CHAPTER-6

KEY ISSUES IN DETERMINING CHANNEL REQUIREMENT

- DISTRIBUTION CHANNELS KEY CONCEPTS & STEPS
- KEY MANAGEMENT ISSUES
- ETHICAL ISSUES IN MARKETING CHANNELS
KEY ISSUES IN DETERMINING CHANNEL REQUIREMENT

1. DISTRIBUTION CHANNELS KEY CONCEPTS & STEPS

Before you begin
You can evaluate a new distribution channel or improve your channel marketing / management at any time. It's especially important to think about distribution when you're going after a new customer segment, releasing a new product, or looking for ways to aggressively grow your business.

Evaluate how your end-users need to buy
Your distribution strategy should deliver the information and service your prospects need. For each customer segment, consider:
  ➢ How and where they prefer to buy
  ➢ Whether they need personalized education and training
  ➢ Whether they need additional products or services to be used along with yours
  ➢ Whether your product needs to be customized or installed
  ➢ Whether your product needs to be serviced

Match end-user needs to a distribution strategy
If your end-users need a great deal of information and service, your company can deliver it directly through a sales force. You can also build a channel of qualified resellers or consultants. The size of the market and your price will probably dictate which scenario is best.
If the buying process is fairly straightforward, you can sell direct via a website/catalog or perhaps through a wholesale/retail structure. You may also use an inbound telemarketing group or a field sales team.
If you need complete control over your product's delivery and service, adding a channel probably isn't right for you.

Identify natural partners
If you want to grow beyond the direct model, look for companies that have relationships with your end-users. If consultants, wholesalers or retailers already reach your customer base, they're natural partners.
Build your distribution channel
If you're setting up a distribution channel with one or more partners, treat it as a sales process:

- Approach the potential channel partner and "sell" the value of the partnership.
- Establish goals, service requirements and reporting requirements.
- Deliver inventory (if necessary) and sales/support materials.
- Train the partner.
- Run promotions and programs to support the partner and help them increase sales.

Minimize pricing conflicts
If you use multiple channels, carefully map out the price for each step in your channel and include a fair profit for each type of partner. Then compare the price that the end-user will pay; if a customer can buy from one channel at a lower price than from another, your partners will rightfully have concerns. Pricing conflict is common, and it can jeopardize your entire strategy, so do your best to map out the price at each step and develop the best solution possible.

Drive revenue through the channel
Service your channel partners as you'd service your best customers and work with them to drive revenue. For example, provide them with marketing funds or materials to promote your products; run campaigns to generate leads and forward them to your partners.

After Distribution Channels
As you're creating a new channel you'll need a pricing strategy and a sales process. When your channel is up and running, you can start launching marketing campaigns to channel partners and end-users.

Distribution channels are formed to solve three critical distribution problems: functional performance, reduced complexity, and specialization. The central focus of distribution is to increase the efficiency of time, place, and delivery utility. When demand and product availability are immediate, the producer can perform the exchange and delivery functions itself. However, as the number of producers grows and the geographical dispersion of the customer base expands, the need for both internal and external intermediaries who can facilitate the flow of products, services, and information via a distribution process increases.

Distribution management also can decrease overall channel complexity through sorting and assistance in routinization. Sorting is the group of activities associated with transforming products acquired from manufacturers into the assortments and quantities demanded in the marketplace. Routinization refers to the policies and procedures providing common goals, channel arrangements, expectations, and mechanisms to facilitate efficient transactions. David F. Ross describes sorting as including four primary functions: Sorting is the function of physically separating a heterogeneous group of items into homogeneous subgroups. This includes grading and grouping individual items into an inventory lot by quality or eliminating defects from the lot.
Accumulating is the function of combining homogeneous stocks of products into larger groups of supply. Allocation is the function of breaking down large lots of products into smaller salable units. Assorting is the function of mixing similar or functionally related items into assortments to meet customer demand. For example, putting items into kit form. As the supply chain grows more complex, costs and inefficiencies multiply in the channel. In response, some channels add or contain partners that specialize in one or more of the elements of distribution, such as exchange or warehousing. Specialization then improves the channel by increasing the velocity of goods and value-added services and reducing costs associated with selling, transportation, carrying inventory, warehousing, order processing, and credit.

**ROLE OF THE DISTRIBUTION FUNCTION**

There are a number of critical functions performed by the channel distributor. Ross describes these functions as:

**Product acquisition.** This means acquiring products in a finished or semi-finished state from either a manufacturer or through another distributor that is higher up in the supply channel. These functions can be performed by independent channel intermediaries or by the distribution facilities of manufacturing companies.

**Product movement.** This implies significant effort spent on product movement up or down the supply channel.

**Product transaction.** Distributors can be characterized as selling products in bulk quantities solely for the purpose of resale or business use. Downstream businesses will then sell these products to other distributors or retailers who will sell them directly to the end customer, or to manufacturers who will consume the material/components in their own production processes.

Following are the separate elements contained within the three critical functions of distribution:

**Selling and promoting.** This function is very important to manufacturers. One strategy involves the use of distribution channels to carry out the responsibilities of product deployment. In addition to being marketing experts in their industry, distribution firms usually have direct-selling organizations and a detailed knowledge of their customers and their expectations. The manufacturer utilizing this distributor can then tap into these resources. Also, because of the scale of the distributing firm's operations and its specialized skill in channel management, it can significantly improve the time, place, and possession utilities by housing inventory closer to the market. These advantages mean that the manufacturer can reach many small, distant customers at a relatively low cost, thus allowing the manufacturer to focus its expenditures on product development and its core production processes.

**Buying and building product assortments.** This is an extremely important function for retailers. Most retailers prefer to deal with few suppliers providing a wide assortment of products that fit their merchandising strategy rather than many with limited product lines.
This, of course, saves on purchasing, transportation, and merchandizing costs. Distribution firms have the ability to bring together related products from multiple manufacturers and assemble the right combination of these products in quantities that meet the retailer's requirements in a cost-efficient manner.

**Bulk breaking.** This is one of the fundamental functions of distribution. Manufacturers normally produce large quantities of a limited number of products. However, retailers normally require smaller quantities of multiple products. When the distribution function handles this requirement it keeps the manufacturer from having to break bulk and repackage its product to fit individual requirements. Lean manufacturing and JIT techniques are continuously seeking ways to reduce lot sizes, so this function enhances that goal.

**Value-added processing.** Postponement specifies that products should be kept at the highest possible level in the pipeline in large, generic quantities that can be customized into their final form as close as possible to the actual final sale. The distributor can facilitate this process by performing sorting, labeling, blending, kitting, packaging, and light final assembly at one or more points within the supply channel. This significantly reduces end-product obsolescence and minimizes the risk inherent with carrying finished goods inventory.

**Transportation.** The movement of goods from the manufacturer to the retailer is a critical function of distribution. Delivery encompasses those activities that are necessary to ensure that the right product is available to the customer at the right time and right place. This frequently means that a structure of central, branch, and field warehouses, geographically situated in the appropriate locations, are needed to achieve optimum customer service. Transportation's goal is to ensure that goods are positioned properly in the channel in a quick, cost-effective, and consistent manner.

**Warehousing.** Warehousing exists to provide access to sufficient stock in order to satisfy anticipated customer requirements, and to act as a buffer against supply and demand uncertainties. Since demand is often located far from the source (manufacturer), warehousing can provide a wide range of marketplaces that manufacturers, functioning independently, could not penetrate.

**Marketing information.** The distribution channel also can provide information regarding product, marketplace issues, and competitors' activities in a relatively short time.

### 2. **KEY MANAGEMENT ISSUES**

While manufacturing firms face an agenda of issues related to finance, marketing and industrial relations, attention is focused on selected topics of manufacturing that directly impact marketing channel arrangements. Two keys of manufacturing issues are discussed:

(2.1) product proliferation and dynamics and (2.2) total quality initiatives. Although not a comprehensive list of all channel manufacturer-related issues, these two issues are significant drivers for a typical firm in determining how channel requirements will be delineated.
2.1 Product Proliferation and Dynamics

Product proliferation occurs when organizations market many variations of the same products. This can be done through different color combinations, product sizes and different product uses. This produces diversity for the firm as it is able to capture its sizable portion of the market. However, it can also be considered that marketing so many new products leads to economic resources being wasted; the consumer becomes confused and mistakes are made in the purchase of products.

Product proliferation is often used by incumbent firms as method of entry deterrence. By developing a large variety of products, the incumbent firm is able to occupy gaps in the market that potential entrants may have exploited, thus reducing the threat of competition.

The very dynamism of product proliferation makes it hard to manage. Complexity is spawned by an ever-changing landscape of customer demand and companies' attempts to meet that demand with configurable products and more product variations.

Product proliferation can sometimes also lead to cannibalization of the existing product line of the company and should be justified by overall increase in market share.

Product proliferation is an important tool of competitive strategy used by firms in diverse industries. As discussed by Connor (1981), indicators of product proliferation include a large number of new product introductions, wide product variety, and long product lines. Today, the practice of product proliferation is clearly evident.[1] For example, in 1994 new product introductions in supermarkets set records when over 21,000 new SKUs were launched. In the beverage category alone, almost two thousand new SKUs are added each year to the 20,000 existing beverage SKUs. Crest and Colgate each have more than 35 types of toothpaste, and Head & Shoulders dandruff shampoo has 15 different varieties. Moreover, product proliferation is not restricted to the supermarket, as companies like Goodyear Tire & Rubber, Gillette, and Eastman Kodak have all recently increased the length of their product lines (Stern 1992). Product line proliferation is also particularly evident in technologically dynamic industries such as personal computers; for example, in 1992 there were over 2,000 different PC models available in the market.

On the demand side, a broad product line can allow a firm to satisfy the needs and wants of heterogeneous consumers more precisely. Consequently, product proliferation can increase the overall demand faced by the firm. On the supply side, a broad product line will increase the firm's per unit production costs when scale economies are present. In addition, a broad product line may lead to added design costs, additional inventory holding costs, and added complexity in the assembly process. Thus, in making its product line decisions, a firm must balance any demand increases due to proliferation with the associated increases in costs. Finally, external strategic considerations can also play an important role in individual firm proliferation strategies. For example, broad product lines in oligopolistic markets can deter entry, thereby allowing an incumbent firm to raise its market prices (e.g., Benson 1990, Levy and Reitzes 1993, Putsis 1997). Similarly, a long product line can be used as a defensive strategy to protect against a proliferating competitor or to enhance firm reputation. Recent related research in marketing has focused on distribution issues (Villas-Boas 1998) and price expectations.

Numerous examples are available from the food industry to illustrate the product-proliferation dilemma. The industry is characterized by a constant effort on the part of
manufacturers to introduce new products into distribution. Many supermarkets offer the public over 10,000 different food items, which represent approximately 20 percent of those available in the channel of distribution. Retailers and wholesalers faced with a continuous deluge of new products have increasingly resorted to requiring manufacturer to sign performance agreements in which they agree to buy all unsold inventory back at the retail price if a product fails. Independent of the fairness of such agreements, the fact remains that the inventory mistakes must be cleansed from the channel.

The scope of proliferation is not limited to off-the-shelf consumer products. An increasing number of new product ideas are being launched as a result of basic research and development. Whereas a few years ago only two products were available to combat high blood pressure, today dozens of alternatives are available from which prescribing physicians may select. In many situations, vendor-based research and development is driving features that ultimately become part of new products. In the automotive industry such items as non-headlight nighttime illumination, elimination of all engine belts required to drive accessories, materials that have form and shape memory that resists denting, and environmentally toxic-free air conditioning are a few examples of technology-based development.

From the manufacturer’s level in the distribution arrangement new-product frenzy is launched. Because the rate of new product introduction is competitively driven, many manufacturers have reduced or eliminated the time traditionally devoted to market testing. Instead, they move directly into launch if the product appears to have the attributes of success. Since all new-product ideas have their champions, it is easy to see how the failure and recall rates could multiply as a result of the “throw it at the market and hope it sticks” philosophy. The sorting out of new-product mistakes is a costly channel management responsibility.

-by V S Rama Rao on April 24, 2008 City.Communities

Profiting from Proliferation

An explosion of new customer segments, sales and service channels, media, and brands is challenging marketers to reinvent themselves so they can simultaneously prioritize opportunities in a more sophisticated way and increase the consistency and coordination of their marketing execution.

The Proliferation of Marketing Channels and Integrated Marketing Strategies—New Challenges and Opportunities.

There’s an explosion of new and growing marketing channels today that is presenting unprecedented challenges – and new opportunities – to companies everywhere. This proliferation of channels affects every company in every industry. Marketers must reinvent themselves and their approach in order to choose the right mix of channels, increasing the consistency and coordination of their marketing execution to succeed. The question is, how do companies effectively respond to these new challenges in an increasingly competitive environment?
According to the Media Awareness Network, studies show that on average we see over 3,000 ads per day – an amazing amount. At the gas pumps, in the movie theatre, in a washroom stall, during sporting events—advertising is impossible to avoid. Companies used to deliver their marketing messages to buyers and consumers through a select handful of media channels; now, there are countless consumer touch points, and in fact, thousands of social media channels, each with a slightly different value proposition. Buyers and consumers faced with a deluge of so much media, can easily tune out advertising messages, and companies must find ways to reach their audience in new- and much more sophisticated—ways.

In the article “The Proliferation Challenge” by David Court, Thomas French and Trond Riiber Knudsen, they write: “The scope of today’s marketing challenge is breathtaking, and proliferation is the reason. Recent advances in technology, information, communications, and distribution have created an explosion of new customer segments, sales and service channels, media, marketing approaches, products and brands. But despite better customer information management and lower communications costs, marketing to consumers and businesses is becoming more complex and difficult every day...the number of communications vehicles will continue to grow dramatically as event marketing, viral marketing, product placement, and other approaches augment traditional media such as television, whose effectiveness is under assault.” They also write that “although proliferation is playing out differently across some sectors, a few common characteristics underlie its challenge for marketers,” namely: (1) Polarizing and fragmenting customer segments; (2) More sales and distribution touch points; (3) Diverse communications vehicles.

How then, do smart marketers respond to such challenges in the face of such an increasingly complex and diverse media and marketing landscape? I believe one answer is a coherent integrated strategy and approach. With a greater integration of brand, growth, sales and marketing strategies, marketers can respond effectively to the challenge of proliferation.

2.2 Total Quality Initiatives

Manufacturing the right way the first time has become a key issue throughout Indian industry. The concept of total quality is exclusively simple-do it right the first time. Embodied in this hard to dispute theorem are a host of practical and philosophical issues. The general concept of total quality is to focus managerial attention to three key concepts of manufacturing: People, process and design.

Human resources in Manufacturing

The concepts of human resources essentially are the same faced through all aspects of channel management, namely, how to attract high quality individuals to a process that has traditionally been viewed as unskilled, low status work. The manufacturing human resource issue is captured in the following perspective of the situation:

Somehow during the post-war years plants and the people who run them came to be regarded as second class. A caste system grew up, separating engineering, where things are
designed, from production, where things are made. Engineers kept their distance from operations people and factories often became dead ends for people who weren't too bright.

The challenge for manufacturing management is to seek ways to involve workers in the process of manufacturing to the extent that they begin to take ownership or responsibility for the outcome of the effort. Such empowerment means that the workforce must be positioned to share in the risk and the rewards related to overall success of basic manufacturing strategies. Realization that meaningful involvement of people would ultimately result in producing products quicker and better was an essential step toward quality attainment.

Manufacturing Process:

The process of manufacturing have changed radically to help achieve total quality. Four related process oriented notions tend to dominate the manufacturing environment:

- Group technology
- Statistical process control
- Zero defects
- Continuous improvement

While these concepts do not fully convey the effort to upgrade manufacturing, they are reflecting of the key points of managerial emphasis.

The basic idea of group technology is to design overall manufacturing work flow in a manner that minimizes material handling distances, eliminates unnecessary or unproductive movement, sequences production steps to reduce required handlings and focuses responsibility concerning who performs selected tasks in the overall process. So that group technology can be fully implemented, traditional first line supervision is eliminated in favor of group or team leadership. Thus, process design to focus group responsibility reflects the integration of equipment lay out, material handling and procedures, and has pinpointed responsibility for high quality performance to the level of the individual worker.

Statistical Process control (SPC) is a technique used to identify and resolve potential or developing product quality problems. It is based on measurement of trends in manufacturing variance. The implementation of SPC permits the elimination of output quality inspection. With the application of SPC comes continued monitoring of manufacturing variance to assume that each step of the process remains within tolerance. When variances begin to track toward tolerance limits, corrective action is taken and verified as part of the basic manufacturing process. As a result of continuous monitoring and correction, the cost and quality of the manufacturing process become highly predictable.

The concept of Zero defects means that there is only one acceptable way of manufacturing- the correct way. The correct way in modern manufacturing is to assume that all aspects of the process will be in tolerance and that total quality is essential. The managerial mind set required to implement a zero defect program is significantly different from one that assumes that goals will not be achieved a given percentage of the time. A Program designed to do 100 percent of the time what is expected will require a far different style of management than one designed to achieve 98 percent compliance. Implementation
of a successful Zero defect process means that the traditional quality department can be eliminated.

Continuous improvement initiatives represent one logical conclusion of the total quality initiative the idea is to introduce a program to seek out and implement ways to achieve zero defects more efficiently. Manufacturing firms are reporting continuous improvement in productivity and controllable plant costs up to 40 percent per year. The key to continuous improvement is to identify and implement innovative work concepts to manage productivity break through.

3. ETHICAL ISSUES IN MARKETING CHANNELS

One ethical issue that arises in connection with distribution is the use of power by a channel leader. How far should a leader go in forcing less powerful channel members to behave in a prescribed manner?
Powerful supermarket chains often demand payments from producers (slotting allowances) to ensure that their products will have shelf space in supermarkets. Many supermarket operators also demand pay-to-stay fees payments to supermarkets by producers to keep their products on the shelf.

At one time the shoe was on the other foot. Powerful consumer product firms could easily force supermarkets to stock their products in quantities larger than the stores wanted. In other words, producers pushed excessive inventories onto supermarkets. They were able to do this because of strong brand loyalty to their products.

The gray market also raises ethical issues. The gray market is unauthorized intermediaries that go around authorized marketing channels by buying in low-price markets and reselling in high-price markets at lower prices than those charged by authorized channel members. Many consumer packaged goods including toothpaste, bath soap, and deodorant are often purchased in the gray market. Other examples include perfumes, cars, tires, cameras, and watches.
In a typical case of gray marketing a broker buys goods from distributors overseas, where wholesale prices are low. The broker then diverts the goods to the United States and undersells domestic distributors. Although not illegal, the gray market reduces sales for authorized intermediaries and disrupts distribution strategies.