition with each other. And there can be considerable variation across the different channels in customer experience, product information, pricing, and service levels (Belu1, Marinoiu, 2014).

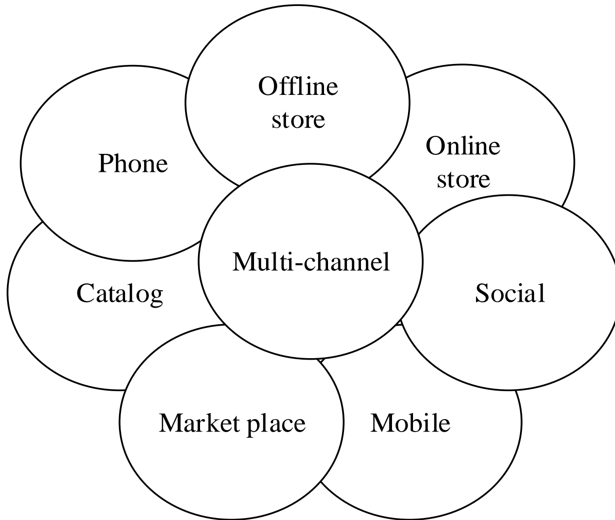


Figure 2.2. Scheme of omni-channel approach

One channel serves another. Let’s say a client goes to a bookstore with a specific need, can’t find it so ask a sales person who will check on one of the shop’s computer. So, the book isn’t available in store anymore but the salesperson says he can order it online, right now, for the client. The client gives his credentials, confirm his address, pays and will receive the book at home (Multi-channel, Cross-channel, 2019).

The omni-channel approach is more complex than the traditional multi-channel approach because the customer experience in every channel must be identical and switching from one channel to another must be seamless. If the retailer knows the preferences of an in-store customer, this information must be shared with the online channel (and vice versa). This

must be done in a timely manner, ideally in real time, as this information could impact buying decisions. Similarly, the retailer must capture each customer interaction in each channel and leverage these purchasing behavior insights to build the optimal omni-channel strategy (Belu1, Marinoiu, 2014).

Important **differences** between multi-channel & omnichannel marketing are (Becker, 2016):

**1. The Channel vs. The Customer.** The multi-channel approach merely aims to get the word out via the maximum possible number of channels. Multi-channel marketing is about casting the widest net to get the most customer engagements; the more the merrier. Companies utilizing the multi-channel strategy are adopting two or more channels to engage their consumers; most popular are social media and email.

Conversely, the omnichannel approach inter-relates every channel to engage with customers as a holistic whole, to ensure they are having a wonderful overall experience with the brand throughout each and every channel. The focus is on building a stronger relationship between consumers and the brand.

In fact, companies with well-defined omnichannel customer experience strategies in place achieve a 91% higher year-over-year increase in customer retention rate on average, compared to organizations without omnichannel programs in place.

**2. Consistency vs. Engagement.** Omnichannel's focus on the customer's experience brings about the second key difference between the strategies: consistency. Omnichannel businesses are diligent in ensuring their customers receive the same experience and messaging through each and every channel.

A consistent brand image and message ensure a heightened sense of familiarity and relationship with the brand. Marketers implementing an omnichannel marketing strategy must ensure that all internal departments are on board and in-tune with the messaging. For example, PR, customer success, social media and sales teams, must all be portraying this consistent message to ensure the strategy implementation is successful.

**3. Effort vs. Effortless.** Another priority of omnichannel marketing is in "understanding how to eliminate effort from the customer experience". There is a tendency to consider the many channels available to connect with consumers today as simply more options to be used. That's more of a multi-channel approach. Omnichannel involves using data to understand where effort exists in the customer experience and how to remove, rather

than add, effort. Omnichannel marketing wants to foster an effortless buying experience for consumers.

**4. Optimization.** More and more of companies try to work across own channels more productively, to enable effective and measurable commerce independent of the channels themselves. That sense of working more efficiently, and optimizing the use of each channel, caters to the omnichannel approach. Omnichannel marketing is all about the individualized and consistent customer experience.

The omni-channel approach aims to enable a seamless personalized customer experience anytime, anywhere, on any device.

Today's leading omni-channel adopters typically focus first on personalizing the in-store shopping experience (stores are and will continue to be the dominant sales channel globally). Leveraging new technologies, these adopters aim to simplify the consumer's in-store journey by removing any friction factors. The second area of focus for today's omni-channel adopters is to personalize customer engagement beyond the store via online, mobile, and social media interactions (Heutger, 2015).

Key areas of seamless omni-channel approach are in the Table below.

Table 2.1. Key areas of seamless omni-channel approach (Heutger, 2015)

| | |
|---|---|
| High-performing, cost-effective omni-channel fulfillment network | 1. Seamless inventory visibility and optimization across channels.<br>2. Flexible dynamic omni-channel warehouses often handling smaller quantities in an ever-decreasing timeframe.<br>3. Leveraging warehouses as showrooms and enabling customer fulfillment activities such as pick-ups.<br>4. Logistics marketplaces and real-time consumer engagement |
| Enhance speed, exibility and convenience in last-mile delivery | 1. Leveraging stores for fulfillment, thereby increasing microwarehouses.<br>2. Anytime, anywhere delivery models.<br>3. Expanding the range of omni-channel value-added services |

The main ways of omni-channel are(Heutger, 2015):

1. Personalized in-store shopping experience:

– merging online and offline experience in the store;
– easing navigation with in-store robots;

– driving traffic to stores with 'on-the-go' promotions;
– providing store shopping assistance from home.

2. Personalized customer engagement beyond the store:

– offering virtual expert advice;
– utilizing social media;
– leveraging customer loyalty;
– simplifying replenishment and automated services;
– customizing products.

Also, an important question is the difference between traditional and omni-channel fulfillment (Table 2.2).

Table 2.2. Differences between traditional and omni-channel fulfillment (Heutger, 2015)

| Traditional Fulfillment Model | Omni-channel Fulfillment Model |
|---|---|
| 1. Dedicated inventory by channel; limited to no cross-channel visibility.<br>2. Channel-specific warehouses:<br>– scope: online or offline. B2B or B2C. Retail store or home delivery;<br>– fixed space; no flexibility to move from one location to another.<br>3. Warehouses used purely for storage and processing<br>4. Reactive customer management with time-consuming quotes, focus on status reporting | 1. **Seamless inventory visibility** and optimization across channels.<br>2. **Omni-channel warehouses**<br>– scope: Online and offline. B2B and B2C. Delivery to stores and homes;<br>– dynamic space allocation within network and _exible contract terms.<br>3. Warehouses used as **showrooms** or for **customer-facing** activities.<br>4. **Proactive and personalized customer management** with logistics marketplaces and focus on maximizing value for the customer |

Brick-and-mortar stores remain a crucial component of the global shopping experience, and their role is changing in the omni-channel business model. Stores are becoming fulfillment centers, serving as pick-up locations for online orders (buy online, pick up in-store) and fulfilling local deliveries in the city (ship-from-store). More businesses are likely to adopt these programs in the omni-channel journey to generate maximum return on their brick-and-mortar investments.

Collaboration is fueling another innovation. Today, many e-retailers are partnering with brick-and-mortar retailers to enable speedy and cost-effective delivery by leveraging store merchandise. The stores benefit

because the e-retailer provides an additional sales channel. The e-retailer benefits by leveraging stores as fulfillment centers

Next highlight key success factors of the omni-channel journey (Heutger, 2015):

1. Focus on the consumer journey. Great customer experiences start with great interactions at every opportunity. It is essential to understand the end customer's cross-channel journey and develop solutions and systems that meet the customer's expectations.

2. Organize as per the consumer journey. To create a seamless consumer experience, the organization may have to change, aligning itself with the omni-channel shopper. Companies cannot retain separate online and offline organizations for marketing, merchandising, and logistics. Instead, they must create one common strategy and vision for an omni-channel customer experience.

3. Optimize the omni-channel supply chain network. Optimizing the supply chain network in support of an omni-channel approach requires the following steps:

**3.1. Integrate inventory across channels and in transit.** This requires significant technology investment and may also require a review of the existing inventory allocation and ownership model.

**3.2. Design a flexible and dynamic distribution network.** Can existing storage and processing capacity be translated into a virtual network? Can this be managed and reallocated based on demand? Are suppliers and logistics providers appropriately aligned with flexible, dynamic contract terms?

**3.3. Expand the utilization of physical assets in support of the omni-channel strategy**. Could stores, warehouses, and distribution centers serve a greater role in directto consumer fulfillment (in some or all locations, and possibly with phased introduction)? Is it possible to segment and evaluate fulfillment options based on product characteristics such as value, volume, seasonality, service requirements, and margin?

**3.4. Consider innovative last-mile delivery options**. Do last-mile capabilities complement the product portfolio and omni-channel customer expectations? Companies must model the preferred delivery options for cost impact to select the right approach. Would it be better to develop in-house delivery centers or outsource to service providers?

Consumers' expectations for omni-channel experience are the following (Heutger, 2015):

1. Fast delivery.

2. Product variety and availability.
3. Enhanced search functionality.
4. Flexible delivery options.
5. Easy return and exchange.

## 2.2. Cooperation, competition and conflict in marketing channels

The main phases of interaction between participants of a marketing channel are (Кирюков, 2010, с. 90):

1. **Phase of verification:** identification of the role and position of the participants, first contacts, peer review.
2. **Provision of positions:** gathering channel members during the transition, use of strategic units for business run, establishing forms of communication.
3. **Consensus and co-operation:** development of one common idea, mission and strategy, the establishment of interaction and co-operation, the coordination of existing participants' activities.
4. **Reliability channel practice:** participants' identification of their positions, missions and overall strategy, achievement of synergistic effect from the results of interaction.

Communication in channel can be evaluated using such indicators (Кирюков, 2010, с. 91):

1. Adequacy of the transmitted information.
2. Speed of information transfer.
3. The level of feedback.
4. Efficiency of the received information processing.
5. The level of information technology used in the information's processing and transmission.
6. Reliability of communication flows.

There are following types of interaction of marketing channel participants:

- cooperation;
- conflicts;
- competition.

**I. Cooperation** involves the exchange of information, conclusion of agreements, partnerships, strategic alliances, development of marketing systems - horizontal, vertical, etc.

Factors influencing the formation of the cooperation are (Біловодська, 2010, с. 256):

- interdependence;
- the key role of specialization;
- the ratio of forces.

For cooperation (strategic alliances and partnerships) to be effective, the following conditions are required (Біловодська, 2010):

- recognizing the interdependence of channel members;
- close relationship with the channel members;
- definition of roles and functions (common rights and responsibilities of each channel member);
- concerted actions aimed at achieving the overall goal (s);
- channel members' trust and relationships.

**II. Competition** in channels is characterized by mutual confrontation, which aims to gain some benefit (in retail, for example, from the provision of additional services, goods at lower prices, etc.). The competition clearly identifies and realizes the goals, the result.

The peculiarity of competition is the use of only those forms of struggle that are recognized as morally and economically legal.

Moreover, competition may or may not be accompanied by conflict. The competition is most clearly represented in the retail market, while taking the forms of internal and mutual (Біловодська, 2010).

Internal competition takes place between trade enterprises similar in specialization and size, equivalent in scale and scope.

Mutual competition consists in competition between trade enterprises with different degree of trade organization, volumes of turnover.

There are following types of competition (Competition and conflict, 2015):

1. **Horizontal competition** is competition between firms of the same type at one channel level; for example, an automobile manufacturer versus another automobile manufacturer, a plumbing supply wholesaler versus another plumbing supply wholesaler, or one supermarket versus another. This is the most visible and frequently discussed form of competition. In economic theory, much of the treatment of competition deals with this horizontal type, although it is usually referred to simply as "competition," and often the firms involved are producers or manufacturers rather than wholesalers or retailers.

2. **Intertype competition** is competition between different types of firms at the same channel level but with different essence of actions; for example, the off-price store versus the department store or the merchant wholesaler versus agents and brokers.

3. **Vertical competition** is competitions between channel members at different levels as they both compete, such as wholesale versus manufacture.

4. **Competition between marketing channels** is competition of one marketing channels with another. Channel system competition refers to complete channels competing with other complete channels.

**III. Channel conflict** arises when the behavior of a channel member is in opposition to its channel counterpart. It is opponent centered and direct, in which the goal or object sought is controlled by the counterpart (Coughlan et al., 2001, cited in Goldkuhl, 2005).

The three type of channel **conflicts** which can occur are

**1. Horizontal channel conflicts** (Mack**,** 2019; Bhasin, 2017). A horizontal conflict refers to a disagreement among two or more channel members at the same level (Fig. 2.3).

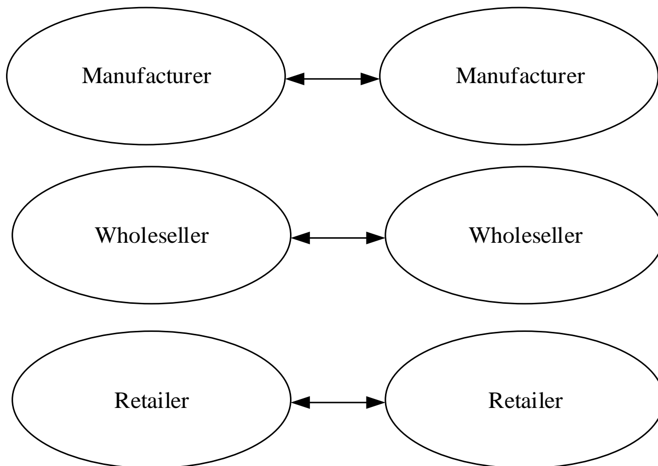


Figure 2.3. Horizontal channel conflicts

For example, suppose a toy manufacturer has deals with two wholesalers, each contracted to sell products to retailers in different regions. If one wholesaler decides to branch its operations into the other

wholesaler's region, a conflict will result. If the toy manufacturer doesn't help solve the problem, its business dealings with both the wholesalers – and the downstream retailers, as well – might be in jeopardy. So, a conflict between 2 distributors or a conflict between 2 retailers is known as horizontal channel conflict.

**2. Vertical channel conflict** (Mack, 2019; Bhasin, 2017). Another type of conflict seen in channel management is the vertical channel conflict (Fig. 2.4). Where the horizontal channel conflict exists between players within the same level of the distribution channel, the vertical channel conflict happens at different levels of the distribution channel. Vertical conflicts involve a disagreement between two channel members on consecutive levels. A typical conflict might be between the retailer and the distributor, or it might be between the distributor and the company. For example, if the toy manufacturer discovers its products are arriving at retail stores later than scheduled, a conflict might develop between the manufacturer and the wholesaler responsible for shipping to retailers. At the same time, the retail stores might be in conflict with the wholesaler due to its inability to ship products on time.

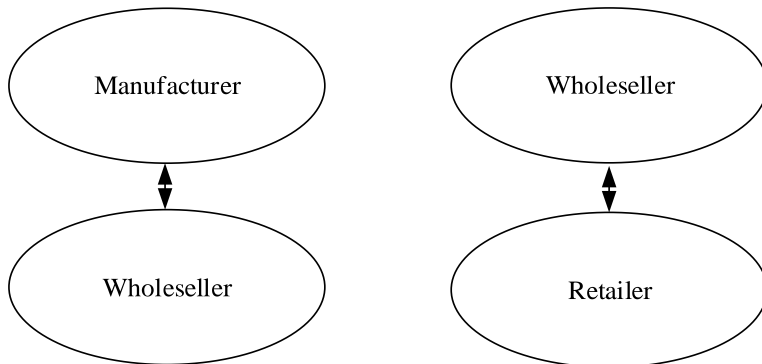


Figure 2.4. Vertical channel conflict

Handling vertical channel conflicts is far difficult for companies as compared to handling horizontal conflicts. Horizontal conflicts always happen at a lower level then the company. But vertical channel conflicts might involve the manufacturer or the distributors themselves. Hence, managing vertical channel conflicts becomes important for the company.

**3. Multiple channel conflict** (Mack, 2019; Bhasin, 2017; Kotler, Keller, 2012). Multichannel conflicts refer to disagreements among members in separate marketing channels (Fig. 2.5). While neither strictly horizontal nor vertical, these conflicts can affect all members of every channel. For instance, suppose the toy manufacturer participates in two marketing channels. In the first channel, the manufacturer sells its products directly to consumers via its official website. In the second channel, the manufacturer sells its products to wholesalers for resale to retailers. If the toy manufacturer's website sells the products for much lower prices than retail stores, sales in the second channel will plummet. The resulting conflict will require some solution that works for both channels. Multichannel conflict exists when the manufacturer has established two or more channels that sell to the same market. It's likely to be especially intense when the members of one channel get a lower price (based on larger-volume purchases) or work with a lower margin.

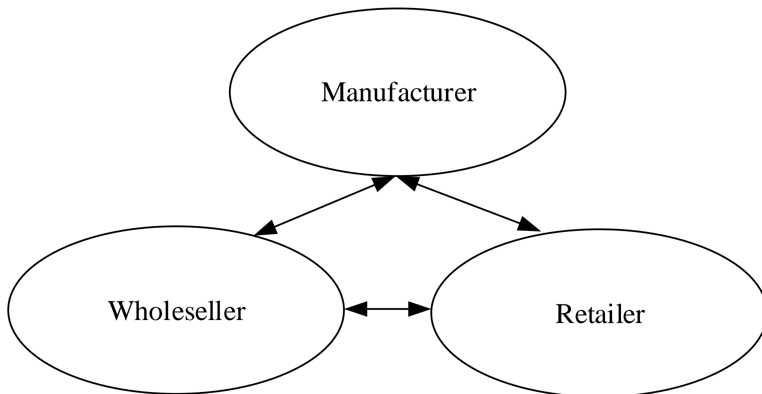


Figure 2.5. Multiple channel conflict

When small retailers and businessmen were thriving in business, modern retail came in the picture. Large hypermarkets and malls were started where people could do all their shopping. An altogether different distribution channel was created. Due to their bulk buying power, these hypermarkets were giving huge discounts and making huge sales as well.

As a result, many companies were boycotted by small retailers because they felt left out and they could not cope with the price. This created a huge multiple channel conflict with small retailers standing in

unity against the tyranny of large markets. Ultimately, the companies had to come in and settle the dispute by maintaining the price across multiple channels. So, they set a standard price of products, whether it was selling in hyper markets or small retail.

Now, the same thing is repeating but the players are three fold – small business, modern retail and e-commerce. E-commerce went a step ahead of modern retail and even small businessmen got back at modern retailers by offering even lower prices on online platforms. There was no store to be leased, no rent to be paid, not a dollar to be spent but only material had to be bought and it had to be shipped. The lower the price of buying, the lower the selling price.

In the times of e-commerce, hypermarkets had leased huge spaces for which they were paying sky high rents. When E-commerce started, hypermarkets dropped a bit in demand and today all of them are fighting each other. It is a constant multiple channel conflict for each company because if there are lower prices anywhere, it immediately gets public and then the other channel starts complaining or demanding lower prices. Furthermore, one channel might complain about the other and vice versa.

In the end, these are the three types of channel conflicts which exist in channel marketing. Horizontal conflict might be quite regular but its effect will be localised. Vertical conflict is not regular and its effect might be regional. Because of their very nature, vertical channel conflicts happen rarely, but once they happen, they have a long-lasting effect. However, multiple channel conflict generally has a national level effect because it always occurs when the company has made major changes (Bhasin, 2017).

Some causes of channel conflict are easy to resolve; others are not. Conflict may arise from (Kotler, Keller, 2012; Marketing Channel, n.d.):

**1. Goal incompatibilities:** each member of the marketing channel has his own set of goals and objectives that are very often incompatible with those of other channel members – the manufacturer may want to achieve rapid market penetration through a low-price policy; dealers, in contrast, may prefer to work with high margins and pursue short-run profitability.. When goals of two or more members are incompatible, conflicts may result and incompatible goals often arise between channel members for example the most common conflict issues, which arise between manufacturer and industrial distributor are:

– how to handle large accounts;
– the required inventory stocking levels;
– the quality of distributors management;

– size of distributor's margin.

Clearly underline many of these issues, are the difference in goals, aims and values among channel members involves. Furthermore, in consumer goods market there are literally items of thousands of small retailer served by large manufactures. Large manufacturers tend to be growth oriented where as small retailers are more interested in status quo. The likelihood of the conflict is high in such situation is because in their pursuit of policies that re congruent with their dynamic goal.

**2. Role incongruities** (unclear roles and rights): a role is a set of perception defining what the behavior of position member should be. When applied to the marketing channel, any given member of the channel has a series to role to which he is expected to fulfil. For example, a franchiser is expected to provide extensive management assistance and promotional support for his franchises. In return the franchisees are expected to operate in strict accordance with the franchiser standards operating procedure. If either of the franchisee or franchiser deviate from his role, conflict situation may result.

**3. Perceptual difference:** perceptions refers to the way an individual selects and interprets environmental stimuli. The manufacturer may be optimistic about the short-term economic outlook and want dealers to carry higher inventory, while the dealers may be pessimistic. The way stimuli are perceived however is often quite different from objective reality. In a marketing channel context, the various channel members may perceive the same stimuli but attach different interpretation to them. A common example of this is the case of sale material provided by manufacturing company for their retailer to put on at their retail counters. From the company point of view these sale materials are valuable promotional tools needs to move their products of the retailer shelves. Whereas the retailer often perceives the material as useless junk which serves only to take up its valuable space.

**4. Intermediaries' dependence on the manufacturer:** the fortunes of exclusive dealers, such as auto dealers, are profoundly affected by the manufacturer's product and pricing decisions. This situation creates a high potential for conflict.

**5. Resource scarcities:** this refers to conflict stemming between channel members over the allocation of some valuable resources needed to achieve their respective goals. A common example of this is the allocation of resources between the wholesaler and the salesman. In the case both wholesaler and salesman as a valuable resource necessary to achieve their

target view the retailer. Frequently the wholesale distributor decides to keep some of high volume retailers for himself as his accounts. This leads to objection by salesperson over what they consider to be an unfavorable allocation of resources. This kind of disputes is often one of the conflicts.

**6. Expectational difference:** various channel members have expectations about the behavior of the other channel members. In practice, these expectations are predictions or forecast concerning the future behavior of the other channel members. Sometimes this forecast turns out to be inaccurate but the channel members who make the forecast will take action based on the predictive outcome. By doing so, he can elicit a response behavior from other channel member which might now have occurred in the absence of the original action. An example of this could be seen at the retail end where a retailer expects stock on credit due to his past experience, now if the salesman, upon instructions of the distributor, tries to tightens the credit suddenly the retailer might refuse to oblige, resulting in possible conflict.

**7. Decision domain disagreement:** each channel member explicitly or implicitly carves out for himself an area of decision making which he feels is exclusively his own. In contractual channel system such as franchise, the decision domain is quite explicit and usually spelled out clearly in franchise contract. But in more traditional loosely aligned channels made up of independent firms, the decision domains are sometime up for grabs. Hence conflicts can arise over which member has the right to moves to make the decision.

**8. Communication difficulties:** Communication is the vehicle for all interactions among these channel members. Whether such interactions are cooperative or conflictive. A foul up or break down in the process of communication can turn quickly a cooperative relationship into a conflicting one. For example, manufacture often make changes in product design, prices and promotional strategies. The resellers generally feel that they are entitled to ample advance notice of such changes so that they can make appropriate strategic adjustments, if necessary. If adequate communication is not provided and these failing results in negative consequences for a channel member, severe conflict can result.

**9. Lack of channel planning:** lack of a clear work plan for the channel as a whole and its participants in particular; uncertainty of the desired results of the channel.

**10. Competition within the channel for certain functions:** different channel participants claim to perform the same functions, which may cause duplication of work or failure to perform other functions.

**11. Desire to control the situation alone:** each channel participant explicitly or implicitly reserves the right to make certain decisions, in some cases this may be an exclusive right, regardless of the desire of other participants to also address these issues.

**12. Lack of motivation for activity:** inconsistency of measures to stimulate and motivate channel participants with their real needs and requests; incorrectly selected tools to stimulate and motivate channel participants.

Some channel conflict can be constructive and lead to better adaptation to a changing environment, but too much is dysfunctional. The challenge is not to eliminate all conflict, which is impossible, but to manage it better. Verbal reprimands, fines, withheld bonuses, and other remedies can punish a firm in violation and deter others.

The mechanisms for effective conflict management are the following (Kotler, Keller, 2012):

1. **Strategic Justification.** In some cases, a convincing strategic justification that they serve distinctive segments and do not compete as much as they might think can reduce potential for conflict among channel members. Developing special versions of products for different channel members is a clear way to demonstrate that distinctiveness.
2. **Dual Compensation**. Dual compensation pays existing channels for sales made through new channels.
3. **Superordinate Goals**. Channel members can come to an agreement on the fundamental or superordinate goal they are jointly seeking, whether it is survival, market share, high quality, or customer satisfaction. They usually do this best when the channel faces an outside threat, such as a more efficient competing channel, an adverse piece of legislation, or a shift in consumer desires.
4. **Employee Exchange**. A useful step is to exchange persons between two or more channel levels. Manufactures' executives might agree to work for a short time in some dealerships, and some dealership owners might work in manufactures' dealer policy department. Thus participants can grow to appreciate each other's point of view.
5. **Joint Memberships**. Similarly, marketers can encourage joint memberships in trade associations. The associations can consider issues

between food manufacturers and middlemen and resolve them in an orderly way.

6. **Co-optation.** Co-optation is an effort by one organization to win the support of the leaders of another by including them in advisory councils, boards of directors, and the like. If the organization treats invited leaders seriously and listens to their opinions, co-optation can reduce conflict, but the initiator may need to compromise its policies and plans to win outsiders' support.

**7. Diplomacy, Mediation, and Arbitration**. When conflict is chronic or acute, the parties may need to resort to stronger means. **Diplomacy** takes place when each side sends a person or group to meet with its counterpart to resolve the conflict. **Mediation** relies on a neutral third party skilled in conciliating the two parties' interests. In **arbitration**, two parties agree to present their arguments to one or more arbitrators and accept their decision.

8. **Legal Recourse**. If nothing else proves effective, a channel partner may choose to file a lawsuit.

The main ways of resolving conflicts in marketing channels according to Thomas Kilmann model are in Table below.

Table 2.3. The main styles of resolving conflicts in marketing channel (based on Коротков А.В., Пилипчук В.П., Сагер Л.Ю.)

| Conflict resolution style | Events |
|---|---|
| 1 | 2 |
| Competing | – forced resolution of the conflict;<br>– individual development and approval of the channel's plan and strategy;<br>– ensuring cooperation in marketing channels by creating vertical marketing systems;<br>– change of channel owner |
| Avoiding | – supply of various goods to the market through various intermediaries;<br>– determining the scope of influence on the market of intermediaries, by assigning them to certain clients or individual territories;<br>– regular assessment of channel participants and adjustment of cooperation's conditions depending on their success in the goods' distribution;<br>– adjustment of the client base, termination of work with those who do not fulfill their obligations |

Table 2.3 (continued)

| 1 | 2 |
|---|---|
| Collaborating | – mediation: the third party tries to resolve the conflict by persuading the parties, conducting negotiations, making recommendations on certain issues;<br>– joint membership in trade and other associations;<br>– arbitration;<br>– development of partnership relations, which provide financial support (favorable terms;<br>– creation of a commission or group to investigate the causes of the conflict and its elimination;<br>– exchange of employees between channel participants to increase mutual understanding;<br>– development of the work's general strategy;<br>– change of channel owner;<br>– co-optation: joint management and collegial decision-making |
| | – |
| Accommodating | – exchange of employees of participating companies to develop mutual understanding;<br>– mediation: the third party tries to resolve the conflict by persuading the parties, negotiating, making recommendations on the issue;<br>– search for mutually beneficial solutions in a conflict situation, improving the work of the mediator;<br>– directing activities to achieve the goals set by other participants of the channel;<br>– performance of roles and functions that are put forward individually by individual participants of the channel |
| Compromising | – constant consultations of participating companies with each other to harmonize interests and business plans;<br>– diplomacy: conducting negotiations with channel participants, collecting and disseminating information of interest to participants and allowing them to respond quickly to received signals;<br>– joint development and approval of the tasks list;<br>– adoption of superordinate goals (goals that can be achieved through the interaction of all parties) |

Also, use of multi-channel approach can cause both internal and external conflicts in marketing channel.

Internal conflicts manifest themselves between two or more channels dedicated to the same market. External conflicts involve third parties. Direct channels are almost exclusively subject to internal conflicts, while indirect channels manifest both internal and external conflicts.

Four types of **internal conflict** can be identified, often cross-correlated (Tesser, 2002):

1. Cannibalisation between channels. The creation of a new distribution channel almost inevitably leads to the redistribution of the total sales volume among the different channels, automatically giving rise to the cannibalisation of existing channels by the newly formed ones. In organizations with an orientation toward channels rather than toward customers, friction amongst the different channel managers emerges. Incentives are usually tied to the volume moved through the sales channel. Therefore, each channel tends to maximize its sales volume, even if this damages the other channels. The danger of cannibalisation does not only involve Internet, but becomes more evident when a new channel is activated.

2. Under-utilization of property. Traditional sales channels need various kinds of physical structures: warehouses, branch offices, call centres, etc. The optimisation of the number, size and use of these resources is crucial since they generate a high proportion of total company costs. Therefore, if a sizable fraction of the manufactured volume were to be transferred onto the online channels, the cost structure would be changed, with possible significant negative effects on corporate income.

3. Price conflicts. Online prices tend to be substantially lower than for other channels, since the former – usually referred to Internet based companies – benefit from lower primary costs and have lower margins than what is considered acceptable by traditional companies. Companies operating with a multi-channel system are the first to face this problem: to remain competitive online they must accept the prices imposed by online competitors. This policy, however, also influences prices through other channels. Customers can hardly accept different prices for the same product sold by different channels. Therefore, the company is forced to adjust the prices for all channels. However, a policy of price differentiation, when planned, can be an excellent tool to transfer customers from traditional and more costly channels to online channels.

4. Unsynchronised channels. Using a brand in the dot.com version of the company without any ties to the ‘traditional’ company can undermine success in the online channel. Indeed, customers tend to perceive the company as a whole, independently of the distribution channels: they just choose the most advantageous one, without considering the potential that they could be run by independently managed companies.

On the contrary, they expect a certain degree of integration between the online and offline channels.

Three main sources of **external conflict** as identified are (Tesser, 2002):

1. Establishment of a direct sale channel by manufacturers. Manufacturers using indirect channels to reach markets can, using Internet, supplant intermediaries. The setup of a direct sales channel could hence be opposed by indirect sale organisations. These commercial partners could actually abandon the company and switch to the competition, thus determining sizable negative effects for the business as a whole. In most industries, most sales are still made through traditional channels, and therefore companies must decide whether to risk losing revenues and the relationship with external organisations to establish direct channels based on e-commerce technologies.

2. Loss of control over sales channels. Even if companies seldom control the relationship with customers directly, they try to control their sales channels through: the establishment of planned sales areas, the distribution of operational guidelines to the retailers, product presentation and promotions. These forms of control become very difficult to apply, however, if the distributors choose the online channel as a distribution method.

3. Shifts within the value creation chain. Even when manufacturers decide not to sell their products directly online, the presence of Internet sites determines a change in the relative strength of the partners operating in the distribution network. Very important functions, such as the information provided by dealers to customers can now be implemented directly by the manufacturer, thus changing the value creation chain and redefining the role of dealers very significantly. The automotive industry offers an important example of this mechanism. The online search for information about cars has become a well-established part of the car purchase process. The important role of the dealer thus disappears, reducing his importance and hence his contractual power with respect to the parent company.

Thus, conflicts constantly arise in marketing channels. However, timely and correct measures can help to reduce the negative impact or resolve conflicts constructively.

## 2.3. Motivation of marketing channels' members

**Stimulation in marketing channel** is an external influence of the manufacturer on intermediaries through appropriate incentives, which ensures cooperation between the manufacturer and the intermediary in order to implement the strategy of the channel, solve problems and perform work. **Motivation of participants in marketing channels** is a strategic direction of the manufacturer, aimed at forming an internal need, an unconscious motive to interact with the manufacturer and implement tasks. Thus, stimulation is a component of the motivation process.

Stimulating and motivating the participants of the marketing channel allow to achieve the following goals:

- ensuring cooperation between the manufacturer and intermediaries;
- solving the tasks set by the channel (implementation of plans for product sales, winning new customers and new markets, minimizing costs, etc.);
- establishing trust and a favorable atmosphere of interaction in channels;
- conflict reduction or elimination;
- reducing the risk of non-sales of products as a result of participants' insufficient motivation;
- reduction or elimination of high staff turnover and cases of trade secrets;
- increasing the channel's resilience to adverse environmental conditions, including fierce competition;
- increasing market power and market influence of the channel.

Motivation refers to the actions taken by the manufacturer to foster channel member cooperation in implementing the manufacturer's distribution objectives.

Importance of motivating channel members (Jain, Bhardwaj, Goel, 2014):

1. Build preference for brands:

- motivational tools help to ensure that channel members give preference to company's product over competitor's product;
- motivation plays an important role in winning channel member's mind share;

– by winning mind share, channel member recommended or actively promote company's product over competitor's product.

2. Add value to product offer:

– motivating intermediaries is an important strategy for influencing channel members behavior;

– offering training programs or marketing support to members add value to the relationship between supplier and channel by helping them to improve their performance and grow their own business;

– a strong relationship makes it easier to launch new products or marketing campaigns through the channel, helping to build revenue and profits.

3. Increase sales through the channel:

– financial Incentives are an important source of motivation to channel members;

– by offering discounts on purchases above an agreed level channel member can be encouraged to stock or sell more products;

– financial incentives help in launching new products, increase sales of existing products and widen distribution base.

4. Improve performance:

– motivation helps channel members to improve their performance;

– offering them different bonus or discount levels, marketing and training support, performance level can be enhanced.

There are three basic facets involved in motivation management (Motivating the channel, n.d.; Rosenbloom, 2012):

1. Finding out the needs and problems of channel members.

2. Offering support to the channel members that is consistent with their needs and problems.

3. Providing leadership through the effective use of power.

We'll explore these facets in more details (Motivating the channel, n.d.; Rosenbloom, 2012).

**1. Finding Out the Needs and Problems of Channel Members.** Before the channel manager can successfully motivate channel members, an attempt must be made to learn what the members want for the channel relationship.

Manufacturers are often unaware of or insensitive to the needs and problems of their channel members.

Approaches for Learning about Channel Member Needs and Problems. All marketing channels have a flow of information running through them as part of the formal and informal communications systems that exist in the channel.

Ideally, such systems would provide the manufacturer with all of the information needed on channel member needs and problems. However, most marketing channel communication systems have not been formally planned and carefully constructed to provide a comprehensive flow of timely information.

Consequently, the channel manager should not rely solely on the regular flow of information coming from the existing channel communication system for accurate and timely information on channel member needs and problems.

There is a need to go beyond the regular system and make use of one or all of the following four additional approaches (Motivating the channel, n.d.; Rosenbloom, 2012):

1) **research studies of channel members.** Most manufacturers never conduct research of channel member needs and problems. Estimates indicate that less than one percent of manufacturers' research budgets are spent on channel member research;

2) **research studies by outside parties.** Research designed and executed by a third party is sometimes necessary if complete and unbiased data on channel member needs and problems are to be obtained. The use of outside parties to conduct research on channel member needs and problems provides higher assurance of objectivity;

3) **marketing channel audits.** The basic thrust of this approach should be to gather data on how channel members perceive the manufacturer's marketing program and its component parts, where the relationships are strong and weak, and what is expe cted of the manufacturer to make the channel relationship viable and optimal.

For example, a manufacturer may want to gather data from channel members on what their needs and problems are in areas such as (Motivating the channel, n.d.; Rosenbloom, 2012):

– pricing policies, margins, and allowances;

– extent and nature of the product line;

– new products and their marketing development through promotion;

– servicing policies and procedures such as invoicing, order dating, shipping, warehousing and others;

– sales force performance in servicing the accounts.

Further, the marketing channel audit should identify and define in detail the issues relevant to the manufacturer-wholesaler and/or manufacturer-retailer relationship. Whatever areas and issues are chosen, they should be cross-tabulated or correlated as to kind of channel members, geographical location of channel members, sales volume levels achieved, and any other variables that might be relevant.

Finally, for the marketing channel audit to work effectively, it must be done on a periodic and regular basis so as to capture trends and patterns. Emerging issues are more likely to be spotted if the audit is performed on a regular basis.

4) **distributor advisory councils.** Three significant benefits emerge from the use of a distributor advisory council. First, it provides recognition for the channel members. Second, it provides a vehicle for identifying and discussing mutual needs and problems that are not transmitted through regular channel information flows. And third, it results in an overall improvement of channel communications, which in turn helps the manufacturer to learn more about the needs and problems of channel members, and vice versa (Motivating the channel, n.d.; Rosenbloom, 2012).

**2. Offering Support to Channel Members.** Support for channel members refers to the manufacturer's efforts in helping channel members to meet their needs and solve their problems. Such support for channel members is all too often offered on a disorganized and ad hoc basis.

The attainment of a highly motivated cooperating "team" of channel members in an interorganizational setting requires carefully planned programs.

Such programs can generally be grouped into one of the following three categories: 1) cooperative, 2) partnership or strategic alliance, and 3) distribution programming (Motivating the channel, n.d.; Rosenbloom, 2012):

1. **Cooperative arrangements.** Cooperative arrangements between the manufacturer and channel members at the wholesale and retail levels have traditionally been used as the most common means of motivating channel members in conventional, loosely aligned channels. The underlying rationale of all such cooperative programs, from the

manufacturer's point of view, is to provide incentives for getting extra effort from channel members in the promotion of the products.

Cooperative Arrangements:

- focuses on channel member needs & problems;
- simple & straightforward;
- conveys a clear sense of mutual benefit.

Typical types of cooperative programs provided by manufacturers to channel members are:

- cooperative advertising allowances;
- payments for interior displays;
- contests for buyers, salespeople, etc.;
- allowances for warehousing functions;
- payments for window display space;
- demonstrators;
- coupon-handling allowance;
- free goods;

2. **Partnerships and strategic alliances.** Partnerships or strategic alliances stress a continuing and mutually supportive relationship between the manufacturer and its channel members in an effort to provide a more highly motivated team, network, or alliance of channel partners (Motivating the channel, n.d.; Rosenbloom, 2012).

Webster points to three basic phases in the development of a "partnership" arrangement between channel members (Motivating the channel, n.d.; Rosenbloom, 2012):

- an explicit statement of policies should be made by the manufacturer in such areas as product availability, technical support, pricing and any other relevant areas;
- an assessment should be done of all existing distributors as to their capabilities for fulfilling their roles;
- the manufacturer should continually appraise the appropriateness of the policies that guide his or her relationship with channel members.

**Strategic Distribution Alliance**:

1) characteristics: enduring connections; substantial connections.

2) what sets sda apart from others: trust; commitment; norm-based motivation (solidarity, mutuality, continuity).

3) building commitment: expectation of continuity; bilateral communication; balanced power between the two; commitment is mutual.

**3. Distribution programming.** Distribution programming: "a comprehensive set of policies for the promotion of a product through the channel" (Motivating the channel, n.d.; Rosenbloom, 2012).

The essence of this approach is the development of a planned, professionally managed channel.

The first step in developing a comprehensive distribution program is an analysis by the manufacturer of marketing objectives and the kinds and levels of support needed from channel members to achieve these objectives.

Further, the manufacturer must ascertain the needs and problem areas of channel members.

Distribution programming is:

– developed as a joint effort between the manufacturer and the channel members to incorporate the needs of both;

– offer all channel members advantages of vertically integrated channel and allow them maintaining their status as independent business firms.

Nevertheless, virtually all of the policy options available can be categorized into three major groups (Motivating the channel, n.d.; Rosenbloom, 2012):

– those offering price concessions to channel members;
– those offering financial assistance;
– those offering some kind of protection for channel members.

**3. Providing Leadership to Motivate Channel Members.** Control must still be exercised through effective leadership on a continuing basis to attain a well-motivated team of channel members.

In attempting to exercise such leadership, however, the channel manager must remember to deal with several significant challenges' characteristic of the interorganizational setting of marketing channel. Among these are:

– the looseness of the organization of many channel systems;

– a proclivity (tendency) by channel members to avoid central direction;

– lack of single ownership;

– no clear demarcation (separation) of a superior subordinate relationship.

Seldom is it possible for the channel manager to achieve total control, no matter how much power underlies his or her leadership attempts. For the most part, a theoretical state, where the channel manager

were able to predict all events related to the channel with perfect accuracy, and achieve the desired outcomes at all times, does not exist or is not achievable in the reality of an interorganizational system such as the marketing channel. Little explained succinctly the problems of achieving very high levels of control and leadership in this interorganizational setting when he said: “Because firms are loosely arranged, the advantages of central direction are in large measure missing. The absence of single ownership, or close contractual agreements, means that the benefits of a formal power (superior, subordinate) base are not realized. The reward and penalty system is not as precise and is less easily affected. Similarly, overall planning for the entire system is uncoordinated and the perspective necessary to maximize total system effort is diffused. Less recognition of common goals by various member firms in the channel, as compared to a formally structured organization, is also probable” (Motivating the channel, n.d.; Rosenbloom, 2012).

Methods of motivating participants in marketing channels are in Table below.

Table 2.4. Methods of motivation in marketing channels
(based on Кирюков1, 2011; Кирюков2, 2010; Channel motivation, n.d.; Jobber, 2001; Osman, 2008; Rosenbloom, 2012; Shipley, 1984)

| Method of motivation | Positive results | Negative results |
|---|---|---|
| 1 | 2 | 3 |
| *Economic methods of motivation* | | |
| Discounts, including | - the main source of intermediary’s income;<br>- encouragement of intermediaries’s current sales | - intermediary’s perception of the manuf'acturer's products as secondary, as a result – low motivation to make efforts to bring it to market |
| - volume discounts (quantity discounts) | - stimulating the distribution of goods’ that require intensive distribution and high availability (mass consumption goods);<br>- purchase of more products either within a specific order or over a period of time (cumulative discounts) | - purchase of small batches by the intermediary. It may lead to either under-sale of products or the need to attract a large number of intermediaries |

Table 2.4 (continued)

| 1 | 2 | 3 |
|---|---|---|
| - functional discounts | - providing additional services by intermediaries (for example, providing a showroom, installation, goods' presentation, customers' consulting, etc.) | - dispersal of intermediaries and producers: the intermediary is responsible for physical distribution of products to the consumer; the manufacturer must provide pre- and after-sales service of products |
| Bonuses | - intermediaries stimulation to implement and overfulfill plans agreed with the manufacturer | - low responsibility of the intermediary for the distribution plan's implementation |
| Preferential terms of payment | - commodity loans, deferred or installment payments, preferential terms of payment for goods provided on consignment, etc.; the intermediary gets the opportunity to save own working capital | the reluctance of the intermediary to purchase large batches of products due to high one-time costs |
| *Non-economic methods of motivation* | | |
| Joint planning of the marketing channel | - involvement of intermediaries in the process of the channel planning;<br>- development of a unified strategy for channel development, formation of sales and marketing plans | - manufacturer's individual decision-making on the structure of the marketing channel; disregarding the wishes and capabilities of other participants may cause failure or even necessitate of channel's elimination |
| Resource support, including<br>- technical support and training | - providing the intermediaries' with the technical knowledge and skills necessary for effective sales;<br>- intermediaries visitings to manufacture enterprises;<br>- obtaining by intermediaries more information about the product and its advantages | - intermediaries ignorance of products' qualitative characteristics, technology of production, principles of product differentiation, products' competitive advantages ect., that does not allow them to convey complete and truthful information to consumers |

Table 2.4 (continued)

| 1 | 2 | 3 |
|---|---|---|
| - marketing support | - manufacturer’s financing of advertising campaigns;<br>- distribution of costs for advertising campaigns and promotions between the manufacturer and the intermediary equally or in a certain ratio by agreement of the parties;<br>- providing marketing channel participants with free advertising materials, souvenirs, catalogs and other elementsal by the manufacturer | - manufacturer's definition of the wrong communication strategy |
| Sales staff loyalty management | - increasing intermediaries' commitment to products and manufacturer's strategy | - lack of intermediary commitment to the manufacturer may lead to failure in the working |
| Information support about new products | - providing the communication between manufacturer and intermediary through the paid transfer of software products that allow to support the logistics and marketing operations of the intermediary | - insufficient information about innovations and market complicates the assessment of the market situation and action planning for the future |
| Strengthening the image and status of the intermediary | - the intermediaries’ feeling of greater exclusivity; intermediaries’ reputation among other producers, intermediaries and consumers is growing | - the lack of intermediary’s image doesn’t attract consumers attention and doesn’t encourage buying |
| Joint development and production of new products | - the intermediaries’ understanding of the product’s idea, its purpose, ways of application, that allows them to choose the best ways of products;<br>- the intermediaries immediately assume the risks and understand all the options for future events | - difficulties in intermediaries’ understanding of the product’s specifics, which may cause the choice of wrong tools for its distribution |

Tips to motivating channel partners (Calderon-Arroyo, 2018):

1. **Engage with tools and resources.** All employees need tools and resources to complete their job. But, to be successful in their job, the tools and resources should be engaging and inspirational. Use company internal content to resonate with channel partners, so that they can be inspired to drive more sales. Channel partner marketing is just as important when attracting channel partners as it is retaining them.

2. **Set realistic targets.** A part of motivating channel partners is managing and setting realistic sales goals. When channel partners are given attainable targets, they are more likely to succeed. Lowering expectations will not only decrease stress on the sales team, but with the right motivation, it will push them to reach for goals higher than what is set. The reversal of aiming for less, will demonstrate to channel partners that they can meet their goals and this feeling of success will give them the drive to reach for more.

3. **Praise channel partners.** When a channel partner or a channels sales team meets a quota, praise them! Not just when a quota is met, but anytime a goal is achieved or simply because you see a team member who is having a good, productive day. Praising channel partners will make them feel appreciated and valued. It's a feeling that everyone desires. By simply praising and encouraging channel partners, the company will see a boost in results. We all crave for recognition, implementing an award program will also help with this.

4. **Incentivise channel partners to increase channel sales.** Sometimes it may take a little incentive to motivate channel partners to sell to their full capabilities. An incentive can be something as simple as a friendly competition amongst team members. i.e. top channel sales partner for the month of June will win a $100 pre-paid credit card.

5. **Provide channel partners with support and build a relationship.** A well-managed channel partner will bring the company success. Sales teams need to feel like they have support. Channel managers and or leaders, need to be available to build a relationship with their channel teams and provide the proper support needed. Creating a relationship with channel partners can be of great benefit, be a friend, and you can reap the benefits of that friendship.

6. **Seek help when needed.** Not every company or channel manager has the time or resources to implement processes to motivate channel partners. Motivation can bring your company the sales support it needs. Think about hiring an internal employee success manager, or implementing

an automation tool that can help inspire, motivate, and guide channel partners to success.

**Benefits** of motivating channel partners are the following (Calderon-Arroyo, 2018):

1. **Less turn over.** Motivated employees tend to enjoy their job and stay with the company for long periods of time. Motivating channel partners will give a company the ability to grow their channel partners into well-oiled selling machines.
2. **Create a reputable channel sales program.** Motivated and well taken care of channel partners will brag about how good their company is. This helps differentiate you from your competitors and in return, eases the recruiting process to attract partners of interest with talent.
3. **Employee development.** When a channel partner is motivated, they are not only inspired to meet their goals, but they also become driven and seek further training and education. Providing them with those development resources will play into their growth and success as a channel partner.
4. **Loyalty.** Channel partners who are motivated are loyal to the company. When a partner feels as though the work they're doing is valued, they are far more like to remain a fan of the company.

This chapter has been concerned with relationships in marketing channels. The main aspects covered were:

– concepts of distribution: single-channel, cross-channel, multi-channel and omni-channel concepts of distribution were analyzed. Pros and cons of esch concept were defined;

– types of interactions between participants in marketing channels: specifics of cooperation, competition and conflict in marketing channels were introduced. Types of channel conflicts, their causes and mechanisms for effective conflict management were described;

– stimulation and motivation in marketing channels: the importance of channel members motivation was mentioned. Basic facets involved in motivation management were defined. Methods of marketing channels participants motivation were proposed.

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# SECTION 3

# PARTICIPANTS IN MARKETING CHANNELS

## 3.1. Roles and functions of participants in marketing channels

**Intermediaries (middlemen)** institutions that have specialized in rendering distributive services both to the producers and consumers. They are of three types (Ilesanmi, 2011):

1. **Merchant Middlemen:** this category of intermediaries buys and take title to the goods they buy from producers (e.g. wholesalers and retailers).
2. **Agent Middlemen:** they look for markets for the producer and receive commission or fee for expediting exchanges, e.g., sales representatives.
3. **Facilitators:** this group of intermediaries render services that facilitate the movement of goods and services form the point of production to po int of consumption, e.g., warehousing, transportation etc.

Intermediaries also perform function by providing time, place and ownership utilities, which help to increase the value of products. Intermediaries equally obtain information about consumers (social outlook, economic profit, demographic characteristic, concentration and dispersion etc.) and pass them to producers to assist them in planning their productions to attune them to the environment. They assist producers in advertising, promoting and pricing of their products for the markets. In addition, they are risk takers (e.g., goods becoming obsolete in their hands with time during storage, pilfering, damage from fire etc.). Also, some production/economic activities are financed by them. In most cases they buy from and pay the producers and sell to consumers in appropriate sizes at credit. From the above analysis, the importance of middlemen in the marketing of goods and services shall not be overemphasized. In conclusion, the reasons for their importance are as summarized below (Ilesanmi, 2011):

1. Middlemen reduce the number of transactions required, there by reducing cost: the contribution of middlemen is important. Shipping products to too many retailers by manufacturers without a wholesaler who can perform this duty incurs costs, which are reflected in the prices charged

for products. If the number of transactions can be reduced through the use of middlemen, costs will be less and lower prices will result.

2. Middlemen perform marketing function: middlemen are valuable because they perform almost every marketing functions. They can conduct marketing research, advertise, employ sales force and engage in physical distribution. They can also maintain inventories, extend credit and collect debts, and provide a variety of services to their customers. Manufacturers therefore can shift the performance of these functions from themselves to middlemen.

3. Middlemen are specialists: since middlemen may be specialists in performing some marketing functions, their efficiency in performing these functions which are normally shifted to them by manufacturers results to lower costs and hence lower prices for the products in the hands of customers.

4. Middlemen perform the concentration and dispersion functions: two important functions by middlemen are the concentration and dispersion functions. Concentration is the consolidation of small lots into larger lots for more economic shipment performed mainly by wholesalers/distributors and dispersion, which is breaking large lots into smaller, lot sizes for convenient purchase by consumers performed by retailers.

5. Middlemen enhance the value of products: mainly because of the ability of middlemen to store and transport products, the values of these products are enhanced. Through storage, time utility is created. These products become more valuable to consumers because they are made available when the consumers want to purchase them. On the other hand, products are more valuable if they are made available at convenient locations to the customers i.e. the products have place utility. This utility is created by middlemen who transport these products to stores close to population concentrations.

6. Middlemen bring buyers sellers together: they also play the role of bringing buyers and sellers together by matching buyers who seek certain products with sellers who offer them.

7. Middlemen act as information sources: they provide information on the market and competition to the companies.

8. Middlemen save companies money: for new companies that lack financial competence or established companies that do not have adequate

financial resources as they expand their operations, middlemen perform these costly marketing functions for them.

9. Middlemen are valuable for companies marketing new products: companies trying to sell products in new markets may lack the experience of these new markets which middlemen who possess such can perform.

10. Middlemen are valuable for companies marketing new products: new products that are substantially different from existing product lines always pose as problems for the innovating firm to market. Middlemen who possess the requisite skill and experience help these companies for the introduction of these new products.

11. Middlemen are helpful for small companies: small companies which are not strong financially and often lack product and market expertise, make use of retailer and wholesalers to their advantage.

Distribution's role within a marketing mix is getting the product to its target market. Distribution is the arrangement necessary to transfer ownership of a product and transport the product from where it is produced to where it is finally consumed. The most important activity in getting a product to market is arranging for its sale and the transfer of title from producer to final consumer. Other common activities (or functions) are promoting the product, storing it, and assuming some of the financial risk during the distribution process. Typically, however, firms called middlemen perform some of these activities on behalf of the producer or the consumer.

Typical activities of a middleman are (Ilesanmi, 2011):

1. Sales specialist for producer:
– provides market information;
– interprets consumers' wants;
– promotes producers' products;
– creates assortments;
– stores products;
– negotiates with customers;
– provides financing;
– owns products;
– shares risks.
2. Purchasing agent for buyer:
– anticipates wants;
– subdivides large quantities of a product;
– stores product;

– transports products;
– creates assortments;
– provides financing;
– makes products readily available;
– guarantees products;
– shares risks.

The various kinds of middlemen in the market are (Various kinds, n.d.):

1. **Wholesalers:** They are the people who buy in bulk from the producers and sell in small quantities to the retailers.
2. **Retailers:** They are the people who buy in small quantities from the wholesalers and sell to the ultimate consumers.
3. **Agents:** They are the middlemen who do not take any title to goods. They render all services required in marketing. They represent either the seller or the buyer. They receive commission for their work.
4. **Brokers:** Like agents, brokers also represent either the buyer or the seller. They do not usually have physical control over the goods in which they deal. Example: share brokers. They get 'brokerage' for their work.
5. **Dealers:** They are the business houses that resell goods.
6. **Distributors:** They are the same as wholesalers.
7. **Jobbers:** They are associated with stock exchanges. A jobber deals in certain securities. He transacts only with a broker and does not deal directly with the public.
8. **Branches:** These are establishments maintained by manufacturers at different places to promote sales. Example: Bata Shoe company.
9. **Consumer Co-operatives:** These are owned and managed by the ultimate consumers. Such cooperatives buy and distribute goods mainly to the members.
10. **Company show room:** A company may run its own show room to sell its goods. Example: Philips, BPL and Thomson have their own showrooms in Chennai.
11. **Facilitating Agencies:** These agencies are directly or indirectly involved in the performance of certain marketing functions. These are transport organizations, warehouses, banks, insurance companies and so on.

In details channel member **functions** (Kotler, Keller, 2012) are following:

1. Gather information about potential and current customers, competitors, and other actors and forces in the marketing environment.

2. Develop and disseminate persuasive communications to stimulate purchasing.

3. Negotiate and reach agreements on price and other terms so that transfer of ownership or possession can be affected.

4. Place orders with manufacturers.

5. Acquire the funds to finance inventories at different levels in the marketing channel.

6. Assume risks connected with carrying out channel work.

7. Provide for the successive storage and movement of physical products.

8. Provide for buyers' payment of their bills through banks and other financial institutions.

9. Oversee actual transfer of ownership from one organization or person to another.

The middlemen perform the following marketing functions which are listed in sequence (Channels of Distribution, n.d.):

1. Searching out buyers and sellers (contacting & mechandising), matching goods to the requirements of market.
2. Offering goods in the form of assortments or packages.
3. Persuading and influencing the prospective buyers to favour a certain product and its maker (personal selling/sales promotion).
4. Implementing pricing policies in such a manner that would be acceptable to buyers and ensure effective distribution.
5. Providing feedback information, marketing intelligence and sales forecasting services for the regions to their suppliers.
6. Looking after the process of distribution where necessary.
7. Participating actively in the creation and establishment of a market for a new product.
8. Offering pre and after sale services to consumers.
9. Communicating the use of technique of the product to the users.
10. Offering credit to retailers and consumers.
11. Risk bearing with reference to stock hoarding/transport.

All functions of marketing channels' members can be divided into three big groups (Table 3.1).

Table 3.1. Main functions of marketing channels' intermediaries
(Heskett, 1976 cited in Burnett, n.d.)

| Function | Activities |
|---|---|
| **Transactional function** | **Buying:** purchasing products to resale or as an agent to supply of a product |
| | **Selling:** contacting potential customers, promoting products, and seeking orders |
| | **Risk taking:** assuming business risks in the ownership of inventory that can become obsolete or deteriorate; additional risk comes from uncollectable customer accounts |
| **Logistical function** | **Assorting:** creating product assortment from several sources to serve customers |
| | **Storing:** assembling and protecting products at a convenient location to offer better customer service |
| | **Sorting:** purchasing in large quantities and breaking into smaller amounts desired by customers |
| | **Transporting:** physically moving a product to customers |
| **Facilitating function** | **Financing:** intermediaries may invest in inventory, sell and deliver merchandise to business user, and provide credit terms, then finance the exchange process |
| | **Grading:** inspecting, testing, or judging products and assigning them quality grades |
| | **Marketing information and research:** providing information to customers and suppliers, including competitive conditions and trends, final user needs, pricing conditions, and user satisfaction |

However, the existence of middlemen may lead to several short comings. The elimination of middlemen is based on the following grounds (Channels of Distribution, n.d.):

1. Excessive number: Often there are too many middlemen between the manufacturers and consumers. As every middleman charges some commission or profit, the ultimate consumer has to pay a very high price for goods. They are social parasites thriving at the cost of the consumer and their ultimate elimination will reduce prices and burden on consumers.
2. Superfluous: Most middlemen do not render any useful service in lieu of profit or commission. They act as only transfer agents and unnecessarly cause delay in the flow of goods. Their elimination will result in quick and smooth flow of goods.

3. Limited risk taking: Middlemen do not bear the producers' risk such as loss due to strikes, lockouts, depression and change in fashions and habits, etc.

4. Anti-social activities: They take undue advantage of adverse conditions in business. Some businessmen (middlemen) indulge in anti-social activities like hoarding and adulteration to earn huge amount to profits.

5. Limiting consumers' choice: The middlemen often promote products which are inferior in quality and get high margin of profit. Thus, they exploit consumers and limit their choice.

## 3.2. Intermediaries in wholesaling

**Wholesaling** includes all the activities in selling goods or services to those who buy for resale or business use. It excludes manufacturers and farmers because they are engaged primarily in production, and it excludes retailers (Kotler, Keller, 2012).

Wholesalers (also called distributors*)* differ from retailers in a number of ways. First, wholesalers pay less attention to promotion, atmosphere, and location because they are dealing with business customers rather than final consumers. Second, wholesale transactions are usually larger than retail transactions, and wholesalers usually cover a larger trade area than retailers. Third, the government deals with wholesalers and retailers differently in terms of legal regulations and taxes (Kotler, Keller, 2012). Wholesaling includes all activities required to sell goods or services to other firms, either for resale or for business use, usually in bulk quantities and at lower-than-retail prices.

The major types of wholesalers are (based on Kotler, Keller, 2012 & Marketing intermediaries, n.d.):

1. **Merchant wholesalers.** Independently owned businesses that take title to the merchandise they handle. They are full-service and limited-service jobbers, distributors, and mill supply houses. There are two types of merchant wholesalers:

1) **full-service wholesalers** usually handle larger sales volumes; they may perform a broad range of services for their customers, such as stocking inventories, operating warehouses, supplying credit, employing salespeople to assist customers, and delivering goods to customers. Wholesale merchants sell primarily to retailers: Some carry several merchandise lines, some carry one or two lines, others carry only part of a

line. General-line wholesalers carry a wide variety of merchandise, such as groceries; specialty wholesalers, on the other hand, deal with a narrow line of goods, such as coffee and tea or seafood.

2) **limited-service wholesalers:** limited-service wholesalers, who offer fewer services to their customers and suppliers, emerged in order to reduce the costs of service. There are several types of limited-service wholesalers:

– cash-and-carry wholesalers usually handle a limited line of fast-moving merchandise, sell a limited line of fast-moving goods to small retailers for cash and not delivering goods:

– truck wholesalers or jobbers sell and deliver directly from their vehicles, often for cash, a limited line of semi-perishable goods to supermarkets, grocery stores, hospitals, restaurants, hotels;

– drop shippers serve bulk industries such as coal, lumber, and heavy equipment; they take orders but have manufacturers ship merchandise directly to final consumers. They assume title and risk from the time an order is accepted to its delivery, they do not carry inventory or handle the merchandise;

– rack jobbers handle nonfood lines such as housewares or personal goods, primarily serve drug and grocery retailers. Delivery people set up displays, price goods, and keep inventory records; they retain title to goods and bill retailers only for goods sold to the end of the year.

– producers' cooperatives owned by their members, who are farmers – assemble farm produce to be sold in local markets and share profits at the end of the year.;

– mail-order wholesalers send catalogs to retail, industrial, and institutional customers; orders are filled and sent by mail, rail, plane, or truck.

2. **Brokers and agents.** Manufacturers may use brokers and agents, who do not take title possession of the goods, in marketing their products. Facilitate buying and selling, on commission of 2 percent to 6 percent of the selling price; limited functions; generally, specialize by product line or customer type. Brokers bring buyers and sellers together and assist in negotiation; they are paid by the party hiring them – food brokers, real estate brokers, insurance brokers. **Brokers**, most commonly found in the food, real estate, and insurance industries, may represent either a buyer or a seller and are paid by the party who hires them. Brokers often can represent several manufacturers of noncompeting products on a

commission basis. They do not carry inventory or assume risk. **Agents** represent buyers or sellers on a more permanent basis. Unlike merchant wholesalers, agent middlemen do not take legal ownership of the goods they sell; nor do they generally take physical possession of them. The three principal types of agent middlemen are manufacturers' agents, selling agents, and purchasing agents. Manufacturers' agents, who represent two or more manufacturers' complementary lines on a continuous basis, are usually compensated by commission. As a rule, they carry only part of a manufacturer's output, perhaps in areas where the manufacturer cannot maintain full-time salespeople. Many manufacturers' agents are businesses of only a few employees and are most commonly found in the furniture, electric, and apparel industries. Sales agents are given contractual authority to sell all of a manufacturer's output and generally have considerable autonomy to set prices, terms, and conditions of sale. Sometimes they perform the duties of a manufacturer's marketing department, although they work on a commission basis. Sales agents often provide market feedback and product information to the manufacturers and play an important role in product development. They are found in such product areas as chemicals, metals, and industrial machinery and equipment. Purchasing agents, who routinely have long-term relationships with buyers, typically receive, inspect, store, and ship goods to their buyers.

3. **Manufacturers' and retailers' branches and offices.** Wholesaling operations conducted by sellers or buyers themselves rather than through independent wholesalers. Separate branches and offices are dedicated to sales or purchasing. Manufacturers may engage in wholesaling through their sales branches and offices. This allows manufacturers to improve the inventory control, selling, and promotion flows. Numerous retailers also establish purchasing offices in major market centres that play a role similar to that of brokers and agents. The major difference is that they are part of the buyer's own organization.

4. **Specialized wholesalers.** Agricultural assemblers (buy the agricultural output of many farms), petroleum bulk plants and terminals (consolidate the output of many wells), and auction companies (auction cars, equipment, etc., to dealers and other businesses).

In general, **wholesalers** are more efficient in performing one or more of the following **functions** (based on Kotler, Keller, 2012 & Channels of Distribution, n.d.)::

1. **Selling and promoting.** Wholesalers' sales forces help manufacturers reach many small business customers at a relatively low

cost. They have more contacts, and buyers often trust them more than they trust a distant manufacturer.

2. **Buying and assortment building.** Wholesalers are able to select items and build the assortments their customers need, saving them considerable work.

3. **Bulk breaking.** Wholesalers achieve savings for their customers by buying large carload lots and breaking the bulk into smaller units.

4. **Warehousing.** Wholesalers hold inventories, thereby reducing inventory costs and risks to suppliers and customers.

5. **Transportation.** Wholesalers can often provide quicker delivery to buyers because they are closer to the buyers.

6. **Financing.** Wholesalers finance customers by granting credit, and finance suppliers by ordering early and paying bills on time.

7. **Risk bearing.** Wholesalers absorb some risk by taking title and bearing the cost of theft, damage, spoilage, and obsolescence.

8. **Market information.** Wholesalers supply information to suppliers and customers regarding competitors' activities, new products, price developments, and so on.

9. **Management services and counseling.** Wholesalers often help retailers improve their operations by training sales clerks, helping with store layouts and displays, and setting up accounting and inventory-control systems. They may help industrial customers by offering training and technical services.

10. **Storage.** Wholesalers hold large stocks and serves as a reservoir and supplies to retailers. Wholesalers help in stablising prices by adjusting supply of goods to their demand.

11. **Packing and grading.** A wholesaler packs and repacks goods in convenient lots. He sorts out goods in different grades. He also gives brand names to the products packed and graded by him.

12. **Advertising and sales promotion.** A wholesaler performs advertising and sales promotion activities to increase the sale of products. He also takes the services of experts for this purpose.

## 3.3. Intermediaries in retailing

**Retailing** includes all the activities in selling goods or services directly to final consumers for personal, nonbusiness use. A **retailer** or **retail store** is any business enterprise whose sales volume comes primarily from retailing (Kotler, Keller, 2012).

Any organization selling to final consumers – whether it is a manufacturer, wholesaler, or retailer is doing retailing. It doesn't matter *how* the goods or services are sold (in person, by mail, telephone, vending machine, or on the Internet) or *where* (in a store, on the street, or in the consumer's home) (Kotler, Keller, 2012).

There are four basic principles that form the retailing concept (Dhaliwal):

1. Customer orientation: The retailer finds out the attributes and needs of its customers and tries to satisfy these needs to the fullest.
2. Coordinated effort: The retailer integrates all plans and activities to maximize efficiency.
3. Value-driven: The retailer offers good value to customers, whether it is upscale or discount that is having prices appropriate for the level of products and customer service.
4. Goal orientation: The retailer sets goals and then uses its strategy to attain them.

There are three factors which describes the nature of retailing. Each factor imposes unique requirements on retail firms (Dhaliwal):

1. Final consumers make many unplanned or impulse purchases. Research shows that a great percentage of consumers do not look at commercials or advertisement before shopping do not prepare shopping lists and make fully unplanned purchases. This behaviour shows the value of in-store displays, attractive store layouts, and well-organized stores, catalogues, and Web sites. Candy, cosmetics, snack foods, magazines, and other items are sold as impulse goods when placed in visible, high-traffic areas in a store, catalogue, or Web site. Because many times purchases are done unplanned, the retailer's ability to forecast, budget, order merchandise, and have sufficient personnel on the selling floor is compromised.
2. The average amount of a sales transaction for retailers is much less than for manufacturers. This low amount creates a need to tightly control the costs related to each transaction such as credit verification, sales personnel, and bagging; to maximize the number of customers drawn to the

retailer, more emphasis may be placed on advertisements and special promotions; and impulse sales may be invoked by more aggressive selling. However, still cost control can be tough.

3. Retail customers usually visit a store, even though mail, phone, and Web sales have increased. Despite the inroads made by non-store retailers, most retail transactions are still conducted in stores—and will continue to be in the future. Many people prefer shopping personally because they want to touch, smell, and/or try on products; like to browse for unplanned purchases; feel more comfortable taking a purchase home with them than waiting for a delivery; and desire privacy while at home. This store-based shopping orientation has implications for retailers; they must work to attract shoppers to their stores and consider such factors as store location, transportation, and store hours, proximity of competitors, product selection, parking, and advertisements.

**The functions of retailing** include (Dhaliwal):

1. Sorting: The items are arranged in an order by the retailers so that the customers are able to locate and pick up their needed goods easily.

2. Storage: The retailer holds stocks of goods and thereby meets the day to day needs of the consumer.

3. Channels of Communication: The retailer spreads by word of mouth communication, valuable information to the customers about the product.

4. Transportation: Nowadays, small grocery stores are undertaking the work of door to door deliveries in the case of durable goods.

Consumers today can shop for goods and services at store retailers, non-store retailers, and retail organizations:

1. **Store retailers.** Perhaps the best-known type of store retailer is the department store. Different formats of store retailers will have different competitive and price dynamics. Discount stores, for example, compete much more intensely with each other than other formats. Retailers also meet widely different consumer preferences for service levels and specific services. Specifically, they position themselves as offering one of four levels of service (Kotler, Keller, 2012):

– **self-service:** self-service is the cornerstone of all discount operations. Many customers are willing to carry out their own “locate-compare-select” process to save money;

– **self-selection:** customers find their own goods, although they can ask for assistance;

– **limited service:** these retailers carry more shopping goods and services such as credit and merchandise-return privileges. Customers need more information and assistance.;

– **full-service:** salespeople are ready to assist in every phase of the "locate-compare-select" process. Customers who like to be waited on prefer this type of store. The high staffing cost, along with the higher proportion of specialty goods and slower-moving items and the many services, result in high-cost retailing.

Table 3.2. Types of store retailers (Kotler, Keller, 2012 & Marketing intermediaries, n.d. & Channels of Distribution, n.d.)

| Retailer | Description |
|---|---|
| 1 | 2 |
| Specialty store | Narrow product line. Furniture stores, florists, sporting-goods stores, and bookstores are all specialty stores |
| Department store | Several product lines. Department stores carry a wider variety of merchandise than most stores but offer these items in separate departments within the store. These departments usually include home furnishings and household goods, as well as clothing, which may be divided into departments according to gender and age. Departments within each store are usually operated as separate entities, each with its own buyers, promotions, and service personnel. The most influential of the department stores may even be trendsetters in various fields, such as fashion. A departmental store is a big retail store with many departments under one roof. It offers a wide range of products so as to suit different consumer tastes and preferences. All the departments are centrally controlled but each department forms a complete sales unit in itself |
| Supermarket | Large, low-cost, low-margin, high-volume, self-service store designed to meet total needs for food and household products. Supermarkets are characterized by large facilities (15,000 to 25,000 square feet (1,394 to 2,323 square metres) with more than 12,000 items), low profit margins (earning about 1% operating profit on sales), high volume, and operations that serve the consumer's total needs for items such as food and household sundries. They are organized according to product departments and operate primarily on a self-service basis. Supermarkets also may sell wines and other alcoholic beverages (depending on local licensing laws) and clothing |

Table 3.2 (continued)

| 1 | 2 |
|---|---|
| Convenience store | Small store in residential area, often open 24/7, limited line of high-turnover convenience products plus takeout. Located primarily near residential areas, convenience stores are relatively small outlets that are open long hours and carry a limited line of high-turnover convenience products at high prices. Although many have added food services, consumers use them mainly for "fill-in" purchases, such as bread, milk, or miscellaneous goods |
| Drug store | Prescription and pharmacies, health and beauty aids, other personal care, small durable, miscellaneous items |
| Discount store | Standard or specialty merchandise; low-price, low-margin, high-volume stores. |
| Extreme value or hard-discount store | A more restricted merchandise mix than discount stores but at even lower prices |
| Off-price retailer | Leftover goods, overruns, irregular merchandise sold at less than retail. Off-price retailers purchase at below-wholesale prices and charge less than retail prices. This practice is quite different from that of ordinary discounters, who buy at the market wholesale price and simply accept lower margins by pricing their products below retail costs. Off-price retailers carry a constantly changing collection of overruns, irregulars, and leftover goods and have made their biggest forays in the clothing, footwear, and accessories industries. The three primary examples of off-price retailers are factory outlets, independent carriers, and warehouse clubs. Stocking manufacturers' surplus, discontinued, or irregular products, factory outlets are owned and operated by the manufacturer. Independent off-price retailers carry a rapidly changing collection of higher-quality merchandise and are typically owned and operated by entrepreneurs or divisions of larger retail companies. Warehouse (or wholesale) clubs operate out of enormous, low-cost facilities and charge patrons an annual membership fee. They sell a limited selection of brand-name grocery items, appliances, clothing, and miscellaneous items at a deep discount. These warehouse stores maintain low costs because they buy products at huge quantity discounts, use less labour in stocking, and typically do not make home deliveries or accept credit cards |

Table 3.2 (continued)

| 1 | 2 |
|---|---|
| Superstore | Huge selling space, routinely purchased food and household items, plus services (laundry, shoe repair, dry cleaning, check cashing). Category killer (deep assortment in one category); combination store; hypermarket (huge stores that combine supermarket, discount, and warehouse retailing). Superstores, hypermarkets, and combination stores are unique retail merchandisers. With facilities averaging 35,000 square feet, superstores meet many of the consumer's needs for food and nonfood items by housing a full-service grocery store as well as such services as dry cleaning, laundry, shoe repair, and cafeterias. Combination stores typically combine a grocery store and a drug store in one facility, utilizing approximately 55,000 square feet of selling space. Hypermarkets combine supermarket, discount, and warehousing retailing principles by going beyond routinely purchased goods to include furniture, clothing, appliances, and other items. Ranging in size from 80,000 to 220,000 square feet, hypermarkets display products in bulk quantities that require minimum handling by store personnel |
| Catalog showroom | Broad selection of high-markup, fast-moving, brand-name goods sold by catalog at a discount. Customers pick up merchandise at the store |

**2. Nonstore retailing.** Although the overwhelming bulk of goods and services – 97 percent – is sold through stores, nonstore retailing has been growing much faster than store retailing. Nonstore retailing falls into four major categories: direct selling, direct marketing (which includes telemarketing and Internet selling), automatic vending, and buying services (Kotler, Keller, 2012).

**Direct selling**, also called multilevel selling and network marketing, is a multibillion-dollar industry, with hundreds of companies selling door-to-door or at home sales parties. The distributor's compensation includes a percentage of sales made by those he or she recruits, as well as earnings on direct sales to customers. These direct-selling firms, now finding fewer consumers at home, are developing multidistribution strategies (Kotler, Keller, 2012).

**Direct marketing** has roots in direct-mail and catalog marketing; it includes telemarketing, television direct-response marketing, and electronic shopping. As people become more accustomed to shopping on the Internet,

they are ordering a greater variety of goods and services from a wider range of Web sites (Kotler, Keller, 2012).

**Automatic vending** offers a variety of merchandise, including impulse goods such as soft drinks, coffee, candy, newspapers, and other products such as hosiery, cosmetics, hot food. Vending machines are found in factories, offices, large retail stores, gasoline stations, hotels, restaurants, and many other places. They offer 24-hour selling, self-service, and merchandise that is stocked to be fresh (Kotler, Keller, 2012).

**Buying service** is a storeless retailer serving a specific clientele – usually employees of large organizations – who are entitled to buy from a list of retailers that have agreed to give discounts in return for membership (Kotler, Keller, 2012).

**3. Retail organizations.** Description of retail organizations is in Table below.

Table 3.3. Types of retail organizations (Kotler, Keller, 2012 & Marketing intermediaries, n.d. & Hibbard, Grayson, Kotler, n.d.)

| Retailer | Description |
|---|---|
| Corporate chain store | Two or more outlets owned and controlled, employing central buying and merchandising, and selling similar lines of merchandise |
| Voluntary chain | A wholesaler-sponsored group of independent retailers engaged in bulk buying and common merchandising |
| Retailer cooperative | Independent retailers using a central buying organization and joint promotion efforts |
| Consumer cooperative | A retail firm owned by its customers. Members contribute money to open their own store, vote on its policies, elect a group to manage it, and receive dividends. Local cooperative grocery stores can be found in many markets. They are based on open consumer membership, equal voting among members, limited customer services, and shared profits among members in the form of rebates generally related to the amounts of their purchases |
| Franchise organization | Contractual association between a franchisor and franchisees, popular in a number of product and service areas. Typified by a unique product, service, business method, trade name, or patent, franchises have been prominent in many industries, including fast foods, video stores, health and fitness centres, hair salons, auto rentals, motels, and travel agencies |
| Merchandising conglomerate | Corporation that combines several diversified retailing lines and forms under central ownership, with some integration of distribution and management |

Retailers' role in distribution of goods is enumerated below (Channels of Distribution, n.d.):

1. **Wide choice to consumers.** The retailer anticipates needs of consumers. He assembles goods from different sources and stocks different varieties of products. Thus, he offers a wide choice to consumers. They can buy according to their purchasing power and requirements.

2. **Availability of goods in small quantities and at convenient locations.** A retailer provides ready supply of goods so that consumers can buy conveniently and quickly in small lots without any inconvenience of placing advance orders and waiting for supplies. By ensuring uninterrupted and fresh supply of goods, he saves consumers from the botheration of buying goods in bulk and storing them.

3. **Home delivery.** A retailer transports goods from wholesalers to ultimate consumers. Some retailers provide free home delivery service to their consumers. Thus they create place utility.

4. **Assurance of regular supply.** He maintains adequate supply of goods so that consumers are sure of getting regular supply at the time of their need.

5. **Credit facility.** Although retailers mostly sell goods for cash, they also supply goods on credit to their regular customers.

6. **Close interaction with customers.** A retailer brings new products to the notice of customers and educates them in their uses. A retailer thus, acts as a friend and guide to his customers. Indeed his interaction with customers is of intimate personal nature and thus he is able to provide feed back to wholesalers and manufacturers about consumers' preferences.

Retailing challenges and trends for the future a number of enormous challenges face retailers in the 21st century (Krafft, Mantrala).

**Trend 1:** Consolidation in the Retailing Industry Numerous retailers are facing imminent problems, since they are unable to deliver high levels of value relative to their more astute competitors.

**Trend 2:** Value Is Key Successful retailers are developing strategies that offer customers greater value over competitors and are sustaining them over time. To do so, they are focusing their energies on creating centers of excellence, such as connecting with their customers, being a leader in terms of the merchandise and assortment that they provide, and having excellent operations in place. Although retailers that provide value do not always provide it at a low price.

**Trend 3:** Being Innovative Retailers are experimenting with their store formats more and more. In addition, they are effectively designing and managing the various strategic levels to en-hance the overall customer shopping experience. The problem with being known as an innovative retailer is that it can only remain innovative as long as its customers see the innovations as fresh and excit-ing. Bear in mind that department stores were once thought of as an innovative retail format. Thus, innovative retailers must continuously implement new ideas or their customers will begin to view them as "old hat."

**Trend 4:** Cost Controls Successful retailers, particularly those competing in the low-price segment and many in the Big Middle, are efficient and effective in integrating their suppliers, manufacturers, warehouses, stores, and transportation intermediaries into a seam-less value chain, in order to minimize system-wide costs while satisfying the ser-vice levels required by its customers. They are seeking out and using innovative technology throughout their supply chains, so as to reduce costs and provide value for their customers. In the last few years, some of the largest retailers in the US have invested in so-phisticated merchandise optimization techniques that help them make decisions about planning assortments, initial pricing, buying, allocation of merchandise to stores, promotion, planning replenishment (rebuys), space management (planograms), and markdown pricing. These techniques enable retailers to do bet-ter in controlling costs, buying, allocating, and promoting the right merchandise, and pricing and marking down merchandise. By utilizing these techniques, they ensure that customers get what they want, which translates into loyal customers and, in many cases, a competitive advantage.

## 3.4. Industrial intermediaries

Channel members assume a central role in the marketing strategies of business-to-business firms, large and small. A channel management strategy begins with an understanding of the intermediaries that may be used. Primary attention is given to two: (1) industrial distributors and (2) manufacturers' representatives. They handle a sizable share of business-to-business sales made through intermediaries (Hutt, Speh, 2009).

**Industrial distributors** are full-service intermediaries; that is, they take title to the products they sell, and they perform the full range of marketing functions. Industrial distributor is an independently owned and managed operation that buys, stocks, and sell products like for example production tools, operating equipment, and other supplies used by all forms of industry. The distributor is basically a wholesaler that services and sells to business markets instead of consumer markets (Larsson, 2015).

Some of the more important **functions** are (Hutt, Speh, 2009):

– providing credit, offering wide product assortments, delivering goods;
– offering technical advice;
– and meeting emergency requirements.

Not only are distributors valuable to their manufacturer-suppliers but their customers generally view them favorably. Some purchasing agents view the distributor as an extension of their "buying arms" because they provide service, technical advice, and product application suggestions (Hutt, Speh, 2009).

To create more value for their customers, many large distributors have expanded their range of services. Value is delivered through various supply chain and inventory management services, including automatic replenishment, product assembly, in-plant stores, and design services. The most popular services involve helping customers design, construct, and, in some cases, operate a supply network. Other value-adding activities include partnerships in which the distributor's field application engineers work at a customer's site to help select components for new product designs. To reap the profits associated with these important services, many distributors now charge separate fees for each unique service.

To select the best distributor for a channel, the marketing manager must understand the diversity of distributor operations. Industrial distributors vary according to product lines and user markets. Firms may be

ultraspecialized (for example, selling only to municipal water works), or they may carry a broad line of generalized industrial products. However, three primary distributor classifications are usually recognized.

**The following types of** industrial **distributors** are (Hutt, Speh, 2009):

1. **General-line distributors** (generalist distributors) cater to a broad array of industrial needs. They stock an extensive variety of products and could be likened to the supermarket in consumer-goods markets. They are almost like industrial supermarkets, stocking a wide variety of goods without any specific area of specialisation.
2. **Specialists** focus on one line or on a few related lines; specialise in certain product categories. Such a distributor may handle only power transmission equipment – belts, pulleys, and bearings. The most common specialty is fasteners, although specialization also occurs in cutting tools, power transmission equipment, pipes, valves, and fittings. There is a trend toward increased specialization as a result of increasing technical complexity of products and the need for higher levels of precision and quality control.
3. **A combination house** operates in two markets: industrial and consumer. Such a distributor might carry electric motors for industrial customers and hardware and automotive parts to be sold through retailers to final consumers.

The generalized responsibilities of industrial distributors are in the Table below.

Table 3.4. Distribution Responsibilities (Hutt, Speh, 2009)

| Responsibility | Activity |
| --- | --- |
| Contact | Reach all customers in a defined territory through an outside sales force that calls on customers or through an inside group that receives telephone orders |
| Product availability | Provide a local inventory and include all supporting activities: credit, just-in-time delivery, order processing, and advice |
| Repair | Provide easy access to local repair facilities (unavailable from a distant manufacturer) |
| Assembly and light | Purchase material in bulk, then shape, form, or assemble to user |
| Manufacturing | Requirements |

Industrial distributors are a powerful force in business marketing channels, and all indications point to an expanded role for them.

Industrial distributors are commonly used in situations where (Hutt, Speh, 2009):

- the product is relatively standardized;
- the unit value of the product is low;
- gross margin is low;
- customer purchasing effort is low;
- customers make frequent purchases;
- the market is decentralised and scattered.

**Manufacturers' Representative** is the other commonly used intermediary in business marketing is the manufacturers' representative, often simply called the rep. A manufacturers' representative is a self-employed salesperson who represents one or more manufacturers on a commission basis. Unlike the distributor, the representative does not take title of the goods involved, and usually does not even take possession of it. Basically, the rep is an independent salesperson that usually sells within assigned territories and is compensated on a straight commission basis for those sales. The rep often represents a number of manufacturers in that territory, whose products are normally complementary rather than competitive. With a line of complementary products from various manufacturers, the reps are often able to provide complete product lines to their customers. Normally, the rep does not possess much authority when it comes to price and terms of sale. The function of this channel intermediary is just simply to sell the principal's products in the assigned territory (Venkataraman, 2017).

A rep neither takes title to nor holds inventory of the products handled (some reps do, however, keep a limited inventory of repair and maintenance parts). The rep's forte is expert product knowledge coupled with a keen understanding of the markets and customer needs. Reps are usually limited to defined geographical areas; thus, a manufacturer seeking nationwide distribution usually works with several rep companies. Compared with a distributor channel, a rep generally gives the business marketer more control because the firm maintains title and possession of the goods (Hutt, Speh, 2009).

Reps are the manufacturers' selling arm, making contact with customers, writing and following up on orders, and linking the manufacturer with the industrial end users. Although paid by the

manufacturer, the rep is also important to customers. Often, the efforts of a rep during a customer emergency (for example, an equipment failure) mean the difference between continuing or stopping production. Most reps are thoroughly experienced in the industries they serve – they can offer technical advice while enhancing the customer's leverage with suppliers in securing parts, repair, and delivery. The rep also provides customers with a continuing flow of information on innovations and trends in equipment, as well as on the industry as a whole (Hutt, Speh, 2009).

Reps are paid a commission on sales; the commission varies by industry and by the nature of the selling job. Commissions typically range from a low of 2 percent to a high of 18 percent for selected products. The average commission rate is 5.3 percent. Percentage commission compensation is attractive to manufacturers because they have few fixed sales costs. Reps are paid only when they generate orders, and commissions can be adjusted based on industry conditions. Because reps are paid on commission, they are motivated to generate high levels of sales – another fact the manufacturer appreciates (Hutt, Speh, 2009).

Reps possess sophisticated product knowledge and typically have extensive experience in the markets they serve. Most reps develop their field experience while working as salespersons for manufacturers. They are motivated to become reps by the desire to be independent and to reap the substantial monetary rewards possible on commission.

Reps are commonly used in situations where (Hutt, Speh, 2009):

1. Large and Small Firms. Small and medium-sized firms generally have the greatest need for a rep, although many large firms – for example, Dow Chemical, Motorola, and Intel – use them. The reason is primarily economic: smaller firms cannot justify the expense of maintaining their own sales forces. The rep provides an efficient way to obtain total market coverage, with costs incurred only as sales are made. The quality of the selling job is often very good as a result of the rep's prior experience and market knowledge.

2. Limited Market Potential. The rep also plays a vital role when the manufacturer's market potential is limited. A manufacturer may use a direct sales force in heavily concentrated business markets, where the demand is sufficient to support the expense, and use reps to cover less-dense markets. Because the rep carries several lines, expenses can be allocated over a much larger sales volume.

3. Servicing Distributors. Reps may also be employed by a firm that markets through distributors. When a manufacturer sells through hundreds of distributors, reps may sell to and service those distributors.

4. Reducing Overhead Costs. Sometimes the commission rate paid to reps exceeds the cost of a direct sales force, yet the supplier continues to use reps. This policy is not as irrational as it appears. Assume, for example, that costs for a direct sales force approximate 8 percent of sales and that a rep's commission rate is 11 percent. Using reps in this case is often justified because of the hidden costs of a sales force. First, the manufacturer does not provide fringe benefits or a fixed salary to reps. Second, the costs of training a rep are usually limited to those required to provide product information. Thus, using reps eliminates significant overhead costs.

In summary, the use of reps seems most appropriate when the following conditions exists (Hutt, Speh, 2009; Venkataraman, 2017):

1. Customers require personal selling but the market is not large enough to support full-time company sales personnel.

2. Gross margins are not large enough to support the cost of full-time company sales personnel, but personal selling is required.

3. The manufacturer is moving into new markets and wishes to penetrate those markets quicker by using already established rep contacts in those markets.

4. The product is better sold as part of a total package with other manufacturers' products rather than an individual item.

5. The market is new and does not have full-time sales personell, but customers require personal selling.

When a company builds a direct selling channel to a foreign market, it can distribute its goods to the following parties (Louckx, 2014):

1. **Foreign distributor.** Distributors buy products from the manufacturer at a discount and then resell or distribute them to retailers or end-users. The contract established between them is renewable as long as the conditions are beneficial for both. The distributer is a merchant who buys and maintains merchandise in its own name, and this simplifies the credit and payment activities for the manufacturer.

2. **Foreign retailer.** Manufacturers and retailers engage in direct trade relationships to decrease costs and personally discuss prices and other issues. Generally, manufacturers that produce very expensive and large products prefer to work without intermediaries.

3. **State-controlled trading company.** Special products, for example telecommunication equipment, agricultural machinery, and technical instruments, must be sold only to state-controlled companies. These companies have monopoly in buying and selling a set of specific goods, and they are controlled by the government's policies and regulations.

4. **End user.** For some manufacturers, that for example produce costly industrial products, it is reasonable to sell directly to the end-users. The difficulties that might arise are duty and clearance problems, for example when a customer orders goods without understanding of his/her country's import regulations.

Choosing an indirect selling channel, manufacturers collaborate with one or more domestic intermediaries, which move and sell the goods to foreign parties or end-consumers. All the local middlemen can be divided into two broad categories: **domestic agent** – it represents the manufacturer, and it can make contracts on its behalf, but it can never take title to goods; and **domestic merchant** – it represents the manufacturer's goods and takes title to those goods, but it has no power to make contracts on behalf of the manufacturer (Onkvisit & Shaw 2004; Rushton et al. 2014; Cateora & Graham 2007, cited in Louckx, 2014).

**The main types of domestic agents are** (Onkvisit & Shaw 2004; Rushton et al. 2014 cited in Louckx, 2014)**:**

1. **Export broker.** This is an individual or organization that operates under its own or manufacturer's name in one or more markets, negotiates the most favourable conditions for the manufacturer, but cannot conclude the deal without the manufacturer's approval. The broker performs only the contractual function. It gets paid for any action performed.

2. **Manufacturer's export agent or sales representative.** This is an independent external person, who works on the permanent basis, but does not operate under the manufacturer's name. The task is to make potential buyers interested in the manufacturer's products by presenting literature, products' samples, and other materials.

3. **Export management company (EMC).** EMC is an organization that is responsible for the whole manufacturer's export program as well as for programs of other manufacturers as long as the exported goods do not compete against each other. It performs activities under the manufacturer's name, and it makes arrangements starting from promotional activities to export documentation.

4. **Cooperative exporter (piggyback exporter or export vendor).** This is an organization which in addition to manufacturing acts as an export agent, it is responsible for organizing shipping. Cooperative exporter can have goods in possession but not the title. The business objective of this exporter is to decrease own costs by sharing them with other companies which want to sell their products in the same market(s).

**The main types of domestic merchants are** (Rushton et al. 2014; Cateora & Graham 2007 cited in Louckx, 2014)**:**

1. **Export merchant.** This is an independent organization, which goal is to make profit. The task is to look for the unmet needs in a foreign market and fulfil the needs with products purchased from manufacturers in its home country. The merchant can possess the goods and resell them in foreign markets under its own name.
2. **Export drop shipper.** This intermediary receives an order for a foreign buyer, places order for a manufacturer and informs where to "drop shipper" directly to the overseas buyer.
3. **Export distributor.** This distributor, located in the manufacturer's country, can represent it and sell goods in foreign market(s) under own or the manufacturer's name. The export distributor organises shipment and selling of the goods abroad, and it takes the risks.
4. **Trading company.** Generally, it is a large company which buys and sells goods, engages in production, goods accumulation, physical distribution channel development, marketing planning arranges transportation and prepares documents for customs, searches for buyers and etc. It does not represent manufacturers or buyers, it can take title to goods.

This chapter has been concerned with participants in marketing channels. The main aspects covered were:

– intermediaries in marketing channels: various kinds of middlemen in the market were introduced; the main functions of marketing channels' intermediaries were defined;

– wholesaling and intermediaries: essence of wholesaling was given; the major types of wholesalers were mentioned; functions of wholesalers were defined;

– retailing and intermediaries: essence and functions of retailing was given; the types of retailers were defined, they were divided into three groups – store retailers, non-store retailers, and retail organizations; retailing challenges and trends for the future were highlighted;

– industrial intermediaries: industrial distributors and manufacturers’ representative were described, their roles and functions were defined.

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# SECTION 4

# STRUCTURE AND STRATEGIES OF MARKETING CHANNELS

## 4.1. Types of marketing channels systems

All marketing systems can be divided into three big groups: conventional marketing channel; horizontal marketing system; vertical marketing system.

1. A **conventional marketing channel** consists of an independent producer, wholesaler(s), and retailer(s). Each is a separate business seeking to maximize its own profits, even if this goal reduces profit for the system as a whole. No channel member has complete or substantial control over other members (Kotler, Keller, 2012).

Conventional marketing channels comprise autonomous business units, each performing a defined set of marketing functions. Co-ordination among channel members is through the bargaining process. Membership of the channel is relatively easy; loyalty is low, and this type of network tends to be unstable. Members rarely co-operate with each member working independently of others. Decision makers are more concerned with cost and investment relationships at a single stage of the marketing process and tend to be committed to established working practices.

Responsibilities of each member are limited to its task, for example, manufacturer worries about making products, and retailer – selling the products (Louckx, 2014).

But conventional marketing system can lead to the unending conflicts between the channel partners resulting in less profits for the business as a whole (Vertical Marketing, n.d.).

Most food grocery products are marketed through conventional marketing channels; independent food and grocery producers are responsible for growing, rearing and manufacturing products and brands. These are sold through a series of wholesalers and retailers operating as independent businesses in the chain and selling to their own customers (Lancaster, Massingham, 2011).

**2. Horizontal marketing systems (HMS)** is a type of channel arrangement, where two or more different independent organizations join their forces and combine their resources to exploit a new market opportunity. Each company lacks the capital, know-how, production, or

marketing resources to venture alone, or it is afraid of the risk. The companies might work together on a temporary or permanent basis or create a joint venture company. Each company has identified the strength of the other that it can utilize to its own advantage, as a result, both of them can achieve better results and beat the competition (Louckx, 2014).

**3. Vertical marketing systems (VMS)** are in contrast to conventional channels where members co-ordinate activities between different levels of the channel to reach a desired target market. It includes the producer, wholesaler(s), and retailer(s) acting as a unified system. The essential feature is that participants acknowledge and desire interdependence, and view it as being in their best long-term interests.

One channel member, the channel captain, sometimes called a channel steward, owns or franchises the others or has so much power that they all cooperate.

A channel steward might be the maker of the product or service, the maker of a key component, the supplier or assembler, or the distributor or retailer. Within a company, stewardship might rest with the CEO, a top manager, or a team of senior managers. Channel stewardship has two important outcomes. First, it expands value for the steward's customers, enlarging the market or increasing existing customers' purchases through the channel. Second, it creates a more tightly woven and yet adaptable channel in which valuable members are rewarded and the less valuable are weeded out (V. Kasturi Rangan and Marie Bell, 2006).

In VMS one of the members can own the others, franchise them or possess so much power that the other members find it beneficial to cooperate. The strongest member attempts to control the channel, and it tries to eliminate conflicts over other members, i.e. independent organizations perusing their own goals (Louckx, 2014).

Through the recognition of a channel leader, the distribution networks function better, sales and profits are higher, product exposure improves, inventory management systems are initiated, and the coordination of promotional activities becomes a reality. An administered system is not without its problems. Often, this effort is placed on the shoulders of a single individual. Another drawback is the tendency of polarizing channel members. Businesses either become part of the VMS or remain strongly independent. Eventually these independents may find themselves at a tremendous competitive disadvantage, and may even be deprived of certain channel benefits (Channel concepts, 10).

VMS can be classified into three types:

**3.1. Corporate vertical marketing** is when a company owns two or more traditional levels of the channel. A corporate VMS combines successive stages of production and distribution under single ownership. In many economies corporate vertical channels have arisen as a result of a desire for growth on the part of companies through vertical integration. Two types of vertical integration are possible with respect to the direction within which the vertical integration moves a company in the supply chain: when a manufacturer buys, a retail chain, this is referred to as forward integration with respect to the chain.

Backward integration is moving upstream in the supply chain, e.g. when a retailer invests in manufacturing or a manufacturer invests in a raw material source. Although the end result of such movements is a corporate vertical marketing channel, often the stimulus to such movement is less to do with channel economies and efficiencies, and more with control over access to supply or demand, entry into a profitable business or overall scale and operating economies.

Many of the large oil companies are examples of corporate vertical marketing. They prospect for oil, extract it, process it, distribute and retail it through their petrol stations. Other companies operate partial corporate vertical marketing systems in that they integrate only one way. Zara (the clothing retailer) is integrated vertically backward with manufacturing facilities (Lancaster, Massingham, 2011 + Kotler).

**3.2. Administered vertical marketing systems (VMS)** do not have the formal arrangements of a contractual system or the clarity of power dependence of a corporate system. An administered VMS coordinates successive stages of production and distribution through the size and power of one of the members. Manufacturers of dominant brands can secure strong trade cooperation and support from resellers. It is a co-ordinated system of distribution channel organization in which the flow of products from the producer to the end user is controlled by the power and size of one member of the channel system rather than by common ownership or contractual ties. Member organizations acknowledge the existence of dependence and adhere to the leadership of the dominant firm, which may operate at any level in the channel.

An example of a successful administered VMS in is that of the furniture/lifestyle retailer, IKEA who has developed close working relationships with its suppliers. Acting as the channel co-ordinator, IKEA is committed to cost-effective supply and their suppliers benefit from the channel leadership of an effective and marketing-oriented retailer.

Administered VMS are one step removed from conventional marketing channels. In an administered system, co-ordination of marketing activities is achieved by the use of programmes developed by one or a limited number of firms. Successful administered systems are conventional channels in which the principles of effective inter-organizational management have been correctly applied (Lancaster, Massingham, 2011 + Kotler).

**3.3. Contractual VMS** consists of independent firms at different levels of production and distribution integrating their programs on a contractual basis to obtain more economies or sales impact than they could achieve alone.

Sometimes thought of as "value-adding partnerships" (VAPs), contractual VMSs come in three types (Kotler):

– **wholesaler-sponsored voluntary chains** – wholesalers organize voluntary chains of independent retailers to help standardize their selling practices and achieve buying economies in competing with large chain organizations;

– **retailer cooperatives** – retailers take the initiative and organize a new business entity to carry on wholesaling and possibly some production. Members concentrate their purchases through the retailer co-op and plan their advertising jointly, sharing in profits in proportion to their purchases. Nonmember retailers can also buy through the co-op but do not share in the profits;

– **franchise organizations** – a channel member called a franchisor might link several successive stages in the production-distribution process. Franchising has been the fastest-growing retailing development in recent years. Although the basic idea is an old one, some forms of franchising are quite new. The traditional system is the manufacturer-sponsored retailer franchise.

**Franchises** are where the parent company grants an individual person or relatively small company the right or privilege to do business in a prescribed manner over a certain time period in a specified place. The parent company is referred to as the franchiser (or franchisor) and may occupy any position in the channel network. The franchise retailer is termed the franchisee. There are four basic types of franchise system (Lancaster, Massingham, 2011):

– **manufacturer/retailer franchise,** e.g. this type of arrangement is common in the service stations;

– **manufacturer/wholesaler franchise:** e.g. Coca-Cola sell drinks they manufacture to franchised wholesalers, who in turn bottle and distribute soft drinks to retailers. This type of arrangement is common in the food and drinks markets with many of the large companies franchising part of their manufacturing and or wholesaling activities to others;

– **the wholesaler/retailer franchise.** Many retail chains are franchisees of large wholesalers. These wholesalers saw the value of securing a measure of control, and of course a share of the retail profits, from marketing their products and brands;

– **the service/sponsor retailer franchise**. This is the best known and certainly most ubiquitous of franchising arrangements and it has enabled many organizations to rapidly expand their global operations.

Franchises share a set of common features and operating procedures (Lancaster, Massingham, 2011):

1. A franchise essentially sells a nationally, or internationally, recognized trade name, process, or business format to the franchisee.
2. The franchiser normally offers expert advice e.g. location selection, capitalization, operation and marketing.
3. Most franchises operate a central purchasing system at national or international level to enable cost savings to be made at the individual franchise level.
4. The franchise is subject to a contract binding both parties that normally requires the franchisee to pay a franchise fee and royalty fees to the franchiser, but the franchisee owns the business as opposed to being employed.
5. The franchiser often provides initial and continuous training to the franchisee.

Advantages to the **franchisee** are (Lancaster, Massingham, 2011):

1. The franchisee gains the benefit of being able to sell a well-known product or service which has been market tested and known to work.
2. The franchisee enjoys access to the knowledge, experience, reputation and image of the franchiser. Because of this the franchisee is able to enter a business much more easily than setting up from scratch. The learning curve is shortened, expensive mistakes can be avoided, and there is less chance of business failure.

3. Although the franchisee has the backing of what is often the large organization of the franchiser, the franchisee is still essentially an independent business with all that this implies for motivation to succeed.

4. The franchisee is often helped by national or international advertising and promotion by the franchiser which would be beyond the means of a small independent business.

5. The franchisee enjoys the use of the franchiser's trademark, continuous research and development and market information.

6. The franchiser will normally provide a system of management controls such as accountancy, sales and stock control procedures.

Advantages to the **franchiser** are (Lancaster, Massingham, 2011):

1. Finding and recruiting a network of franchisees enables rapid growth as wider distribution can be achieved with less capital.

2. The individual franchisee is more motivated than a hired manager might be.

3. The franchiser secures captive outlets for products or services, especially in the case of trade name franchising and private labels.

4. Franchise and royalty fees provide a regular stream of income for the franchiser.

5. The terms of the franchise contract normally give the franchiser substantial control over how the franchise is operated and normally the franchiser can terminate a contract should the relationship turn out to be unsatisfactory. The costs of such terminations are likely to be less than if the franchiser was operating a corporate owned facility with staff on the payroll.

Normally, terms and restrictions on location and sale of the business by the franchisee ensure that the franchiser is able to maintain territorial exclusivity for its franchisees. There are disadvantages, but the franchise relationship combines the strengths of both small and large scale businesses. The franchisee is the small business person who is able to respond to local market conditions and offer personal services to customers. The franchiser passes on economies of scale in national advertising and bulk purchasing. For a franchise to be successful both parties need to work towards a common goal and avoid conflicts which requires frequent and open communication between partners if the system is to meet changing market conditions while maintaining its integrity.

What constitutes the main disadvantages of franchising depends from whose perspective we are looking; the franchisee or the franchiser. The main disadvantages of franchising from each perspective are:

**Disadvantages to franchiser** (Lancaster, Massingham, 2011)**:**

1. The franchiser loses some control over the provision and marketing of the brand. Poor service on the part of the franchisee can result in problems for brand image.
2. Ideas and techniques can be copied even if seemingly well protected by patents and copyright arrangements.
3. Some proportion of profit has to be foregone.
4. There may be less commitment and enthusiasm from the franchisee.
5. Often franchisees lack business skills or experience.

**Disadvantages to the franchisee** (Lancaster, Massingham, 2011)**:**

1. Lack of support from franchiser.
2. Franchiser may go out of business.
3. Lack of flexibility/scope to use initiative.
4. Close control from franchiser.

Franchising is not solely confined to consumer products like fast food. It is used for a wide range of products and services in both consumer and industrial markets.

## 4.2. Designing the marketing channel

Channel design refers to those decisions involving the development of new marketing channels where none had existed before, or to the modification of existing channels.

Producers, manufacturers, wholesalers (consumer or industrial) and retailers all face channel design decisions. For retailers, however, channel design is viewed from a perspective opposite to that of producers and manufacturers. Retailers look “up the channel” in an attempt to secure suppliers, rather than “down the channel” toward the market (as is the case for producers and manufacturers). Wholesale intermediary face channel design decisions from both perspectives (Rosenbloom, 2012).

The channel design decision can be broken down into seven phases or steps. These are (Rosenbloom, 2012):

1. Recognize need for channel design decision.
2. Set and coordinate distribution objectives.

3. Specify the distribution tasks.
4. Develop alternative channel structures.
5. Evaluate the relevant variable.
6. Choose the "best" channel structure.
7. Select the channel members.

These phases will be described, more in detail below.

**Phase 1: Recognizing the Need for a Channel Design Decision.**

Many situations can indicate the need for a channel design decision. Among them are (Rosenbloom, 2012):

1. Developing a new product or product line. If existing channels for other products are not suitable for the new product or product line, a new channel may have to be set up or the existing channels modified in some fashion.

2. Aiming an existing product at a new target market. A common example of this situation is a firm's introduction of a product in the consumer market after it has sold in the industrial market.

3. Making a major change in some other component of the marketing mix. For example, a new pricing policy emphasizing lower prices may require a shift to lower. Price dealers such as discount department stores.

4. Establishing a new firm, from scratch or as a result of mergers or acquisitions.

5. Adapting to changing existing intermediaries might make their policies so as to inhibit the attainment of the firm's distribution objectives. For example, if intermediaries are beginning to emphasize their own private brand, then the manufacturer may want to add new distributors who will promote the company's products more enthusiastically.

6. Dealing with changes in availability of particular kinds of intermediaries.

7. Opening up new geographic marketing areas (territories).

8. Facing the occurrence of major environmental changes. These changes may be in the economic, sociocultural, competitive, technological, or legal spheres.

9. Meeting the challenges of conflict or other behavioral problems. For example, in some instances conflict may become so instance that it is not possible to resolve it without modifying the channel. A loss of power by a manufacturer to his distributors may also foster the need to design an

entirely new channel. Further, changing roles and communications difficulties may confront the marketer with channel design decisions.

10. Reviewing and evaluating. The regular periodic reviews and evaluations under-taken by a firm may point to the need for changes in the existing channels and possibly the need for new channels.

This list, although by no means comprehensive, offers an overview of the more common conditions that may require the channel manager to make channels design decision. It is important to be familiar with this list, because channel design decisions are not necessarily obvious, especially those involving modification rather than setting up of new channels.

**Phase 2: Setting and Coordinating Distribution Objectives.**

Having recognized that a channel design decision is needed, the channel manager should try to develop a channel structure, whether form scratch or by modifying existing channels, that will help achieve the firm's distribution objectives efficiently. Yet quite often at this stage of the channel design decision, the firm's distribution objectives are not explicitly formulated, particularly since the changed conditions that created the need for channel design decisions might also have created the need for new or modified distribution objectives. It is important for the channel manager to evaluate carefully the firm's distribution objectives at this point to see if new ones are needed (Rosenbloom, 2012).

In order to set distribution objectives that are well-coordinated with other marketing and firm objectives and strategies, channel managers need to perform three tasks (Rosenbloom, 2012):

1. Become familiar with the objectives and strategies in the other marketing mix areas and any relevant objectives and strategies of the firm.
2. Set distribution objectives and state them explicitly.
3. Check to see if the distribution objectives they have set are congruent with marketing and other general objectives and strategies of the firm.

In order to set distribution objectives that are well coordinated with other marketing and firm objectives and strategies, the channel manager needs to perform three tasks (Rosenbloom, 2012):

**1. Become familiar with the objectives and strategies in the other marketing mix areas and any other relevant objectives and strategies of the firm.** Whoever is responsible for setting distribution objectives should also make an effort to learn which existing objectives and strategies in the firm may impinge of the distribution objectives. In practice, often the

same individual(s) who set(s) objectives for other components of the marketing mix will do so for distribution.

**2. Set distribution objectives and state them explicitly.** Distribution objectives are essentially statements describing the part that distribution in expected to play in achieving the firm's overall marketing objectives.

**3. Check to see if the distribution objectives set are congruent with marketing and the other general objectives and strategies of the firm.** A congruency check verifies that the distribution objectives do not conflict with the other areas of the marketing mix.

Some typical objectives used by business marketing managers in setting up their channel of distribution follow (Haas, 1995, s432):

1. Low cost of operation.
2. Control.
3. Closer relationships with intermediaries.
4. Sales effort.
5. Service and technical assistance.
6. Market feedback.
7. Company image.

**Phase 3: Specifying the distribution tasks.**

After the distribution objectives have been set, a number of distribution tasks (intermediary functions) must be performed if the distribution objectives are to be met. The channel manager should, therefore, specify explicitly the nature of these tasks (Rosenbloom, 2012).

In specifying distribution tasks, it is especially important not to underestimate what is involved in making products and services conveniently available to final consumers.

Over the years marketing scholars have discussed numerous lists of marketing tasks (functions). These lists generally include such activities as buying, selling communication, transportation, storage, risk taking, financing, breaking bulk and others. Such classifications of marketing functions, while perhaps useful to those seeking to explain the role of marketing in a macro context, are of little direct value to the channel manager operating in the individual firm. The job of the channel manager in outlining distribution functions or tasks is a much more specific and situational dependent one. The kind of tasks required to meet specific distribution objectives must be precisely stated.

To give an example, according to Rosenbloom (2012) the distribution tasks will be can be defined as follows: promotion; stocking; order solicitation and handling; pre- or post-sales service; market research; sales financing; a variety of value-adding activities; selling; communication; transportation; storage; risk taking; financing.

The specification of distribution tasks for products sold in industrial marketing often has to be even more specifically stated compared to consumer products. For example, a steel or metal producer whose distribution objectives call for dealing with a target market that contains many small customers would have such basic distribution tasks as selling, communication, transportation, storage, risk taking, financing. But in addition, in order to serve the smaller customers, the producer would probably have to perform many more specialized tasks, such as the following (Rosenbloom, 2012):

1. Maintain readily available inventory (specified in terms of quality and type).
2. Provide rapid delivery (specified in terms of days or hours).
3. Offer credit.
4. Provide emergency service.
5. Supply semi fabrication function such as cutting, shearing, slotting, threading, pattern cutting, pattern rolling, re-rolling, stretcher levelling, welding, grinding, forcing, and reaming.
6. Include packaging and special handling.
7. Provide technical assistance such as problem analysis, product selection, application, and end use product.
8. Maintain market information.
9. Offer storage space.
10. Allow for absorption of size and grade obsolescence.
11. Process orders and bill for many accounts.
12. Offer return provision.

Though a number of these functions appear to be production rather than distribution tasks, when viewed in the context of being necessary to meet a particular distribution objective (such as dealing with smaller customers) they are indeed distribution tasks. They performance of these specialized tasks would be necessary because the distribution objective called for dealing with many small customers, and in most cases small customers could not perform these tasks for themselves. Consequently, the specific kinds of distribution tasks required are mainly a function of the

distribution objectives that have been set and, of course, the types of firms involved (Rosenbloom, 2012).

**Phase 4: Developing possible alternative channel structures.**

The channel manager should consider alternative ways of allocating distribution objectives to achieve their distribution tasks. Often, the channel manager will choose more than one channel structure in order to reach the target markets effectively and efficiently.

Whether single – or multiple – channel structures are chosen, the allocation alternatives (possible channel structures) should be evaluated in terms of the following three dimensions: (1) number of levels in the channel, (2) intensity at the various levels, (3) type of intermediaries at each level (Rosenbloom, 2012).

**Number of levels in the channel**. The number of alternatives that the channel manager can realistically consider for this structural dimension is often limited to no more than two or three choices. For example, it might be feasible to consider:

- going direct (two-level);
- using one intermediary (three level);
- or possibly using two intermediaries (four-level).

These limitations result from a variety of factors such as the particular industry practices, nature and size of the market, availability of intermediaries, and other variables. In some instances this dimension of channel structure is the same for all manufacturers in the industry and may remain virtually fixed for long periods of time. In other industries it is more flexible and subject to change in relatively short time periods (Rosenbloom, 2012).

**Number of intermediaries**. The choice of channels will be influenced by the firm's positioning strategy (Rosenbloom, 2012). Companies, therefore, have to decide on the number of intermediaries to use at each level. Three strategies are available for deciding geographical market coverage (Kotler, Keller, 2012).

The intensity of distribution dimension is a very important aspect of channel structure because it is often a key factor in the firm's basic marketing strategy and will reflect the firm's overall corporate objectives and strategies.

**1. Intensive distribution.** For low-priced, convenience or impulse products, companies will generally want to maximize the number of outlets carrying them. The more places carrying the product, the more likely it is to

be bought. The more intensive the distribution required, the greater the efficiencies offered by intermediaries (Doyle, 1998 cited in Larsson, 2015). This strategy serves well for snack foods, soft drinks, newspapers, candies, and gum – products consumers buy frequently or in a variety of locations (Kotler, Keller, 2012).

**2. Exclusive distribution** means severely limiting the number of intermediaries. It's appropriate when the producer wants to maintain control over the service level and outputs offered by the resellers, and it often includes exclusive dealing arrangements. By granting exclusive distribution, the producer hopes to obtain more dedicated and knowledgeable selling. It requires a closer partnership between seller and reseller and is used in the distribution of new automobiles, some major appliances, and some women's apparel brands. Exclusive deals are becoming a mainstay for specialists looking for an edge in markets increasingly driven by price (Kotler, Keller, 2012).

Exclusive distribution is the best option for high-priced, luxury products, the manufacturer will often limit distribution to a very small number of intermediaries. The intermediaries normally gain better margins and the exclusive right to sell the product in a specific area. The manufacturer hopes to achieve in return a greater sales effort, greater control of pricing and selling practices, and a superior brand image (Doyle, 1998 cited in Larsson, 2015).

**3. Selective distribution** means that not all possible intermediaries are used, but rather those included in the channel have been carefully chosen. Furthermore, this strategy aims at firms who like to choose their channel members or "partners" very carefully and then work closely with them in the distribution of the firm's products (Rosenbloom, 2012).

Selective distribution relies on only some of the intermediaries willing to carry a particular product. Whether established or new, the company does not need to worry about having too many outlets; it can gain adequate market coverage with more control and less cost than intensive distribution (Kotler, Keller, 2012).

Essence, advantages and disadvantages of marketing distribution strategies are in the Table below.

Table 4.1. Comparison of intensive, exclusive, and selective marketing distribution strategies (based on Owino, 2017; Louckx, 2014)

| **Distribution scope** | **Exclusive** | **Selective** | **Intensive** |
|---|---|---|---|
| Explanation | A particular middleman sells a product to a specific market segment in a defined geographic area. High price, high margin and lower sales volumes are traits of exclusive distribution | Several middlemen have the right to sell the products in specific area. Customers compare these goods on price/quality basis | A product is available at maximum number of retail outlets, carried by numerous middlemen in a defined area. Products are visible in as many places as possible |
| Advantages | Dealer loyalty, better sales forecasting and inventory control, high level of customer service | High sales volumes can be generated by a relatively small number of middlemen | High sales volumes and high product visibility, impulse buying |
| Disadvantages | Sales volume might be easily lost. When sales are depressed, the middleman can dictate terms to the other channel members | Risk of inadequate market coverage and choice of middlemen. Middlemen can influence producers to reduce the number of retail outlets | Products are low-priced and low-margin, fast turnover is needed. Due to many middlemen, manufacturers give up good control over pricing and product display |
| Retail coverage | Single | Limited | Maximum |
| Major strength | Matches middleman clientele with target market; facilitates close cooperation with middleman | Provides adequate coverage but not at expense of manufac-turer-middlemen cooperation | Maximizes product availability |
| Major weakness | Risk of relying on single middleman | Difficult to implement given interstore competition, especially where discounts may occur | Lack of middlemen support |
| Products most appropriated for | High-involvement specialty or shopping goods | Infrequently purchased shopping goods | Low-involvement consumer convenience goods |
| Examples | Jaguar, Gucci, Rolex, Samsung, Apple, Lamborghini, Mercedes, BMW etc. | Clinique cosmetics; low-end range and mid-level range cars, high-end companies that produce exceptional quality clothing, home appliances, and furniture brands etc. | Products that benefit from intensive distribution include soap, deodorant, laundry, detergent, soft drinks and cigarettes etc. (P&G, Colgate and etc.) |

**Types of intermediaries at each level**. The third dimension of channel structure deals with the particular types of intermediaries to be used, if any, at the various levels of the channel (Rosenbloom, 2012).

The channel manager should not overlook new types of intermediaries that are emerging such as Internet companies. Given that the channel manager should consider all three structural dimensions (level, intensity, and type of intermediaries) in developing channel structures, there are, in theory, a high number of possibilities. Fortunately, in practice, the number of feasible alternatives for each dimension is often limited due to industry or the number of current channel members (Rosenbloom, 2012).

**Phase 5: Evaluating the variables affecting channel structure.**

Having laid out alternative channel structures, the channel manager should then evaluate a number of variables to determine how they are likely to influence various channel structures.

These six basic categories are most important (Rosenbloom, 2012):

1. Market variables.
2. Product variables.
3. Company variables.
4. Intermediary variables.
5. Environmental variables.
6. Behavioral variables.

An example of one such heuristics is as follows: "If a product is technically complex, the manufacturer should sell directly to its user instead of through intermediaries".

Here a product variable (technically complexity) seemingly yields a simple prescription for channel structure. It would be nice if things were simple, but unfortunately such is not the case. Such heuristics, which are commonly mentioned in the marketing literature, are only crude guide to decision making. They should not be viewed as clear-cut prescriptions for choosing a particular channel structure. They are use full only to the extent that they offer some rough reflection of what would typically be expected given a particular condition, and thereby provide a point of departure for that analysis of different channel structures (Rosenbloom, 2012).

With this caveat in mind, we return to a discussion of the six categories of variables and some of the related heuristics relevant to choosing channel structure.

**1. Market Variables.** Market variables are the most fundamental variables to consider when designing a marketing channel.

Four basic subcategories of market variables are particularly important in influencing channel structure. They are market geography, market size, market density, and market behavior (Rosenbloom, 2012).

**Market Geography.** Market geography refers to the geographical size of the markets and their physical location and distance from the producer and manufacturer.

A popular heuristic (rule of thumb) for relating market geography to channel design is:

"The greater the distance between the manufacturer and its markets, the higher the probability that the use of intermediaries will be less expensive than direct distribution".

**Market Size.** The number of customers making up a market (consumer or industrial) determines the market size. From a channel design standpoint, the larger the number of individual customers, the larger the market size. A heuristic about market size relative to channel structure is:

"If the market is large, the use of intermediaries is more likely to be needed because of the high transaction costs of serving large numbers of individual customers. Conversely, if the market is small, a firm is more likely to be able to avoid the use of intermediaries".

**Market Density.** The number of buying units per unit of land area determines the density of the market. In general, the less dense the market, the more difficult and expensive is distribution.

A heuristic for market density and channel structure is as follows:

"The less dense the market, the more likely it is that intermediaries will be used. Stated conversely, the greater the density of the market, the higher the likelihood of eliminating intermediaries".

**2. Product Variables.** Product variables such as bulk and weight, perishability, unit value, degree of standardization (custom-made versus standardized), technical versus nontechnical, and newness affect alternative channel structures (Rosenbloom, 2012).

**Bulk and Weight.** "Heavy and bulky products have very high handling and shipping costs relative to their value. The producer of such products should therefore attempt to minimize these costs by shipping them only in large lots to the fewest possible points. Consequently, the channel structure for heavy and bulky products should, as a general rule, be as short as possible-usually direct from the producer to the user. The exception to this occurs when customers buy in small quantities and need quicker delivery. In this case it may be necessary to use some form of intermediary".

**Perishability.** Products subject to rapid physical deterioration and those of rapid fashion obsolescence require rapid movement from production to consumption.

The following heuristic is appropriate in these situations:

"When products are highly perishable, channel structures should be designed to provide for rapid delivery from producers to consumers".

**Unit Value.** The lower the unit value of the product, the longer the channel should be. This is because low unit value leaves a small margin for distribution costs.

When the unit value is high relative to its size and weight, direct distribution is feasible because the handling and transportation costs are low relative to the product's value.

**Degree of Standardization.** Custom-made products should go from producer to consumer while more standardized products allow opportunity to lengthen the channel.

**Technical versus Nontechnical.** In the industrial market, a highly technical product will generally be distributed through a direct channel. This is because the manufacturer may need sales and service people capable of communicating the product's technical features to the user.

In the consumer market, relatively technical products are usually distributed through short channels for the same reasons.

**Newness.** New products, both industrial and consumer, require extensive and aggressive promotion in the introductory stage to build demand. Usually, the longer the channel of distribution the more difficult it is to achieve this kind of promotional effort from all channel members.

Therefore, a shorter channel is generally viewed as an advantage for new products as a carefully selected group of intermediaries is more likely to provide aggressive promotion.

**Product Prestige.** Prestigious products often associated with famous luxury brands and need to maintain an aura of exclusivity and rareness that would be incompatible with mass market distribution channels. Hence, the channels for these products need to designed to reinforce their prestigious aura by providing limited access to customers seeking to buy prestigious products.

**3. Company Variables.** The most important company variables affecting channel design are size, financial capacity, managerial expertise, and objectives and strategies (Rosenbloom, 2012).

**Size.** "In general, the range of options for different channel structures is a positive function of a firm's size. The power bases available to large

firms, particularly those of reward, coercion, and expertise-enable them to exercise a substantial amount of power in the channel. This gives large firms a relatively high degree of flexibility in choosing channel structures, compared with smaller firms. Consequently, the larger firm's capacity to develop channel that at least approach an optimal allocation of distribution tasks is typically higher than for smaller firms".

**Financial Capacity.** "Generally, the greater the capital available to a company, the lower is its dependence on intermediaries. In order to sell directly to ultimate industrial users, a firm usually needs its own sales force and support service or retail stores, warehousing, and order processing capabilities. Larger firms are better able to bear high cost of these facilities".

**Managerial Expertise.** For firms lacking in the managerial skills necessary to perform distribution tasks, channel design must of necessity include the services of intermediaries who have this expertise. Over time, as the firm's management gains experience, it may be feasible to change the structure to reduce the amount of reliance on intermediaries.

**Objectives and Strategies.** The firm's marketing and general objectives and strategies, such as the desire to exercise a high degree of control over the product, may limit the use of intermediaries.

Strategies emphasizing aggressive promotion and rapid reaction to changing markets will constrain the types of channel structures available to those firms employing such strategies.

**4. Intermediary Variables.** The key intermediary variables related to channel structure are availability, costs, and the services offered (Rosenbloom, 2012).

**Availability.** The availability (number of and competencies of) adequate intermediaries will influence channel structure.

**Cost.** The cost of using intermediaries is always a consideration in choosing a channel structure. If the cost of using intermediaries is too high for the services performed, then the channel structure is likely to minimize the use of intermediaries.

**Services.** This involves evaluating the services offered by particular intermediaries to see which ones can perform them most effectively at the lowest cost.

**5. Environmental Variables.** Economic, sociocultural, competitive, technological, and legal environmental forces can have a significant impact on channel structure (Rosenbloom, 2012).

**6. Behavioral Variables.** Market behavior refers to the following four types of buying behaviors (Rosenbloom, 2012):

- how customers buy;
- when customers buy;
- where customers buy;
- who does buying?

Each of these patterns of buying behavior may have a significant effect on channel structure (Table 4.2).

Table 4.2. Behavioral variables (Rosenbloom, 2012)

| **Buying habits** | **Corresponding channel structure heuristics** |
|---|---|
| **How.** Customer typically buy in very small quantities | Use long channels to reach the market |
| **When.** Buying is highly seasonal | Add intermediaries to the channel to perform the storage function, thereby reducing peaks and valleys in production |
| **Where.** Consumers increasingly tend to shop at home | Eliminate wholesale and retail intermediaries and sell direct |
| **Who.** Industrial market: many individuals influence the purchasing decision | Direct distribution for greater control of sales force to sales force to successfully reach all parties responsible for making purchase decisions |

**Phase 6: Choosing the "Best" Channel Structure.**

In theory, the channel manager should choose an optimal structure that would offer the desired level of effectiveness in performing the distribution tasks at the lowest possible cost. In reality, choosing an optimal structure is not possible (Rosenbloom, 2012).

Some pioneering attempts at developing methods that are more exacting do appear in literature and we will discuss these in brief.

**A) "Characteristics of Goods and Parallel Systems" Approach** (Rosenbloom, 2012)**.**

First laid out in the 1950s by Aspinwall, the main emphasis for choosing a channel structure should be based upon product variables. Each product characteristic is identified with a particular color on the spectrum. These variables are:

1. Replacement rate.

2. Gross margin.
3. Adjustment.
4. Time of consumption.
5. Searching time.

**Using Aspinwall's Approach.** This approach offers the channel manager a neat way of describing and relating a number of heuristics about how product characteristics might affect channel structure. The major problem with this method is that it puts too much emphasis on product characteristics as the determinant of channel structure (Rosenbloom, 2012).

**B) Financial Approach** (Rosenbloom, 2012)**.**

Lambert offers another approach, which argues that the most important variables for choosing a channel structure are financial. Basically, this decision involves comparing estimated earnings on capital resulting from alternative channel structures in light of the cost of capital to determine the most profitable channel.

**Using the Financial Approach.** By viewing the channel as a long-term investment that must more than cover the cost of capital invested in it and provide a better return than other alternative uses for capital, the criteria for choosing a channel structure is more rigorous (Rosenbloom, 2012).

The major problem with Lambert's approach lies in the difficulty of making it operational in a channel decision-making context.

**C) Transaction Cost Analysis (TCA) Approach** (Rosenbloom, 2012)**.**

Based on the work of Williamson, TCA addresses the choice of marketing channel structure only in the most general case situation of choosing between the manufacturer performing all of the distribution tasks itself through vertical integration versus using independent intermediaries to perform some or most of the distribution tasks. It is based upon opportunistic behaviors of channel members (Rosenbloom, 2012).

The main focus of TCA is on the cost of conducting the transactions necessary for a firm to accomplish its distribution tasks.

In order for transactions to take place, *transaction-specific assets* are needed. These are the set of unique assets, both tangible and intangible, required to perform the distribution tasks.

**Using the TCA approach.** TCA has some substantial limitations from the standpoint of managerial usefulness (Rosenbloom, 2012).

First, it deals only with the most general channel structure dichotomy of vertical integration versus use of independent channel members.

Second, the assumption of opportunistic behavior may not be an accurate reflection of behavior in marketing channels.

Third, no real distinction is made between long-term and short-term issues in channel structure relationships.

Fourth, the concept of asset specificity (transaction-specific assets) is very difficult to operationalize.

Finally, TCA is one-dimensional, overly simplistic and neglects other relevant variables in channel choice.

**D) Management Science Approaches** (Rosenbloom, 2012)**.**

It would certainly be desirable if the channel manager could take all possible channel structures, along with all the relevant variables, and "plug" these into a set of equations, which would then yield the optimal channel structure.

**Using Management Science Approaches.** These approaches still need much more development before they are likely to find widespread application to channel choice (Rosenbloom, 2012).

**E) Judgmental-Heuristic Approaches** (Rosenbloom, 2012)**.**

These approaches rely heavily on managerial judgment and heuristics for decisions. Some attempt to formalize the decision-making process whereas others attempt to incorporate cost and revenue data.

**Straight Qualitative Judgment Approach.** The qualitative approach is the crudest but, in practice, the most commonly used approach for choosing channel structures. The various alternative channel structures that have been generated are evaluated by management in terms of decision factors that are thought to be important. These factors may include short- and long-run cost and profit considerations, channel control issues, long-term growth potential, and many others. Sometimes, however, these decision factors are not stated explicitly, and their relative importance is also not made clear. Nevertheless, an alternative is chosen which, in the opinion of management, best satisfies the various explicit or implicit decision factors (Rosenbloom, 2012).

**Weighted Factor Score Approach.** A more refined version of the straight qualitative approach to choosing among channel alternatives is the weighted factor approach suggested by Kotler.

This approach forces management to structure and quantify its judgments in choosing a channel alternative and consists of four basic steps (Rosenbloom, 2012):

1. The decision factors must be stated explicitly.

2. Weights are assigned to each of the decision factors to reflect relative importance precisely in percentage terms.

3. Each channel alternative is rated on each decision factor, on a scale of 1 to 10.

4. The overall weighted factor score (total score) is computed for each channel alternative by multiplying the factor weight (A) by the factor score (B).

**Distribution Costing Approach**. Under this approach, estimates of costs and revenues for different channel alternatives are made, and the figures are compared to see how each alternative compares to another. Regardless of how elaborate or detailed the analysis, the basic theme of this approach stresses managerial judgment and estimations about what the costs and revenues of various channel structure alternatives are likely to be (Rosenbloom, 2012).

**Using Judgmental-Heuristic Approaches.** Regardless of which judgmental-heuristic approach is used, large doses of judgement and "guesstimation" are virtually unavoidable. To say otherwise is to imply that a greater degree of precision exists than is actually the case. This is not to say that the so-called judgemental-heuristic approach is totally subjective. On the contrary, in some cases management's ability to make sharp judgments may be quit high and, if this is coupled with good empirical data on costs and revenues, highly satisfactory (though not optimal) channel choice decisions may be made using judgemental-heuristic approaches.

Judgmental-heuristic approaches also enable the channel manager to readily incorporate non-financial criteria (decision factors) into channel choice decisions. Non-financial criteria such as the degree of control or goodwill available from a particular channel alternative may be of real importance (Rosenbloom, 2012).

**Phase 7: Identification of potential marketing channel members.**

The next step is normally to select channel intermediaries within the select marketing channel segment (Rosenbloom, 2012).

One more approach to marketing channels' design process includes the following steps (Hutt, Speh, 2011):

1. End-User Focus: Define Customer Segments.

2. Identify and Prioritize Customers' Channel Requirements by Segment 1.

3. Assess the Firm's Capabilities to Meet Customers' Requirements.

4. Benchmark Channel Offerings of Key Competitors 1.

5. Create Channel Solutions to Customers' Latent Needs.

6. Evaluate and Select Channel Options.

**Step 1: Define Customer Segments.** The primary goal of the distribution channel is to satisfy end-user needs, so the channel design process should begin there. Step 1 is about defining target market segments and isolating the customer buying and usage behavior in each segment (what they buy, how they buy, and how they put their purchases to use). Some business marketers err by considering their channel partners as "customers and rarely looking beyond them." To inform the channel design process, however, the marketing strategist should center on the importance of the product from the customer's perspective (Hutt, Speh, 2011).

**Step 2: Customers' Channel Needs by Segment.** Identifying and prioritizing the channel function requirements for customers in each market segment is next. This information should be elicited directly from a sample of present or potential customers from each segment. Table 4.3 provides a representative list of channel functions that may be more or less important to customers in a particular segment (Hutt, Speh, 2011).

Table 4.3. Channel functions aligned with customer needs (Hutt, Speh, 2011)

| Channel Function | Customer Needs |
|---|---|
| 1. Product Information | Customers seek more information for new and/or technically complex products and those that are characterized by a rapidly changing market environment |
| 2. Product Customization | Some products must be technically modified or need to be adapted to meet the customer's unique requirements |
| 3. Product Quality Assurance | Because of its importance to the customer's operations, product integrity and reliability might be given special emphasis by customers |
| 4. Lot Size | For products that have a high unit value or those that are used extensively, the purchase represents a sizable dollar outlay and a significant financial decision for the customer |
| 5. Assortment | A customer may require a broad range of products, including complementary items, and assign special value to one-stop shopping |
| 6. Availability | Some customer environments require the channel to manage demand uncertainty and support a high level of product availability |
| 7. After-Sales Services | Customers require a range of services from installation and repair to maintenance and warranty |
| 8. Logistics | A customer organization may require special transportation and storage services to support its operations and strategy |

For example, large customers for information-technology products might rank product customization, product quality assurance, and after-sales service as their top three needs. Whereas small customers may prioritize product information, assortment, and availability as their most important needs. The business marketing manager should also probe customers on other issues that might provide strategy insights (Hutt, Speh, 2011).

**Step 3: Assess the Firm's Channel Capabilities.** Once customer requirements have been isolated and prioritized, an assessment is made of the strengths and weaknesses of the firm's channel. The central focus is on identifying the gaps between what customers in a segment desire and what the channel is now providing. Customers base their choice of a channel not on a single element, but on a complete bundle of benefits (that is, channel functions). To that end, the business-to-business firm should identify particular channel functions, like aftersales support or availability, where action could be taken to enhance the customer value proposition (Hutt, Speh, 2011).

**Step 4: Benchmark to Competitors.** In designing a channel, cost considerations prevent the business marketer from closing all the gaps on channel capabilities that may appear. However, a clear direction for strategy is revealed by understanding the channel offerings of competitors. For example, an aggressive competitor that goes to market with its own team of account managers and dedicated service specialists might demonstrate special strength in serving large corporate customers. However, countless opportunities exist for smaller rivals to counter this strategy by developing special channel offerings tailored to small and medium-sized customers (Hutt, Speh, 2011).

**Step 5: Create Channel Solutions for Customers' Latent Needs.** Sometimes, a review of competitor offerings can alert the marketer to opportunities for new offerings that may have special appeal to customers. "At other times, customers' needs may be latent and unarticulated, and it is the channel steward's responsibility to tap into and surface those requirements."[16] Based on such an assessment, a provider of information-technology equipment created an entirely new channel option for the small and medium-sized customer segment. Rather than selling equipment, this new channel takes responsibility for installing, upgrading, and maintaining the equipment at the customers' locations for an ongoing service fee (Hutt, Speh, 2011).

**Step 6: Evaluate and Select Channel Options.** Channel decisions must ultimately consider the cost-benefit trade-offs and the estimated profitability that each of the viable channel options present. Some of the channel gaps that are uncovered in this assessment can be closed by the independent actions and investments of the business-to-business firm (for example, adding to the service support staff or the sales force). For the most part, however, the greatest progress will come from the channel partners (for example, distributors or reps) working together and discussing how channel capabilities can be aligned to customer needs. "The idea is to enhance the value delivered to customers through collaborative action among channel partners. If the partners can agree on how to pull it off and, indeed, accomplish their redefined tasks," they will squarely respond to customer needs and advance the performance of the channel. One important implication of the framework is that the design of the channel must change as customer and competitor behavior changes. Rather than a static structure, channel management is an ongoing process involving continuous adjustments and evolution (Hutt, Speh, 2011).

The selection of marketing channel is a very responsible and complicated process: decisions of distribution are directly connected with the general politics of enterprise performance, which is being formulated at the top-level management.

More models of marketing channel formation are presented below.

The model for marketing channel design proposed by Kotler. Kotler, 2000 (cited in Gudonaviþienơ, Alijosiene, 2008) suggests the method of five stages that is presented in Figure 4.1. Kotler (2000) suggests the beginning the formation of marketing channel with the analysis of the needs of target consumers. At the second stage the target markets are identified and the main aims of marketing channel are determined, according to product characteristics and qualification of intermediaries. Next, different alternatives of marketing channel participants and conditions of performance. At the fourth stage the selection of intermediaries has to be made and at the fifth – assessment of marketing channel depending on the economic criteria, control level during the period of adaptation has to be performed.

The model of Kotler (2002) suggests to begin the formation of marketing channel from the end user. This model in comparison with others is simpler. It defines the principles of marketing channel formation rather than claims to give the exhaustive projection within this process.

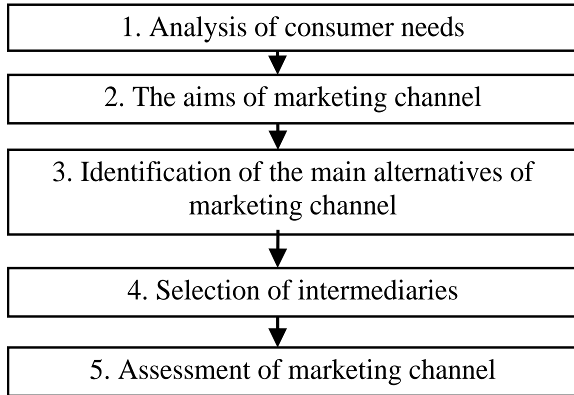



Figure 4.1. The model for marketing channel design by Kotler, 2002

Berman's, 1999 (cited in Gudonaviþienơ, Alijosiene, 2008) model of the selection of marketing channel structure also has 7 stages (Figure 4.2).

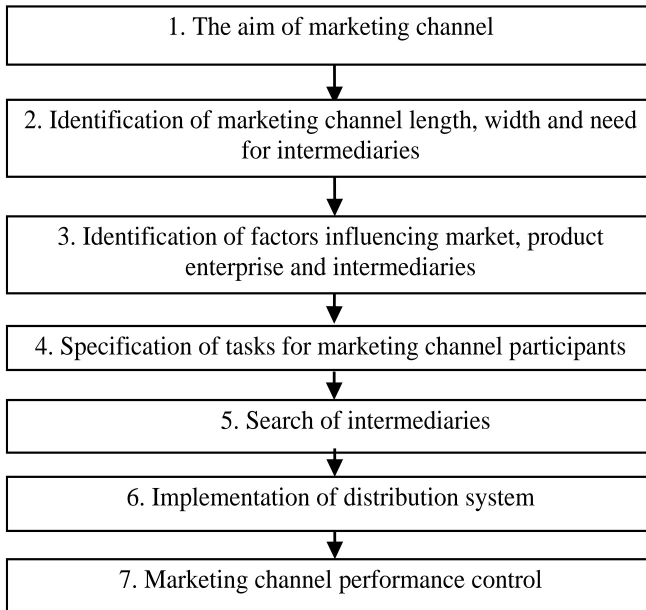
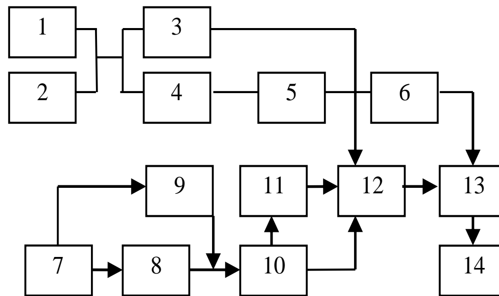



Figure 4.2. The model for marketing channel design by Berman

Five stages of this model are the same as those of Rosenbloom, 2012 model, but some of them are switched around and the model suggests to begin with the identification of goals, not with the preconditions of marketing channel formation.

Berman's (1999) model, without big number of stages, still is very clear and detailed, defining the various factors that have to be analysed at each level.

The model for marketing channel design proposed by Stern, Coughlan, El-Ansary, 2002 (cited in Gudonaviþienơ, Alijosiene, 2008). The oneness of this model is that it analyses the channel creation process in more details (the model has 14 stages) and it indicates the opportunity to perform some stages at the same time (Figure 4.3).




1. Environment analysis. 2. Analysis of existing marketing channels (MCh). 3. Proposals for MCh improvement. 4. Analysis of competitors' MCh. 5. Assessment of existing MCh alternatives. 6. Composing of short time plans. 7. Quantitative analysis of consumers' needs. 9. Analysis of analogues in industry. 10. Formation of ideal MCh. 11. Formation of MCh, restricted by factors. 12. Gap analysis. 13. Strategic decision-making. 14. Design of optimal MCh.

Figure 4.3. The model for marketing channel design by Stern, Coughlan, El-Ansary

In this model (Figure ), stages 1 to 4 of marketing channel formation suppose the thorough acquaintance with present conditions and tasks. Stages 5-6 foresee the possible sharp changes in channel tactics and politics, and the stages 7 to 10 imply the formation of the new marketing channel strategy. After determining the needs of the end users, market should be segmented and accordingly the type of intermediaries should be

selected, by identifying the functions that they should be able and would be able to perform. This is the way of planning the "ideal marketing channel". The stage 11 encompasses a thorough analysis of enterprises' goals, potential, restrictions, and internal and external threats. Analysis of marketing channel alternatives is performed due to the selection of the best alternative. External as well as internal factors change the "ideal" marketing channel, by limiting possible alternatives. At the stage 12, the "ideal", the "restricted by factors" and the existing channels are compared in order to define if the existing marketing channel corresponds to the needs of customers and the enterprise. The stage 13 involves the gap analysis and analysis of possible costs, comparing the "ideal" and existing channel. After this analysis, the strategic decisions about channel design are being made. The last stage allows to implement the optimal marketing channel design. The model proposed by Stern, Coughlan, El-Ansary (2002) comprises the biggest number of marketing channel design stages that are provided in detail. The model of distribution system is created according to the needs of the end user.

The model for marketing channel design suggested by Stern, Coughlan, El-Ansary, 2006 (cited in Gudonaviþienơ, Alijosiene, 2008). The main feature of this model is the orientation to the needs of consumers. The model suggests to identify the needs of consumers and to group them into the separate segments at the very beginning of the process of channel design (Figure 4.4).

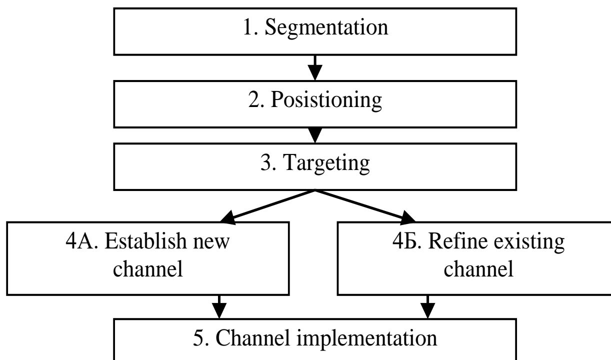



Figure 4.4. The model for marketing channel design by Stern, Coughlan, El-Ansary, 2006

The model suggested by Stern, Coughlan, El-Ansary (2006) emphasizes the needs of consumers. Identification of the consumers needs allows grouping them into separate segments. According to different needs of different targets, specific features of the product, goals and potential of the enterprise, the most acceptable marketing channel is being designed.

The model for marketing channel design supposed by Neves, Zuurbier, and Campomar (cited in Gudonaviþienơ, Alijosiene, 2008). This is one more detailed model for marketing channel design, which comprises 11 stages that are aggregated into four phases: understanding phase, objective phase, implementation phase, monitoring and revision phase. This model was created with reference to other models, especially to the model of Stem, Coughlan, El-Ansary (2002) incorporating additional channel design stages and introducing the new approach to the marketing channel itself (Figure 4.5).

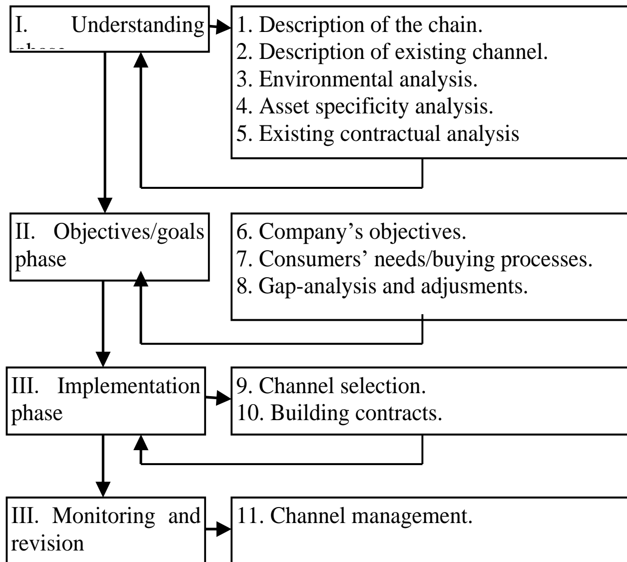



Figure 4.5. The model for marketing channel design by Neves, Zuurbier, and Campomar

As we can see from Figure 5, the first five stages of this model are attributed to the phase of understanding, i.e., the thorough analysis has to be performed. The sixth to eighth stages reflect the objective/goals phase,

i.e., the goals of marketing channel have to be identified according to the needs of consumers and the gap between the existing channel and the one, which is being designed. Stages 9-10 are attributed to the implementation phase: at this phase the selection and implementation of marketing channel is performed, making contracts with channel members. 11th stage involves the channel management. Neves, Zuurbier, Campomar (2001) suggest to begin the marketing channel planning with the description of everyone in the marketing channel, where not only a producer, intermediaries and consumer, but also the suppliers participate. Hereby we need to describe the functions of all of them and to make one systematic approach to channel structure.

Neves, Zuurbier, Campomar (2001) model was created with reference to existing theoretical models, and involves the most important stages of marketing channel formation, with some new ones added.

This chapter has been concerned with marketing channel structure and its design. The main aspects covered were:

– marketing systems: classification of marketing systems was introducev. Advantages and disadvantages of each marketing system (conventional marketing channel; horizontal marketing system; vertical marketing system) were defined.

– marketing channel design: stages of marketing channel design proposed by Rosenbloom were discussed in details. Alternative models for marketing channel design were shown.

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# SECTION 5

# SUPPLY CHAIN MANAGEMENT

## 5.1. Concept of supply chain

Chopra and Meindl (Chopra, Meindl, 2013, P. 1) believes that "a supply chain consists of all parties involved, directly or indirectly, in fulfilling a customer request. Within each organization, such as a manufacturer, the supply chain includes all functions involved in receiving and filling a customer request. These functions include, but are not limited to, new product development, marketing, operations, distribution, finance, and customer service".

Chen and Paulraj (Chen, Paulraj, 2004, P. 119) stated that a typical supply chain is a network of materials, information, and services processing links with the characteristics of supply, transformation and demand, as you can see in the figure below (Figure 5.1).

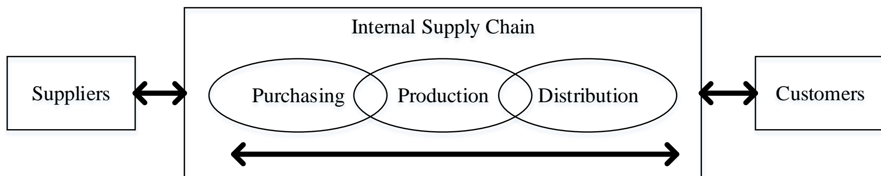


Figure 5.1. An illustration of a company's supply chain
(Chen and Paulraj, 2004, P. 120)

According to Mentzer et al. (Mentzer et al. 2001, P. 4), there is three degrees of supply chain complexity: a "direct supply chain," an "extended supply chain", and an "ultimate supply chain" (Figure 5.2). A direct supply chain consists of a company, a supplier, and a customer involved in the upstream and/or downstream flows of products, services, finances, and/or information (Figure 5.2a). An extended supply chain includes suppliers of the immediate supplier and customers of the immediate customer, all involved in the upstream and/or downstream flows of products, services, finances, and/or information (Figure 5.2b). An ultimate supply chain includes all the organizations involved in all the upstream and downstream flows of products, services, finances, and information from the ultimate

supplier to the ultimate customer (Figure 5.2c). Also, the ultimate supply chain encompasses functional intermediaries such as market research firms, financial and logistics services providers.

Figure 5.2a: Direct Supply Chain

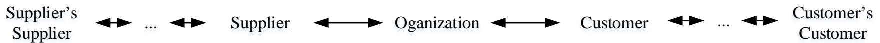


Figure 5.2b: Extended Supply Chain

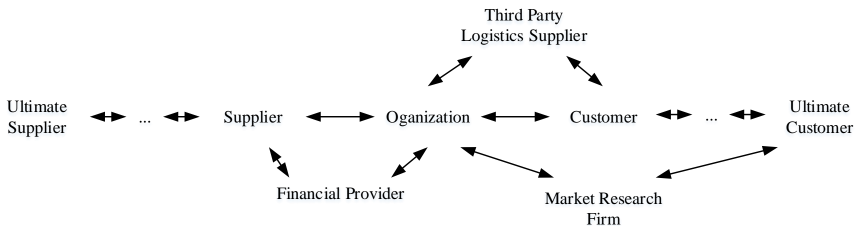


Figure 5.2c: Ultimate Supply Chain

Figure 5.2. Types of channel relationships (Mentzer et al., 2001)

The supply chain not only includes the manufacturer and its suppliers, but also (depending on the logistics flows) transporters, warehouses, retailers, and consumers themselves. It includes, but is not limited to, new product development, marketing, operations, distribution, finance, and customer service (Chopra, Meindl, 2013, P. 1).

A typical supply chain may involve a variety of stages, including the following (Chopra, Meindl, 2013, P. 2):

1. Customers.
2. Retailers.
3. Wholesalers/distributors.
4. Manufacturers.
5. Component/raw material suppliers.

Most supply chains are actually networks (Figure 5.3).

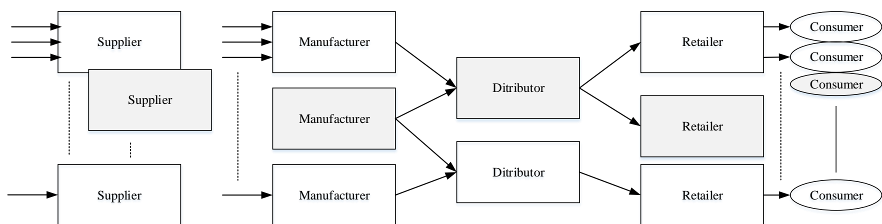


Figure 5.3. Schematic diagram of a supply chain (shaded) within the total supply chain network (Chopra, Meindl, 2013, P. 3)

A supply chain is a sequence of processes and flows that take place within and between different stages and combine to fill a customer need for a product. There are two ways to view the processes performed in a supply chain (Chopra, Meindl, 2013, P. 8):

1. Cycle View: The processes in a supply chain are divided into a series of cycles, each performed at the interface between two successive stages of a supply chain.

2. Push/Pull View: The processes in a supply chain are divided into two categories depending on whether they are executed in response to a customer order or in anticipation of customer orders. Pull processes are initiated by a customer order, whereas push processes are initiated and performed in anticipation of customer orders.

In cycle view of supply chain processes, all supply chain processes can be broken down into the following four process cycles: customer order cycle; replenishment cycle; manufacturing cycle; procurement cycle. Not every supply chain will have all four cycles clearly separated.

Each cycle consists of six subprocesses: supplier stage markets product; buyer stage places order; supplier stage receives order; supplier stage supplies order; buyer stage receives supply; buyer returns reverse flows to supplier or third party;. each cycle starts with the supplier marketing the product to customers. A buyer then places an order that is received by the supplier. The supplier supplies the order, which is received by the buyer. The buyer may return some of the product or other recycled material to the supplier or a third party. The cycle of activities then begins all over again (Chopra, Meindl, 2013, P. 9).

Within each cycle, the goal of the buyer is to ensure product availability and to achieve economies of scale in ordering. The supplier attempts to forecast customer orders and reduce the cost of receiving the

order. The supplier then works to fill the order on time and improve efficiency and accuracy of the order fulfillment process. The buyer then works to reduce the cost of the receiving process. Reverse flows are managed to reduce cost and meet environmental objectives (Chopra, Meindl, 2013, P. 9).

A cycle view of the supply chain clearly defines the processes involved and the owners of each process. This view is useful when considering operational decisions because it specifies the roles and responsibilities of each member of the supply chain and the desired outcome for each process (Chopra, Meindl, 2013, P. 10).

In push/pull view of supply chain processes all processes in a supply chain fall into one of two categories depending on the timing of their execution relative to end customer demand. With pull processes, execution is initiated in response to a customer order. With push processes, execution is initiated in anticipation of customer orders based on a forecast. Pull processes may also be referred to as *reactive processes* because they react to customer demand. Push processes may also be referred to as *speculative processes* because they respond to speculated (or forecasted) rather than actual demand. The *push/pull boundary* in a supply chain separates push processes from pull processes. Push processes operate in an uncertain environment because customer demand is not yet known. Pull processes operate in an environment in which customer demand is known. They are, however, often constrained by inventory and capacity decisions that were made in the push phase (Chopra, Meindl, 2013, P. 10).

A push/pull view of the supply chain categorizes processes based on whether they are initiated in response to a customer order (pull) or in anticipation of a customer order (push). This view is useful when considering strategic decisions relating to supply chain design (Chopra, Meindl, 2013, P. 12).

There are **four main flows** in a supply chain:

1. **Material Flow.** All manufacturing supply chains have material flows from the raw materials at the beginning of the supply chain to the finished products at the end of the supply chain (Dawei, 2011). Material flow includes a smooth flow of an item from the producer to the consumer. This is possible through various warehouses among distributors, dealers and retailers. The main challenge we face is in ensuring that the material flows as inventory quickly without any stoppage through different points in the chain. The quicker it moves, the better it is for the enterprise, as it minimizes the cash cycle. The item can also flow from the consumer to the

producer for any kind of repairs, or exchange for an end of life material. Finally, completed goods flow from customers to their consumers through different agencies. A process known as 3PL is in place in this scenario. There is also an internal flow within the customer company (Supply Chain management, 2016). A furniture-making supply chain will have the wood cut down from forest at the beginning of its supply chain and home furniture at the end of supply chain. The continuous flow of wood been transformed through the chain and end up to furniture ties the whole supply chain together and defines its clear boundary. A furniture supply chain can never be confused with a chocolate manufacturing supply chain because the material flows in between are clearly different and never will they cross with each other (Dawei, 2011).

2. **Information Flow**. All supply chains have and make use of information flows. Throughout a supply chain there are multitude of information flows such as demand information flow, forecasting information flow, production and scheduling information flows, and design and NPI information flows. Unlike the material flow the information can run both directions, towards upstream and downstream alike (Dawei, 2011). Information/data flow comprises the request for quotation, purchase order, monthly schedules, engineering change requests, quality complaints and reports on supplier performance from customer side to the supplier. From the producer's side to the consumer's side, the information flow consists of the presentation of the company, offer, confirmation of purchase order, reports on action taken on deviation, dispatch details, report on inventory, invoices, etc. For a successful supply chain, regular interaction is necessary between the producer and the consumer. In many instances, we can see that other partners like distributors, dealers, retailers, logistic service providers participate in the information network. In addition to this, several departments at the producer and consumer side are also a part of the information loop (Supply Chain management, 2016). Interestingly most of them are unique to the specific supply chain. The information of woman's fashion clothing has no value to a motorbike supply chain. Any supply chain will have its own set of information flows that are vital to its existence which are often jealously protected against those of other supply chains (Dawei, 2011).

3. **Finance Flow**. All supply chains have finance flow. It is basically the money flow or the blood stream of a supply chain. Without it, a supply chain will surely demise. However, for any supply chain, there is only one single source of such finance flow – the end-consumer. This understanding

of single source of finance has led to a concept of “single entity” perspective of a supply chain, which is a very useful foundation for supply chain integration and collaboration. The distribution and sharing of this single financial resource fairly across a supply chain will allow for the better alignment between the contribution and reward for the participating companies (Dawei, 2011). On the basis of the invoice raised by the producer, the clients examine the order for correctness. If the claims are correct, money flows from the clients to the respective producer. Flow of money is also observed from the producer side to the clients in the form of debit notes (Supply Chain management, 2016).

1. **Commercial flow**. All supply chain represents a transactional commercial flow. This means that the material flow that run through the supply chain changes its ownership from one company to another, from supplier to buyer. The transactional process of buying and selling shifts the material flow’s ownership from the supplier to the buyer repeatedly until the end of the supply chain – the end-consumer. This transactional commercial flow will only take place in a supply chain where there are more than one companies. On the other hand, if it is with an organization there will be material flow, but no ownership change, and hence no commercial flow (Dawei, 2011).

The four flows described above not only better explain the function of the supply chain, but also define it more rigorously. They represent four major areas of concerns and research activities in the supply chain management, which covers most of the known issues in the published literatures (Dawei, 2011).

**Drivers** of supply chain performance (Chopra, Meindl, P. 41-42):

1. Facilities are the actual physical locations in the supply chain network where product is stored, assembled, or fabricated. The two major types of facilities are production sites and storage sites. Decisions regarding the role, location, capacity, and flexibility of facilities have a significant impact on the supply chain’s performance.

2. Inventory encompasses all raw materials, work in process, and finished goods within a supply chain. The inventory belonging to a firm is reported under assets. Changing inventory policies can dramatically alter the supply chain’s efficiency and responsiveness.

3. Transportation entails moving inventory from point to point in the supply chain. Transportation can take the form of many combinations of modes and routes, each with its own performance characteristics.

Transportation choices have a large impact on supply chain responsiveness and efficiency.

4. Information consists of data and analysis concerning facilities, inventory, transportation, costs, prices, and customers throughout the supply chain. Information is potentially the biggest driver of performance in the supply chain because it directly affects each of the other drivers. Information presents management with the opportunity to make supply chains more responsive and more efficient.

5. Sourcing is the choice of who will perform a particular supply chain activity such as production, storage, transportation, or the management of information. At the strategic level, these decisions determine what functions a firm performs and what functions the firm outsources. Sourcing decisions affect both the responsiveness and efficiency of a supply chain.

6. Pricing determines how much a firm will charge for the goods and services that it makes available in the supply chain. Pricing affects the behavior of the buyer of the good or service, thus affecting supply chain performance.

## 5.2. Supply chain management

Supply chain management can be defined as the management of flow of products and services, which begins from the origin of products and ends at the product's consumption. It also comprises movement and storage of raw materials that are involved in work in progress, inventory and fully furnished goods (Supply Chain management, 2016).

The main objective of supply chain management is to monitor and relate production, distribution, and shipment of products and services. This can be done by companies with a very good and tight hold over internal inventories, production, distribution, internal productions and sales (Supply Chain management, 2016).

Supply chain management basically merges the supply and demand management. It uses different strategies and approaches to view the entire chain and work efficiently at each and every step involved in the chain. Every unit that participates in the process must aim to minimize the costs and help the companies to improve their long term performance, while also creating value for its stakeholders and customers. This process can also minimize the rates by eradicating the unnecessary expenses, movements and handling (Supply Chain management, 2016).

Any supply chain management practice and activities are captured by the three conceptual components: Supply Chain Configuration; Supply Chain Relationship; and Supply Chain Coordination (Dawei, 2011):

1. **Supply Chain Configuration** is about how a supply chain is constructed from all its participating firms. This includes how big is the supply base for OEM (original equipment manufacturer); how wide or narrow is the extent of vertical integration (which is the single ownership of consecutive activities along the supply chain); how much of the OEM's operations are outsourced; how the downstream distribution channel is designed; and so on. It is also known as supply chain architecture. The decision on supply chain configuration is strategic and at a higher level.
2. **Supply Chain Relationship** is about inter-firm relationships across the supply chain albeit the key focus of relationship is often around the OEM and its first-tier suppliers and first-tier customers and the relationship in between. The type and level of the relationship is determined by the contents of inter-organizational exchanges. The relationship is likely to be "arm's length" if they only exchanged the volume and price of the transaction; on the other hand, the relationship would be regarded as close partnership if the parties exchanged their vision, investment planning, NPI process and detailed financial information. The decision on supply chain relationship is both strategic and operational.
3. **Supply Chain Coordination** refers mainly to the inter-firm operational coordination within a supply chain. It involves the coordination of continuous material flows from the suppliers to the buyers and through to the end-consumer in a preferably JIM manner. Inventory management throughout the supply chain could be a key focal point for the coordination. Production capacity, forecasting, manufacturing scheduling, even customer services will all constitute the main contents of the coordination activities in the supply chain. The decision on the supply chain coordination tends to be operational.

The key concepts and derived concepts used to explain the term SCM are given below (Felea, Albăstroiu, 2013, P. 80):

– the key concepts are the following: planning, implementing, controlling, business processes, customer requirements, processing, movement, storage, point-of-origin, point-ofconsumption, relationship, integration, logistics activities, coordination, managerial processes, collaboration, organizing, , motivating, customer value, competitive advantage, suppliers, manufacturers, warehouses, stores, costs, service level, business function, performance, transportation;

– the derived concepts are the following: operations, efficiently, raw materials, workin-process inventory, finished goods, sharing data, systemic, strategic, sustainable, long-term, right quantity, to the right locations, and at the right time.

Successful SCM requires a change from managing individual business processes within one organisation to integrating activities over organisations into key supply chain processes. The key supply chain processes identified by members of The GSCF (The Global Supply Chain Forum) are (Lambert, Cooper, 2000, P. 72) in the Table 5.1.

Table 5.1. Business processes that could be integrated in the supply chain (Lambert, Cooper, 2000, P. 72)

| **Business process** | **General description** |
| --- | --- |
| Customer relationship management | Specifying service level agreements with key customers. Customer service teams work with customers to further identify and eliminate sources of demand variability. |
| Customer service management | Providing the customer with real-time information on promised shipping dates and product availability through interfaces with the organizations' production and distribution operations |
| Demand management | Balancing the customer's requirements with the firm's supply capabilities |
| Order fulfilment | Delivering products and meeting customer need dates |
| Manufacturing flow management | Pulling product through the plant based on customer needs |
| Procurement | Developing strategic plans with suppliers to support the manufacturing flow management process and development of new products |
| Product development and commercialisation | Customers and suppliers must be integrated into the product development process in order to reduce time to market |
| Returns process | Aligning processes to realise an efficient return of re-usable items |

The four major criteria of supply chain management concept are in the Table 5.2.

Table 5.2. The four major criteria of supply chain management concept (Felea, Albăstroiu, 2013, P. 81)

| Criteria | Concepts | Definition |
|---|---|---|
| 1. Management activities | *Key Concepts*: planning, organizing, implementing, motivating, controlling. *Derived Concepts:* goods, services, efficiency | SCM consist in planning organizing, implementing, motivating and controlling efficiently of all the activities involved in movement of goods and services from the first supplier to the ultimate customer. |
| 2. Logistics activities | *Key Concepts*: transportation, processing, storage. *Derived Concepts*: raw materials, work-inprocess inventory, finished goods | SCM includes transportation, processing and storage of raw materials, work-inprocess inventory and finished goods from initial extraction stage to the final customer. |
| 3. Objectives | *Key Concepts*: value, customer requirements, trust, competitive advantage, relationships. *Derived Concepts:* sustainable, long term | SCM include a number of value-added processes designed to satisfy customer requirements, to establish a long term relationships, to build the trust among the supply chain partners and to achieve a sustainable competitive advantage. |
| 4. Components | *Key Concepts*: suppliers, manufacturers, warehouses, stores. *Derived Concepts:* products, services | SCM encompasses suppliers, manufacturers, warehouses, stores and other intermediaries that are involved in the movement of products and services from point-of-origin to point-of-consumption. |

The key benefits of supply chain management are as follows (Supply Chain management, 2016):

1. Develops better customer relationship and service.
2. Creates better delivery mechanisms for products and services in demand with minimum delay.
3. Improvises productivity and business functions.
4. Minimizes warehouse and transportation costs.
5. Minimizes direct and indirect costs.
6. Assists in achieving shipping of right products to the right place at the right time.
7. Enhances inventory management, supporting the successful execution of just-in-time stock models.

8. Assists companies in adapting to the challenges of globalization, economic upheaval, expanding consumer expectations, and related differences.

9. Assists companies in minimizing waste, driving out costs, and achieving efficiencies throughout the supply chain process.

Here are some of the important goals of supply chain management (Supply Chain management, 2016):

1. Supply chain partners work collaboratively at different levels to maximize resource productivity, construct standardized processes, remove duplicate efforts and minimize inventory levels.

2. Minimization of supply chain expenses is very essential, especially when there are economic uncertainties in companies regarding their wish to conserve capital.

3. Cost efficient and cheap products are necessary, but supply chain managers need to concentrate on value creation for their customers.

4. Exceeding the customers' expectations on a regular basis is the best way to satisfy them.

5. Increased expectations of clients for higher product variety, customized goods, off-season availability of inventory and rapid fulfillment at a cost comparable to in-store offerings should be matched.

6. To meet consumer expectations, merchants need to leverage inventory as a shared resource and utilize the distributed order management technology to complete orders from the optimal node in the supply chain.

SCM literature suggests several redesign strategies to improve the **effectiveness and efficiency** of these business processes in the supply chain. Van der Vorst and Beulens (Vorst, van der et al., 2002, cited in Camps et al., 2004) have identified a generic list of SCM redesign strategies to facilitate the redesign process and accomplish joint supply chain objectives. These are the following:

1. Redesign the roles and processes performed in the supply chain (e.g. change or reduce the number of parties involved, re-allocate roles and eliminate non-value-adding activities).

2. Reduce customer order lead times (e.g. change the position of the decoupling point (see the next section), implement ICT systems for information exchange and decision support, reduce waiting times, increase manufacturing flexibility).

3. Create information transparency (e.g. establish an information exchange infrastructure in the supply chain and exchange demand/supply/inventory or WIP information, standardise product coding).

4. Synchronise logistical processes to consumer demand (e.g. increase execution frequencies of production and delivery processes, decrease the lot sizes).

5. Co-ordinate and simplify logistical decisions in the supply chain (e.g. co-ordinate lot sizes, eliminate human interventions, differentiate and simplify products, systems and processes).

Supply chain performance measure can be defined as an approach to judge the performance of supply chain system. Supply chain performance measures can broadly be classified into two categories (Supply Chain management, 2016):

1. Qualitative measures: For example, customer satisfaction and product quality.

2. Quantitative measures: For example, order-to-delivery lead time, supply chain response time, flexibility, resource utilization, delivery performance.

Here, we will be considering the **quantitative performance measures** only. The performance of a supply chain can be improvised by using a multi-dimensional strategy, which addresses how the company needs to provide services to diverse customer demands.

Mostly the measures taken for measuring the performance may be somewhat similar to each other, but the objective behind each segment is very different from the other.

**Quantitative measures** is the assessments used to measure the performance, and compare or track the performance or products. We can further divide the quantitative measures of supply chain performance into two types. They are (Supply Chain management, 2016):

– non-financial measures;

– financial measures.

**I. The metrics of non-financial measures** comprise cycle time, customer service level, inventory levels, resource utilization ability to perform, flexibility, and quality. In this section, we will discuss the first four dimensions of the metrics (Supply Chain management, 2016):

1. **Cycle time** is often called the lead time. It can be simply defined as the end-to-end delay in a business process. For supply chains, cycle time can be defined as the business processes of interest, supply chain process and the order-to-delivery process. In the cycle time, we should learn about two types of lead times. They are as follows (Supply Chain management, 2016):

– supply chain lead time;

– order-to-delivery lead time.

The order-to-delivery lead time can be defined as the time of delay in the middle of the placement of order by a customer and the delivery of products to the customer. In case the item is in stock, it would be similar to the distribution lead time and order management time. If the ordered item needs to be produced, it would be the summation of supplier lead time, manufacturing lead time, distribution lead time and order management time.

The supply chain process lead time can be defined as the time taken by the supply chain to transform the raw materials into final products along with the time required to reach the products to the customer's destination address.

Hence it comprises supplier lead time, manufacturing lead time, distribution lead time and the logistics lead time for transport of raw materials from suppliers to plants and for shipment of semi-finished/finished products in and out of intermediate storage points.

Lead time in supply chains is governed by the halts in the interface because of the interfaces between suppliers and manufacturing plants, between plants and warehouses, between distributors and retailers and many more.

Lead time compression is a crucial topic to discuss due to the time based competition and the collaboration of lead time with inventory levels, costs, and customer service levels.

2. **Customer service level.** The customer service level in a supply chain is marked as an operation of multiple unique performance indices. Here we have three measures to gauge performance. They are as follows (Supply Chain management, 2016):

– order fill rate: The order fill rate is the portion of customer demands that can be easily satisfied from the stock available. For this portion of customer demands, there is no need to consider the supplier lead time and the manufacturing lead time. The order fill rate could be with respect to a central warehouse or a field warehouse or stock at any level in the system;

– stockout rate: It is the reverse of order fill rate and marks the portion of orders lost because of a stockout;

– backorder level: This is yet another measure, which is the gauge of total number of orders waiting to be filled;

–probability of on-time delivery: It is the portion of customer orders that are completed on-time, i.e., within the agreed-upon due date.

In order to maximize the customer service level, it is important to maximize order fill rate, minimize stockout rate, and minimize backorder levels.

3. **Inventory levels.** As the inventory-carrying costs increase the total costs significantly, it is essential to carry sufficient inventory to meet the customer demands. In a supply chain system, inventories can be further divided into four categories (Supply Chain management, 2016):

–raw materials;

–work-in-process, i.e., unfinished and semi-finished sections;

–finished goods inventory;

–spare parts.

Every inventory is held for a different reason. It's a must to maintain optimal levels of each type of inventory. Hence gauging the actual inventory levels will supply a better scenario of system efficiency.

4. **Resource utilization.** In a supply chain network, huge variety of resources is used. These different types of resources available for different applications are mentioned below (Supply Chain management, 2016):

–manufacturing resources: Include the machines, material handlers, tools, etc.;

–storage resources: Comprise warehouses, automated storage and retrieval systems;

–logistics resources: Engage trucks, rail transport, air-cargo carriers, etc.;

–human resources: Consist of labor, scientific and technical personnel;

–financial resources: Include working capital, stocks, etc.

In the resource utilization paradigm, the main motto is to utilize all the assets or resources efficiently in order to maximize customer service levels, reduce lead times and optimize inventory levels.

**II. Financial Measures.** The measures taken for gauging different fixed and operational costs related to a supply chain are considered the financial measures. Finally, the key objective to be achieved is to maximize the revenue by maintaining low supply chain costs (Supply Chain management, 2016).

There is a hike in prices because of the inventories, transportation, facilities, operations, technology, materials, and labor. Generally, the

financial performance of a supply chain is assessed by considering the following items:

– cost of raw materials;

– revenue from goods sold;

– activity-based costs like the material handling, manufacturing, assembling rates etc.;

– inventory holding costs;

– transportation costs;

– cost of expired perishable goods;

– penalties for incorrectly filled or late orders delivered to customers;

– credits for incorrectly filled or late deliveries from suppliers;

– cost of goods returned by customers;

– credits for goods returned to suppliers.

Financial performance indices can be merged as one by using key modules such as activity based costing, inventory costing, transportation costing, and inter-company financial transactions.

There are number of early **development trends** that can be observed evidently (Dawei, 2011):

1. **From functional to process perspective**. Business management used to see and take action on the functional silos in the business. It was understandable that naturally the function is what seen to be the delivery part of the business. But, today with supply chain management concept managers can see their problems more from the process perspective, understanding that functions can only make sense if it is perceived from a supply chain process perspective.

2. **From operational to strategic viewpoint**. At early years of applying supply chain management concept, managers tend to see it as another operational tactics that will help to reduce operational cost, such as purchasing function improvement and optimizing the logistics operations. But gradually more and more managers realized that the effective changes can only be achieved if the operational issues are addressed from the supply chain wide strategic viewpoint. Operational excellence can only be manifested through its strategic fit.

3. **From single enterprise to extended enterprise**. Enterprise management is now arguably displaced by the supply chain management, where the supply chain is by definition the extended enterprise. The long-established enterprise-centred management thinking was based on that the competition was raged between the organizations, thus it becomes obsolete

as the competitions are now predominantly between the supply chains. Management thinking over the extended enterprise produces a great deal idea that single enterprise alone cannot.

4. **From transactional to relationship-based engagement**. Business engagement between firms in the past was predominantly transaction based and cost driven. The merit of any purchasing and procurement of externally sourced materials and services was judged by the transactional measures such as price, volume and delivery terms. But what's now more of the practices in working with external organizations within the supply chain is so called relationship-based engagement. This relationship approach does not abandon the transactional activities but put its decision baking on much wider consideration of knowledge exchange, long-term commitment, incentives and reward.

5. **From local to regional, and from regional to global**. Connections of supply network have over the last two decades grown from local to regional and to global. Hardly any major enterprise and supply chains is not connected to some part of the world. You need to get out before you can get up. This trend is spurred by the lower cost of labour and materials in many parts of the world, as well as first mover advantages in setting up global market presence.

**Current trends in global SCM are the following** (Dawei, 2011)**:**

**Trend 1**: Supply chain volatility and market uncertainty is on the rise.

The fast development of cyber market and mobile media has given rise to the market visibility leading to high level of market transparency. B2B customers and consumers have found it a lot easier to shop for alternative lower price or better value. The switching cost is evaporated rapidly, and so is the customer loyalty, which adds salt to the injury. The only known approaches to deal with the trend of increased volatility are improving forecasting accuracy and planning for flexible capacity throughout the supply chain. Best performing companies tends to improve supply chain responsiveness through improving visibilities across all supply chain partners. On the downstream side, companies are now focusing more on deepening collaboration with key customers to reduce unanticipated changes.

**Trend 2**: Market growth depends increasingly on global customers and supplier networks.

The immediate implication of this trend is that the supply chain will have to produce higher number of products or variants to fulfil the

customer expectations, albeit this may vary slightly for different geographical regions. In the main, the pattern of global supply chain is going to be more complex in terms of new customer locations, market diversity, product variants, and demand volatility.

On the supply side, the trends indicated that a more dynamic supply networks stretching far and wide globally. Managing those suppliers, developing them and integrating them become more a critical challenge than ever before.

**Trend 3**: Towards more cost-optimized supply chain configurations.

Globalizing supply chain operations and outsourcing specific functions are viewed as critical for controlling costs. It came as no surprise that outsourcing is on the rise across many industrial sectors around the world. Companies are taking advantages of lower costs in emerging markets and increasing their flexibility of their own supply chain. The functions that will see the greatest increase in outsourcing are product development, supply chain planning and shared services.

However, globalization does not seem to have reduced process and management costs. In fact, those hidden costs could be on the rise when supply chain becomes more global if not careful. Leading companies understand the impact of those hidden costs and are taking aggressive steps to identify and manage them. Many are embracing new concepts like Total Supply Chain Cost Engineering, an integral approach to calculating and managing total cost across all supply chain functions and interfaces. Rigorous cost optimization across the end-to-end supply chain – from order management, sourcing, and manufacturing to logistics and transportation – are critical for success.

**Trend 4**: Risk management involves end-to-end supply chain.

To date, risk has become an increasingly critical management challenge across the global supply chains. Dealing with cost pressures of their own, many customers have increased their efforts in asset management and have started shifting supply chain risks, such as inventory holding risks, upstream to their suppliers. This approach, however, merely shifts risks from one part of the supply chain to another but not reduces it for the whole supply chain. These end-to-end supply chain practices include advanced inventory management, joint production and material resource planning, improved delivery to customers and so forth.

Leading companies are taking an end-to-end approach in managing risk at each node of the supply chain. To keep the supply chain as lean as possible, they are taking a more active role in demand planning, which

ensures they order only the amount of material needed to fill firm orders. Firms are also limiting the complexity of products that receive late-stage customization. Leading companies mitigate inventory-related risks by shifting the responsibility for holding inventory to their suppliers and, furthermore, by making sure finished product is shipped immediately to customers after production.

**Trend 5**: More emphasis on supply chain integration and empowerment.

Little can be achieved without appropriate management approaches that truly integrated across all functions throughout the supply chain and empowered them to take bold action. Integrated supply chain management across all key functions still seen to be a myth, with many procurement and manufacturing executives making silo optimization decisions.

Leading companies understand that breakthrough improvements are not possible unless the decisions made are optimal for all supply chain functions. For this reason, they have already taken steps to integrate and empower their supply chain as a single resource under one joint responsibility. These firms are making sure the organization has a strong end-to-end optimization and are integrating supply chain partners up and downstream.

However, the location design for the whole supply chain will mainly consider two aspects of the whole supply chain. The single operation's location decision has to be made in conjunction with the other operations' locations decisions. In other words, it is the combined effect of all locations together that matters for the supply chain. It has been well documented that the total supply chain cost consists broadly two components: the physical cost and market cost.

The **physical cost** measures the supply chain operational efficiency as a whole. It looks at all the involved cost that are necessary for the supply chain to transform the raw materials to the end products for the consumer. It includes the production cost, logistics cost, material cost, labour cost, taxation cost, energy cost and so on. The **market cost** looks at all the loss or cost incurred by the inappropriate supply chain market mediation. If a supply chain failed to produce the products that are the right quantity for the market at the season, delivered to the right location where customers find it convenient to access to, with right quality and functions that they expect, at the right prices that they are willing to pay for, the supply chain will make loss either on unsold products or unsatisfied customers.

measured by the product delivery process (PDP) cost in general (Dawei, 2011).

**An agile supply chain** can be defined as a chain of supply that has the potential to respond to changing requirements in a way that accelerates the delivery of ordered goods to customers (Supply Chain management, 2016). In simple words, supply chain agility is a custom adopted by many companies for choosing a dealer. As we know, a supply chain with flexibility and the ability to quickly react to emergency requirements can help the business answer more efficiently to its customers. Apart from flexibility, speed and accuracy are also signature marks of this type of supply chain.

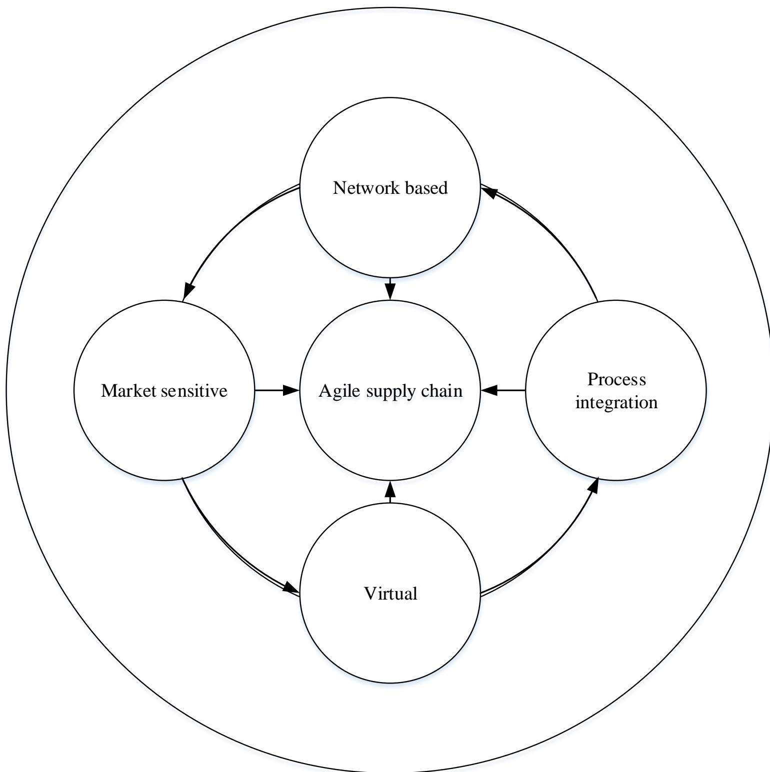


Figure 5.4. Agile supply chain (Supply Chain management, 2016)

To acknowledge the advantages of an agile supply chain, we have to learn about the elements of any type of supply chain. These include elements like collection of orders and processing, supply of materials to create the goods used to complete orders, packaging and transport of finished goods, and the quality of customer service that is advertised throughout the process from the point of sale to the actual delivery and beyond (Supply Chain management, 2016).

Thus, for considering the functions of supply chain as agile, each one of these elements must be managed efficiently and coordinated in such a way that makes it possible to adapt to changing circumstances. With the help of an agile supply chain, merchants can easily respond to the varying requirements of customer with relatively less time required. For example, if a client has already placed a sizable order but demands the product to be delivered few days prior to the projected delivery date, a merchant with a truly agile supply chain can easily accommodate that change in the client's situation, at least in part. Working collaboratively, the merchant and the customer develop a strategy to permit the delivery of as much of the order as possible within the new time frame required (Supply Chain management, 2016).

There are times when merchants need to think creatively along with some flexibility in terms of scheduling production time, selecting shippers and basically looking closely at each step in the order completion process to search for ways to reduce the time required to successfully accomplish those tasks and abide with the customer's request.

**Reverse supply chain** states the evolution of products from customer to merchant. This is the reverse of the traditional supply chain evolution of products from merchant to customer (Supply Chain management, 2016).

**Reverse logistics** is the process of planning, executing, monitoring and controlling the efficient and effective inbound flow and storage of secondary goods and information related to the purpose of recovering value or proper disposal. Some examples of reverse supply chain are as follows (Supply Chain management, 2016):

1. Product returns and handling product displacement.
2. Remanufacturing and refurbishing exercises.
3. Management and sale of surplus, along with returned equipment and machines from the hardware leasing business.

Different types of reverse supply chain arise at different stages of the product cycle. Mostly reverse supply chain is designed to carry out the below given five key processes (Supply Chain management, 2016):

1. Product acquisition: Accumulating the used product from the user by the reseller or manufacturer because of some manufacturing defect or some other reason. It is basically considered as a company's growth strategy.
2. Reverse logistics: Shipping of products from their final destination for auditing, sorting and disposition.
3. Inspection and disposition: Examining the condition of the product returned along with making the most profitable decision for reusing it in some other way.
4. Remanufacturing or refurnishing: Returning the product to its original source from where it was ordered in the very first place along with specifications. This is done basically when there is a manufacturing or furnishing defect in the goods.
5. Marketing: Establishing secondary markets for the goods that have been recovered by the merchant from the client who initially ordered it in the beginning but chose to return it.

In short, we can say that the enterprises that closely coordinate with their forward supply chains are the one that have been most successful with their reverse supply chains. These two chains create a closed-loop system. For example, the company designs a product layout according to the manufacturing decisions followed by recycling and reconditioning.

Technology plays a great role here by reducing the inspection and disposition costs, sanctioning the company to make a profit on the remanufactured tools. In fact, along with reverse supply chains, forward thinking results in big dividends.

Capacity synchronisation has another major beneficial effect. It helps to alleviate the Bullwhip Effects in the supply chain, and the bullwhip effect is a very common phenomenon which has many negative impacts on the supply chain performances. Understanding the bullwhip effect is therefore essential to the supply chain design and planning (Dawei, 2011).

Bullwhip Effect refers to a supply chain-wide phenomenon that modest change of customer demand is distorted and amplified toward the upstream end of the supply chain resulting in large variations of orders placed upstream. Bullwhip effect is also known as Forrester Effect as Jay Forrester (1961) showed that this was so by modelling supply chain mathematically and he called it industrial dynamics. What happened

basically is that when the small demand ripple in the market place is felt by the retailer at the end of the supply chain, the retailer will then start adjusting their orders to the wholesalers, and the wholesaler in turn will adjust its orders to the distributer, and the distributer to the factory. One would imagine when the factory receives the orders, it will have the equally small changes. Unfortunately, it could not be farther from the truth. The small ripples have been significantly amplified stage by stage towards the upstream of the supply chain (Dawei, 2011).

Such phenomenon has been observed repeatedly and reliably through all types of supply chains. It is therefore appropriate to generalize it and theorise it as a universal "effect" model, through which analysis and simulations can be applied. Basically, the bullwhip effect has three key characteristics. **The first** is oscillation. The demand, orders or inventories move up and down in an alternative pattern. **The second** is amplification. The magnitude of the alteration and fluctuation increases as it travels to the upstream end of the supply chain. **The third** is phase lag. The cycle of peaks and troughs of one stage also tends to lag behind the one in the previous stage (Dawei, 2011).

There is a constant interplay between changes in the environment and the concepts, tools and techniques used in business. The market in most industries is changing from a rather stable to a highly unstable environment characterized by short product life cycles, high volatility, low predictability and a high degree of impulse buying by the consumer. **The Demand Chain Management (DCM) concept** is designed to this new environment by explicitly focusing on the customer and aligning interorganizational processes accordingly. The purpose is to create a unique competence aimed at identifying and satisfying customer needs and wishes (Ericsson, 2011).

DCM is not a replacement of SCM, it is one very distinct set of relationships (partnerships). The advantage is that DCM, in this interpretation, is quite well defined and useful in practical applications.

DCM is focusing on the structure and behavior in value chains based on trust and mutual interdependence to create superior perceived consumer value. With this frame of reference, the demand chain may be defined as an integrated and aligned chain built on partnership and mutual interdependence aiming at creation of a unique competence to identify and satisfy customer perceived value, while DCM may be defined as the effort to create, retain and continuously develop a dynamically aligned demand chain (Ericsson, 2011).

One of the main ideas of DCM is to integrate key customers and suppliers in the process in order to improve and to reduce lead time in product development and commercialisation. When product life-times are reduced, products have to be developed and launched in a much shorter time in order to maintain and improve competitive power. This means that the necessity for cross functional and interorganizational integration and cooperation increases. Concurrent design is a rapidly increasing concept aimed at handling this requirement (Ericsson, 2011).

The fashion industry is a very telling example of this. Zara is an example of a company that has reached success by involving people from the right departments and partners at the right time. In a SCM approach all processes have to be taken into account, but the relative importance of the processes and activities can vary (Ericsson, 2011).

The differences between the two concepts (SCM amd DCM) from the literature explained and presented in Table below.

Table 5.3. Comparisons between Demand and Supply Chain (cited in Anning, Okyere, Annan, 2013)

| Characteristics | Supply chain | Demand Chain |
|---|---|---|
| Focus on design | Differed product differentiation | Collaborative filtering |
| Focus on optimization | Stock (product, service and idea) | Customer demand |
| Customer orientation | Satisfy every order, every day at the lowest cost | Attract and retain the most Profitable customer |
| Data requirement | Extract meaning past | Real time data |
| Defining characteristics | Reliability | Agility |
| Process regulated | Control mechanism | Trust Mechanism |
| Output Positioning | End of process | Throughout the process |
| Information Flow | Push data management | Pull data management |
| End to end commitment | Process vs. function source | More process managed largely through functions/channels aligned to consumer real need |
| Waste | All time or cost that does not directly touch product or satisfy goal | Any deviation from brand experience |

The ten principles of the global compact and supply chain sustainability are in Table below.

Table 5.4. The Ten Principles of the Global Compact and Supply Chain Sustainability (Rezaee, 2018)

| The Ten Principles | Relationship to Supply Chain Sustainability |
|---|---|
| 1 | 2 |
| Human Rights.<br>Principle 1: Businesses should support and respect the protection of internationally proclaimed human rights.<br>Principle 2: make sure that they are not complicit in human rights abuses.<br>Principle 3: Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining.<br>Principle 4: the elimination of all forms of forced and compulsory labour.<br>Principle 5: the effective abolition of child labour.<br>Principle 6: the elimination of discrimination in respect of employment and occupation | Companies have a responsibility to respect human rights. The baseline responsibility is not to infringe on the rights of others. In addition, business can take steps to support and promote the realization of human rights, and there are good business reasons to do so.<br>Labour conditions in offices, in factories, on farms and at natural resource extraction sites such as mines, particularly in the developing world, often fall significantly below international standards and national regulatory requirements and can lead to serious human rights abuses. Businesses should strive to uphold international labour standards within their supply chains, including the right to freely chose employment, the freedom of children from labour, freedom from discrimination and the freedom of association and collective bargaining.<br>In addition, workers at times suffer from other labour rights abuses, including excessive work hours, degrading treatment by employers and inhibited movement.<br>In order to avoid complicity in abuses, businesses should seek to ensure that they do not cause the rights of workers and others affected by their supply chain to be infringed upon, including the right to freedom of movement, freedom from inhumane treatment, the right to equal pay for equal work and the right to rest and leisure. The rights of all peoples to work in safe and healthy working conditions are critically important as well.<br>Companies can also begin to address human rights (including and beyond labour conditions) alone or by working with partners to promote a broad range of human rights such as gender equality and access to education and health |
| Environment.<br>Principle 7: Businesses should support a precautionary approach to environmental challenges.<br>Principle 8: undertake initiatives to promote greater environmental responsibility.<br>Principle 9: encourage the development and diffusion of environmentally friendly technologies | Environmental impacts from supply chains are often severe, particularly where environmental regulations are lax, price pressures are significant and natural resources are (or are perceived to be) abundant. These impacts can include toxic waste, water pollution, loss of biodiversity, deforestation, long term damage to ecosystems, hazardous air emissions as well as high greenhouse gas emissions and energy use. Companies should engage with suppliers to improve environmental impacts, by applying the precautionary approach, promoting greater environmental responsibility and the<br>usage of clean technologies |

Table 5.4 (continued)

| 1 | 2 |
|---|---|
| Anti-Corruption.<br>Principle 10: Businesses should work against corruption in all its forms, including extortion and bribery | The significant corruption risks in the supply chain include procurement fraud and suppliers who engage in corrupt practices involving governments. The direct costs of this corruption are considerable, including product quality, but are often dwarfed by indirect costs related to management time and resources spent dealing with issues such as legal liability and damage to a company's reputation. Companies that engage with their supply chains through meaningful anti-corruption programmes can improve product quality, reduce fraud and related costs, enhance their reputations for honest business conduct, improve the environment for business and create a more sustainable platform for future growth |

Business Drivers for Supply Chain Sustainability are (Rezaee, 2018):

1. Managing business risks:

– minimize business disruption from environmental, social and economic impacts;

– protect company's reputation and brand value.

2. Realizing efficiencies:

– reduce cost of material inputs, energy, transportation;

– increase labour productivity;

– create efficiency across supply chains.

3. Creating sustainable products:

– meet evolving customer and business partner requirements;

– innovate for changing market.

"The Seven Principles of Supply Chain Management" provides a clear and compelling case for excellence in supply chain management and are the following (Anderson, Britt, & Favre, 2013):

**Principle 1:** Segment customers based on the service needs of distinct groups and adapt the supply chain to serve these segments profitably.

**Principle 2:** Customize the logistics network to the service requirements and profitability of customer segments.

**Principle 3:** Listen to market signals and align demand planning accordingly across the supply chain, ensuring consistent forecasts and optimal resource allocation.

**Principle 4:** Differentiate product closer to the customer and speed conversion across the supply chain.

**Principle 5:** Manage sources of supply strategically to reduce the total cost of owning materials and services.

**Principle 6:** Develop a supply chain-wide technology strategy that supports multiple levels of decision making and gives a clear view of the flow of products, services, and information.

**Principle 7:** Adopt channel-spanning performance measures to gauge collective success in reaching the end-user effectively and efficiently.

This chapter has been concerned with supply chain management. The main aspects covered were:

– supply chain: types and structure of supply chains were defined. The main flows in a supply chain were introduced. Drivers of supply chain were performed;

– supply chain management: conceptual components supply chain management were investigated. Major criteria of supply chain management concept were defined. Goals and benefits of SCM were highlighted.

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# CONCLUSIONS

The dynamism of the environment of marketing channels functioning, modern trends in the development of wholesaling and retailing, the development of competition are factors that already seriously affect the formation, functioning, and management of marketing channels. In these conditions, the success on the market is achieved by those marketing channels that meet the challenges.

Accordingly, managers and economists of enterprises and institutions must know the theory and methodology of marketing channels formation and management, have practical skills in applying appropriate techniques. This is what this textbook focuses on.

The book presents the main modern trends that must be taken into account while designing and operating marketing channels. Particular attention is paid to the marketing channels formation and the establishment of relationships between participants in these channels as a way of adding value creation.

Besides, the issues of combining marketing and logistics in marketing channels and the formation of supply chains on this basis are revealed.

The form of the material submitted is focused on lecturers and students of economic specialties, and practitioners (specialists in the field of management and marketing, etc.). The presented materials can be used as a methodological aid in solving practical problems.

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У підручнику розглянуто теоретико-методичні основи маркетингової політики розподілу, зокрема розроблення, управління та контроль каналів маркетингу на підприємствах, установлення взаємовідносин між учасниками маркетингових каналів, формування ланцюгів поставок.

Навчальний посібник спрямований на керівників вищих ланок промислових підприємств, спеціалістів, науковців у сфері управління збутом і суміжних галузях. Буде корисним викладачам, аспірантам, студентам економічних спеціальностей ЗВО, а також широкому колу читачів, які цікавляться проблемами маркетингової політики розподілу.

Підручник містить приклади й фактичні матеріали, що ілюструють теоретичні основи.