15 Managing Marketing Channels and Supply Chains

LEARNING OBJECTIVES

After reading this chapter you should be able to:

LO 15-1 Explain what is meant by a marketing channel of distribution and why intermediaries are needed.

LO 15-2 Distinguish among traditional marketing channels, electronic marketing channels, and different types of vertical marketing systems.

LO 15-3 Describe factors that marketing executives consider when selecting and managing a marketing channel, including legal restrictions.

LO 15-4 Explain what supply chain and logistics management are and how they relate to marketing strategy.

Callaway Golf: Designing and Delivering the Goods for Great Golf

What do Morgan Pressel and Phil Mickelson, two world-class golf professionals, have in common? Both use Callaway Golf equipment, accessories, and apparel when playing their favorite sport.

With annual sales approaching $900 million, Callaway Golf is one of the most recognized and highly regarded companies in the golf industry. With its commitment to continuous product innovation and broad distribution in the United States and more than 100 countries worldwide, Callaway Golf has built a strong reputation for designing and delivering the goods for golfers of all skill levels, both amateur and professional.

Callaway Golf primarily markets its products through more than 15,000 on- and off-course authorized golf retailers and sporting goods retailers, such as Golf Galaxy, Inc., Dick's Sporting Goods, Inc., and PGA Tour Superstores, which sell quality golf products and provide a level of customer service appropriate for the sale of such products. Callaway Golf considers its retailers a valuable marketing asset.

The company also has its own online store (**CallawayGolf.com**), which makes it a full-fledged multichannel marketer, and a successful one as well. Soon after CallawayGolf.com was launched, the chief executive of PGA of America called the store "innovative in that it combines that old legacy relationship with the retail channel with the new innovation of the Web." According to a Marketing Group spokesperson, "Callaway produces in-house a wide-ranging, high volume of original content from instructional videos to interviews with R&D leads and Tour Pros, blog posts and even live streams of Callaway events. This commitment to creating original content helps to give consumers a better feel for the Company and its products when they go to purchase equipment online and at retail."

Today, CallawayGolf.com is a dynamic, engaging and interactive website that constantly delivers new in-depth product information and media, original social content, user-generated content, and e-commerce capabilities. All of this helps consumers become better informed during the purchasing process. Not surprisingly, CallawayGolf.com is listed among the top Internet retailers in the United States.

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Providing Callaway's authorized golf retailers and sporting goods retailers with the right products, at the right place, at the right time, and in the right quantity and condition is the responsibility of the company's supply chain. Callaway sources raw materials for its golf equipment, accessories, and all apparel from around the world. At the same time, Callaway delivers its finished products to company retailers through external shipping companies, such as United Parcel Service (UPS).[1]

This chapter first focuses on marketing channels of distribution and why they are an important component in the marketing mix. It then shows how such channels benefit consumers and the sequence of firms that make up a marketing channel. Finally, it describes factors that influence the choice and management of marketing channels, including channel conflict and cooperation.

The discussion then turns to the significance of supply chains and logistics management. In particular, attention is placed on the necessary alignment between supply chain management and marketing strategy and the trade-offs managers make between total distribution costs and customer service.

NATURE AND IMPORTANCE OF MARKETING CHANNELS

LO 15-1

Explain what is meant by a marketing channel of distribution and why intermediaries are needed.

Reaching prospective buyers, either directly or indirectly, is a prerequisite for successful marketing. At the same time, buyers benefit from distribution systems used by companies.

What Is a Marketing Channel of Distribution?

You see the results of distribution every day. You may have purchased Lay's potato chips at a 7-Eleven convenience store, a book online through Amazon.com, and Levi's jeans at a Kohl's department store. Each of these items was brought to you by a marketing channel of distribution, or simply a **marketing channel**, which consists of individuals and firms involved in the process of making a product or service available for use or consumption by consumers or industrial users.

Marketing channels can be compared to a pipeline through which water flows from a source to a terminus. Marketing channels make possible the flow of products and services from a producer, through intermediaries, to a buyer. Intermediaries go by various names (see **Figure 15–1**) and perform various functions. Some intermediaries purchase items from the seller, store them, and resell them to buyers. For example, Celestial Seasonings produces specialty teas and sells them to food wholesalers. The wholesalers then sell these teas to supermarkets and grocery stores, which, in turn, sell them to consumers. Other intermediaries such as brokers and agents represent sellers but do not actually take title to products—their role is to bring a seller and buyer together. Century 21 real estate agents are examples of this type of intermediary.

TERM	DESCRIPTION
Middleman	Any intermediary between the manufacturer and end-user markets
Agent or broker	Any intermediary with legal authority to act on behalf of the manufacturer
Wholesaler	An intermediary who sells to other intermediaries, usually to retailers; term usually applies to consumer markets
Retailer	An intermediary who sells to consumers
Distributor	An imprecise term, usually used to describe intermediaries who perform a variety of distribution functions, including selling, maintaining inventories, extending credit, and so on; a more common term in business markets but may also be used to refer to wholesalers
Dealer	A more imprecise term than *distributor* that can mean the same as distributor, retailer, wholesaler, and so forth

Figure 15–1 Terms used for marketing intermediaries vary in specificity and use in consumer and business markets.

How Customer Value Is Created by Intermediaries

The importance of intermediaries is made even clearer when we consider the functions they perform and the value they create for buyers.

Important Functions Performed by Intermediaries

Intermediaries make possible the flow of products from producers to ultimate consumers by performing three basic functions (see **Figure 15–2**). Intermediaries perform a *transactional function* when they buy and sell products or services. But an intermediary such as a wholesaler also performs the function of sharing risk with the producer when it stocks merchandise in anticipation of sales. If the stock is unsold for any reason, the intermediary—not the producer—suffers the loss.

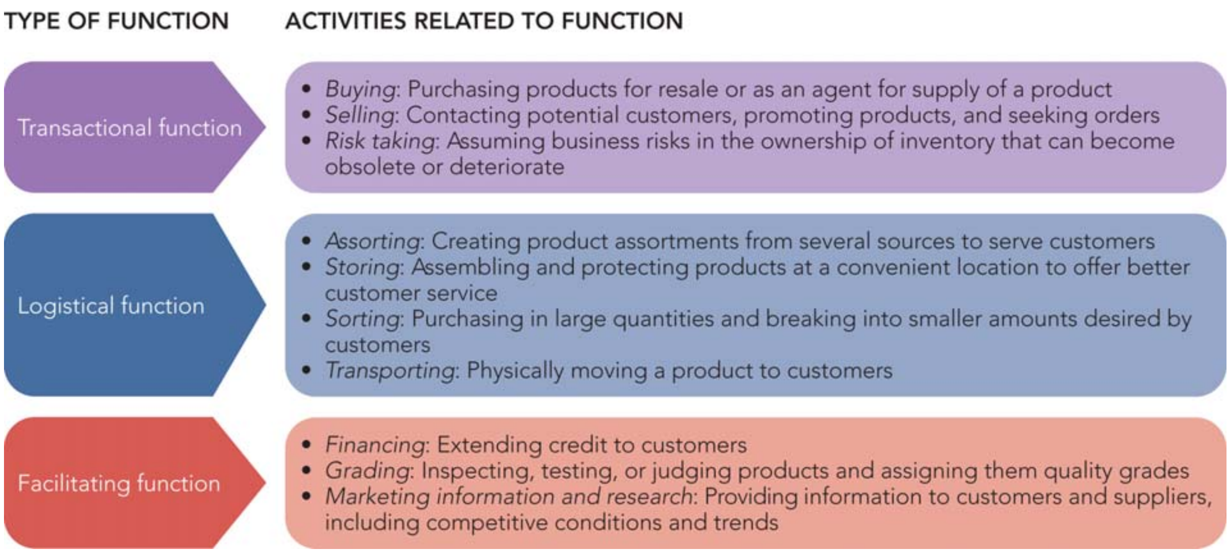

Figure 15–2 Marketing channel intermediaries perform these fundamental functions, each of which consists of different activities.

The logistics of a transaction (described at length later in this chapter) involve the details of preparing and getting a product to buyers. Gathering, sorting, and dispersing products are some of the *logistical functions* of the intermediary—imagine the several books required for a literature course sitting together on one shelf at your college bookstore! Finally, intermediaries perform *facilitating functions* that, by definition, make a transaction easier for buyers. For example, Macy's issues credit cards to consumers so they can buy now and pay later.

All three functions must be performed in a marketing channel, even though each channel member may not participate in all three. Channel members often negotiate which specific functions they will perform and for what price.

Consumer Benefits

Consumers also benefit from intermediaries. Having the products and services you want, when you want them, where you want them, and in the form you want them is the ideal result of marketing channels.

In more specific terms, marketing channels help create value for consumers through the four utilities described in **Chapter 1**: time, place, form, and possession. *Time utility* refers to having a product or service when you want it. For example, FedEx provides next-morning delivery. *Place utility* means having a product or service available where consumers want it, such as having a Chevron gas station located on a long stretch of lonely highway. *Form utility* involves enhancing a product or service to make it more appealing to buyers. Consider the importance of bottlers in the soft-drink industry. Coca-Cola and Pepsi-Cola manufacture the flavor concentrate (cola, lemon-lime) and sell it to bottlers—intermediaries—which then add sweetener and the concentrate to carbonated water and package the beverage in bottles and cans, which are then sold to retailers. *Possession utility* entails efforts by intermediaries to help buyers take possession of a product or service, such as having airline tickets delivered by a travel agency.

learning review

15-1. What is meant by a marketing channel?

15-2. What are the three basic functions performed by intermediaries?

MARKETING CHANNEL STRUCTURE AND ORGANIZATION

LO 15-2

Distinguish among traditional marketing channels, electronic marketing channels, and different types of vertical marketing systems.

A product can take many routes on its journey from a producer to buyers. Marketers continually search for the most efficient route from the many alternatives available. As you'll see, there are some important differences between the marketing channels used for consumer products and business products.

Marketing Channels for Consumer Products and Services

Figure 15–3 shows the four most common marketing channels for consumer products and services. It also shows the number of levels in each marketing channel, as evidenced by the number of intermediaries between a producer and ultimate buyers. As the number of intermediaries between a producer and buyer increases, the channel is viewed as increasing in length. Thus, the producer → wholesaler → retailer → consumer channel is longer than the producer → consumer channel.

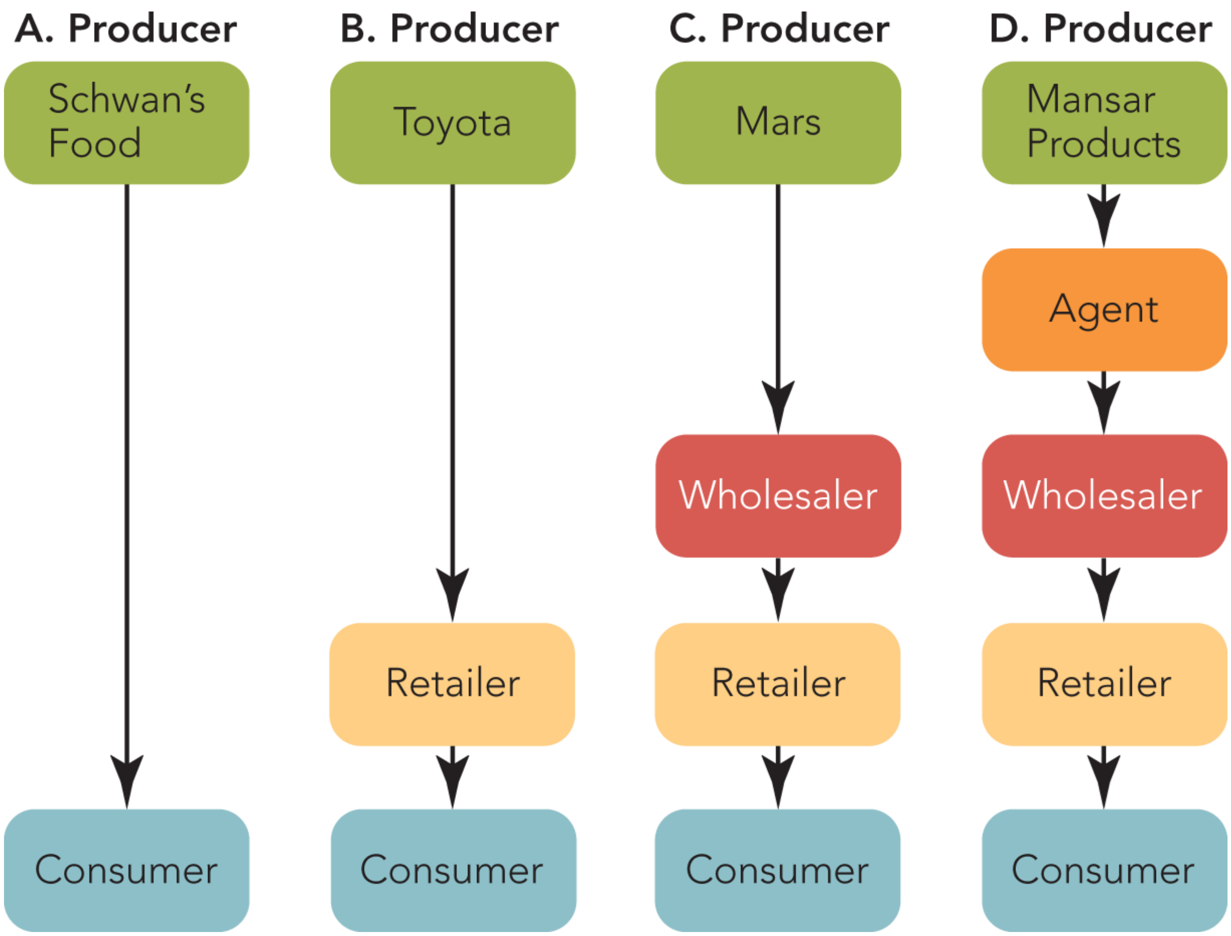

Figure 15–3 Common marketing channels for consumer products and services differ by the kind and number of intermediaries involved.

Direct Channel

Channel A represents a *direct channel* because the producer and the ultimate consumers deal directly with each other. Many products and services are distributed this way. Many insurance companies sell their services using a direct channel and branch sales offices. The Schwan's Food Company of Marshall, Minnesota, the largest direct-to-home provider of frozen foods in the United States, uses route sales representatives who sell from refrigerated trucks. Because there are no intermediaries with a direct channel, the producer performs all channel functions.

Indirect Channel

The remaining three channel forms in **Figure 15–3** are *indirect channels* because intermediaries are inserted between the producer and consumers and perform numerous channel functions. Channel B, with a retailer added, is most common when a retailer is large and can buy in large quantities from a producer or when the cost of inventory makes it too expensive to use a wholesaler. Automobile manufacturers such as Toyota use this channel, and a local car dealer acts as a retailer. Why is there no wholesaler? So many variations exist in the product that it would be impossible for a wholesaler to stock all the models required to satisfy buyers; in addition, the cost of maintaining an inventory would be too high. However, large retailers such as Target, 7-Eleven, Staples, Safeway, and Home Depot buy in sufficient quantities to make it cost effective for a producer to deal with only a retail intermediary.

What kind of marketing channel does IBM use for its Watson computer—an artificially intelligent computer system capable of answering questions in natural language? Read the text to find out.
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Adding a wholesaler in Channel C is most common for low-cost, low-unit value items that are frequently purchased by consumers, such as candy, confectionary items, and magazines. For example, Mars sells case quantities of its line of candies to wholesalers, who then break down (sort) the cases so that individual retailers can order in boxes or much smaller quantities.

Channel D, the most indirect channel, is employed when there are many small manufacturers and many small retailers; in this type of channel, an agent is used to help coordinate a large supply of the product. Mansar Products, Ltd. is a Belgian producer of specialty jewelry that uses agents to sell to wholesalers in the United States, who then sell to many small independent jewelry retailers.

Marketing Channels for Business Products and Services

The four most common channels for business products and services are shown in **Figure 15–4**. In contrast with channels used for consumer products, business channels typically are shorter and rely on one intermediary or none at all because business users are fewer in number, tend to be more concentrated geographically, and buy in larger quantities.

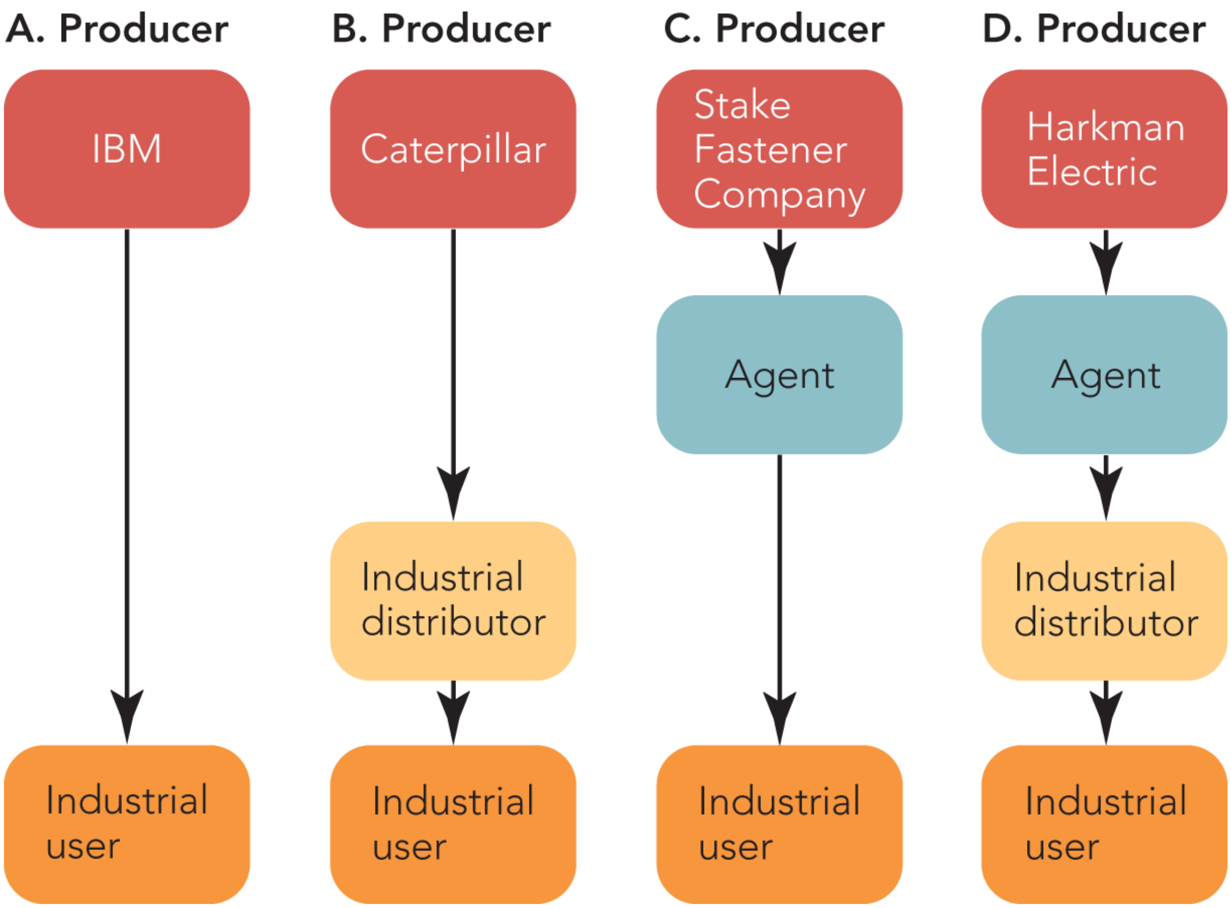


Figure 15–4 Common marketing channels for business products and services differ by the kind and number of intermediaries involved.

Direct Channel

Channel A in **Figure 15–4**, represented by IBM's large, mainframe computer business, is a direct channel. Firms using this channel maintain their own salesforce and perform all channel functions. This channel is employed when buyers are large and well defined, the sales effort requires extensive negotiations, and the products are of high unit value and require hands-on expertise in terms of installation or use. Not surprisingly, IBM's Watson supercomputer, priced at $3 million, is sold and delivered directly to buyers.

Indirect Channel

Channels B, C, and D in **Figure 15–4** are indirect channels with one or more intermediaries between the producer and the industrial user. In Channel B, an industrial distributor performs a variety of marketing channel functions, including selling, stocking, delivering a full product assortment, and financing. In many ways, industrial distributors are like wholesalers in consumer channels. Caterpillar uses industrial distributors to sell its construction and mining equipment in over 180 countries. In addition to selling, Caterpillar distributors stock 40,000 to 50,000 parts and service equipment using highly trained technicians.

Channel C introduces a second intermediary, an agent, who serves primarily as the independent selling arm of producers and represents a producer to industrial users. For example, Stake Fastener Company, a producer of industrial fasteners, has an agent call on industrial users rather than employing its own salesforce.

Channel D is the longest channel and includes both agents and industrial distributors. For instance, Harkman Electric, a producer of electric products, uses agents to call on electrical distributors who sell to industrial users.

Internet Marketing Channels

These common marketing channels for consumer and business products and services are not the only routes to the marketplace. *Internet marketing channels* also make products and services available for consumption or use by consumers or organizational buyers. A unique feature of these channels is that they combine electronic and traditional intermediaries to create time, place, form, and possession utility for buyers.

Figure 15–5 shows the Internet marketing channels for books (Amazon.com), automobiles (Autobytel.com), reservation services (Orbitz.com), and personal computers (Dell.com). Are you surprised that they look a lot like common consumer product marketing channels? An important reason for the similarity resides in the channel functions detailed in **Figure 15–2**. Electronic intermediaries can and do perform transactional and facilitating functions effectively and at a relatively lower cost than traditional intermediaries because of efficiencies made possible by Internet technology. But electronic intermediaries are incapable of performing elements of the logistical function, particularly for products such as books and automobiles. This function remains with traditional intermediaries or with the producer, as is evident with Dell Inc. and its direct channel.

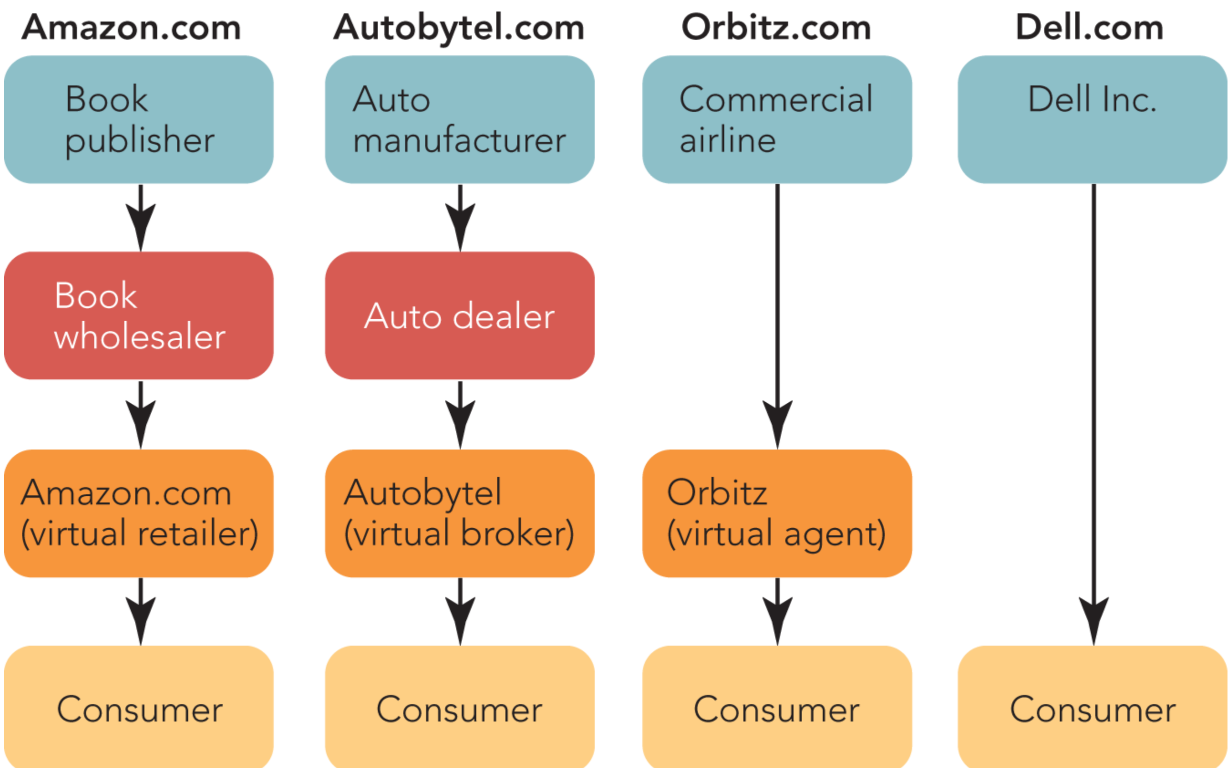
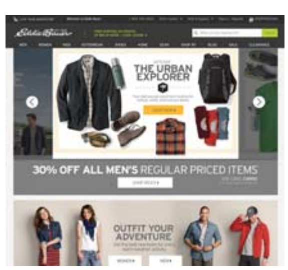


Figure 15–5 Consumer Internet marketing channels look much like those for consumer products and services. Read the text to learn why.

Many services can be distributed through electronic marketing channels, such as car rental reservations marketed by Alamo.com, financial securities by Schwab.com, and insurance by MetLife.com. However, many other services, such as health care and auto repair, still involve traditional intermediaries.



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Eddie Bauer successfully engages in multichannel marketing through its 370 retail and outlet stores, its website, and its catalog.

Left: © Bonnie Kamin/PhotoEdit, Inc.; Middle: Source: Eddie Bauer, LLC; Right: © Mike Hruby

Eddie Bauer

www.eddiebauer.com

Direct and Multichannel Marketing

Many firms also use direct and multichannel marketing to reach buyers. *Direct marketing channels* allow consumers to buy products by interacting with various advertising media without a face-to-face meeting with a salesperson. Direct marketing channels include mail-order selling, direct-mail sales, catalog sales, telemarketing, interactive media, and televised home shopping (the Home Shopping Network). Some firms sell products almost entirely through direct marketing. These firms include L.L.Bean (apparel) and Newegg.com (consumer electronics). Marketers such as Nestlé, in addition to using traditional channels composed of wholesalers and retailers, also employ direct marketing through catalogs and telemarketing to reach more buyers.

Multichannel marketing, sometimes called *omnichannel marketing*, is the *blending* of different communication and delivery channels that are *mutually reinforcing* in attracting, retaining, and building relationships with consumers who shop and buy in traditional intermediaries and online. Multichannel marketing seeks to integrate a firm's electronic marketing and delivery channels. At Eddie Bauer, for example, every effort is made to make the apparel shopping and purchase experience for its customers the same across its retail store, catalog, and website channels. According to an Eddie Bauer marketing manager, "We don't distinguish between channels because it's all Eddie Bauer to our customers."[2]

Multichannel marketing also can leverage the value-adding capabilities of different channels. For example, retail stores leverage their physical presence by allowing customers to pick up their online orders at a nearby store or return or exchange nonstore purchases if they wish. Catalogs can serve as shopping tools for online purchasing, as they do for store purchasing. Websites can help consumers do their homework before visiting a store. Staples has leveraged its store, catalog, and website channels with impressive results. Staples is the third largest Internet retailer in the United States behind Amazon and Apple.[3]

Dual Distribution and Strategic Channel Alliances

In some situations, producers use **dual distribution** , an arrangement whereby a firm reaches different buyers by employing two or more different types of channels for the same basic product. For example, GE sells its large appliances directly to home and apartment builders but uses retail stores, including Lowe's home centers, to sell to consumers. In some instances, firms pair multiple channels with a multibrand strategy (see **Chapter 10**). This is done to minimize cannibalization of the firm's family brand and differentiate the channels. For example, Hallmark sells its Hallmark greeting cards through Hallmark stores and select department stores and its Ambassador brand of cards through discount and drugstore chains.

VIDEO 15-1

Honey Nut Cheerios Ad

kerin.tv/13e/v15-1

An innovation in marketing channels is the use of *strategic channel alliances*, whereby one firm's marketing channel is used to sell another firm's products. Strategic alliances are popular in global marketing, where the creation of marketing channel relationships is expensive and time-consuming. For example, General Mills and Nestlé have an extensive alliance that spans about 140 international markets from Mexico to China. Read the Marketing Matters box so you won't be surprised when you are served Nestlé (not General Mills) Cheerios when traveling outside North America.[4]

Marketing **Matters**

customer value

Nestlé and General Mills—Cereal Partners Worldwide

Can you say Nestlé Cheerios *miel amandes*? Millions in France start their day with this European equivalent of General Mills's Honey Nut Cheerios, made possible by Cereal Partners Worldwide (CPW). CPW is a strategic alliance designed from the start to be a global business. It combines the cereal manufacturing and marketing capability of U.S.-based General Mills with the worldwide distribution clout of Swiss-based Nestlé. The photo shows Nestlé's Trix cereal (not General Mills) sold in China.

From its headquarters in Switzerland, CPW first launched General Mills cereals under the Nestlé label in France, the United Kingdom, Spain, and Portugal in 1991. Today, CPW competes in more than 140 international markets.

The General Mills–Nestlé strategic channel alliance also increased the ready-to-eat cereal worldwide market share of these companies, which are already rated as the two best-managed firms in the world. CPW currently accounts for more than 10 percent of the nearly $30 billion worldwide hot- and cold-cereal market, with more than $4 billion in annual revenue.

© picture alliance/Daniel Kalker/Newscom

Vertical Marketing Systems

The traditional marketing channels described so far represent a loosely knit network of independent producers and intermediaries brought together to distribute products and services. However, other channel arrangements exist for the purpose of improving efficiency in performing channel functions and achieving greater marketing effectiveness. These arrangements are called vertical marketing systems. **Vertical marketing systems** are professionally managed and centrally coordinated marketing channels designed to achieve channel economies and maximum marketing impact.[5] **Figure 15–6** depicts the three major types of vertical marketing systems: corporate, contractual, and administered.

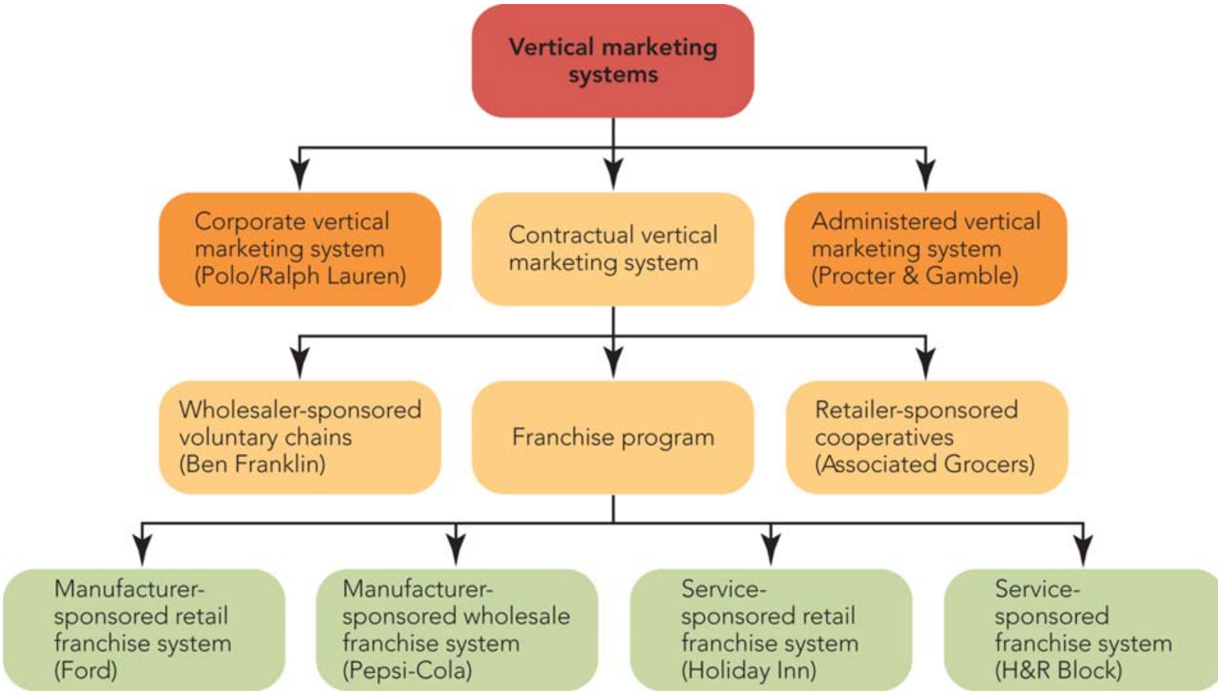


Figure 15–6 There are three major types of vertical marketing systems—corporate, contractual, and administered. Contractual systems are the most popular for reasons described in the text.

Corporate Systems

The combination of successive stages of production and distribution under a single ownership is a *corporate vertical marketing system*. For example, a producer might own the intermediary at the next level down in the channel. This practice, called *forward integration*, is exemplified by Ralph Lauren, which manufactures clothing and also owns apparel shops. Other examples of forward integration include Goodyear, Apple, and Sherwin-Williams. Alternatively, a retailer might own a manufacturing operation, a practice called *backward integration*. For example, Kroger supermarkets operate manufacturing facilities that produce everything from aspirin to cottage cheese for sale under the Kroger label. Tiffany & Co., the exclusive jewelry retailer, manufactures about half of the fine jewelry items for sale through its over 250 specialty stores and boutiques worldwide.

Companies seeking to reduce distribution costs and gain greater control over supply sources or resale of their products pursue forward and backward integration. However, both types of integration increase a company’s capital investment and fixed costs. For this reason, many companies favor contractual vertical marketing systems to achieve channel efficiencies and marketing effectiveness.

Contractual Systems

Under a *contractual vertical marketing system*, independent production and distribution firms integrate their efforts on a contractual basis to obtain greater functional economies and marketing impact than they could achieve alone. Contractual systems are the most popular among the three types of vertical marketing systems.

Three variations of contractual systems exist. *Wholesaler-sponsored voluntary chains* involve a wholesaler that develops a contractual relationship with small, independent retailers to standardize and coordinate buying practices, merchandising programs, and inventory management efforts. With the organization of a large number of independent retailers, economies of scale and volume discounts can be achieved to compete with chain stores. IGA and Ben Franklin variety and craft stores represent wholesaler-sponsored voluntary chains. *Retailer-sponsored cooperatives* exist when small, independent retailers form an organization that operates a wholesale facility cooperatively. Member retailers then concentrate their buying power through the wholesaler and plan collaborative promotional and pricing activities. Examples of retailer-sponsored cooperatives include Associated Grocers and Ace Hardware.

The most visible variation of contractual systems is franchising. *Franchising* is a contractual arrangement between a parent company (a franchisor) and an individual or firm (a franchisee) that allows the franchisee to operate a certain type of business under an established name and according to specific rules.

Four types of franchise arrangements are most popular. *Manufacturer-sponsored retail franchise systems* are prominent in the automobile industry, where a manufacturer such as Ford licenses dealers to sell its cars subject to various sales and service conditions.

Manufacturer-sponsored wholesale franchise systems exist in the soft-drink industry. For example, Pepsi-Cola licenses wholesalers (bottlers) that purchase concentrate from Pepsi-Cola and then carbonate, bottle, promote, and distribute its products to retailers and restaurants. *Service-sponsored retail franchise systems* are used by firms that have designed a unique approach for performing a service and wish to profit by selling the franchise to others. Holiday Inn, Avis, and McDonald's represent this type of franchising approach. *Service-sponsored franchise systems* exist when franchisors license individuals or firms to dispense a service under a trade name and according to specific guidelines. Examples include Snelling and Snelling, Inc. employment services and H&R Block tax services.

Administered Systems

In comparison, *administered vertical marketing systems* achieve coordination at successive stages of production and distribution by the size and influence of one channel member rather than through ownership. Procter & Gamble, given its broad product assortment ranging from disposable diapers to detergents, is able to obtain cooperation from supermarkets in displaying, promoting, and pricing its products. Walmart obtains cooperation from manufacturers in terms of product specifications, price levels, and promotional support due to its position as the world's largest retailer.

learning review

15-3. What is the difference between a direct and an indirect channel?

15-4. Why are channels for business products typically shorter than channels for consumer products?

15-5. What is the principal distinction between a corporate vertical marketing system and an administered vertical marketing system?

MARKETING CHANNEL CHOICE AND MANAGEMENT

LO 15-3

Describe factors that marketing executives consider when selecting and managing a marketing channel, including legal restrictions.

Marketing channels not only link a producer to its buyers but also provide the means through which a firm implements various elements of its marketing strategy. Therefore, choosing a marketing channel is a critical decision.

Factors Affecting Channel Choice and Management

Marketing executives consider three questions when choosing a marketing channel and intermediaries:

1. Which channel and intermediaries will provide the best coverage of the target market?
2. Which channel and intermediaries will best satisfy the buying requirements of the target market?
3. Which channel and intermediaries will be the most profitable?

Target Market Coverage

Achieving the best coverage of the target market requires attention to the *density*—that is, the number of stores in a geographical area—and type of intermediaries to be used at the retail level of distribution. Three degrees of distribution density exist: intensive, exclusive, and selective.

Intensive distribution means that a firm tries to place its products and services in as many outlets as possible. Intensive distribution is usually chosen for convenience products or services such as candy, fast food, newspapers, and soft drinks. For example, Coca-Cola's retail distribution objective is to place its products "within an arm's reach of desire." Cash, yes cash, is distributed intensively by Visa. It operates over 1.4 million automated teller machines in more than 200 countries.

Exclusive distribution is the extreme opposite of intensive distribution because only one retailer in a specific geographical area carries the firm's products. Exclusive distribution is typically chosen for specialty products or services, such as some women's fragrances and men's and women's apparel and accessories. Gucci, one of the world's leading luxury products companies, uses exclusive distribution in the marketing of its Yves Saint Laurent, Sergio Rossi, Boucheron, Opium, and Gucci brands.

Retailers and industrial distributors prefer exclusive distribution for two reasons. First, it limits head-to-head competition for an identical product. Second, it provides a point of difference for a retailer or distributor. For instance, luxury retailer Saks Inc. seeks exclusive product lines for its stores. According to the company CEO, "It's incumbent on us not to be just a place where you can buy the big brands. Those brands are still critical—the Chanels, the Pradas, the Guccis—but even with those brands, we need to find things unique to us."[6]

Selective distribution lies between these two extremes and means that a firm selects a few retailers in a specific geographical area to carry its products. Selective distribution weds some of the market coverage benefits of intensive distribution to the control over resale evident with exclusive distribution. For example, Dell Inc. chose selective distribution when it decided to sell its products through U.S. retailers along with its direct channel.[7] According to Michael Dell, the company CEO, "There were plenty of retailers who said, 'sell through us,' but we didn't want to show up everywhere." The company now sells a limited range of its products through Walmart, Sam's Club, Best Buy, and Staples. Dell's decision was consistent with current trends. Today, selective distribution is the most common form of distribution intensity.

Buyer Requirements

A second consideration in channel choice is gaining access to channels and intermediaries that satisfy at least some of the interests buyers might want fulfilled when they purchase a firm's products or services. These interests fall into four broad categories: (1) information, (2) convenience, (3) variety, and (4) pre- or postsale services. Each relates to customer experience.

Information is an important requirement when buyers have limited knowledge or desire specific data about a product or service. Properly chosen intermediaries communicate with buyers through in-store displays, demonstrations, and personal selling. Apple has opened over 400 retail outlets staffed with highly trained personnel to communicate how its products can better satisfy each customer's needs.

Which buying requirements are satisfied by Jiffy Lube? Read the text to find out.

© David McNew/Getty Images

Convenience has multiple meanings for buyers, such as proximity or driving time to a retail outlet. For example, 7-Eleven stores, with more than 50,000 outlets worldwide, many of which are open 24 hours a day, satisfy this interest for buyers. Candy and snack-food firms benefit by gaining display space in these stores. For other consumers, convenience means a minimum of time and hassle. Jiffy Lube, which promises to change engine oil and filters quickly, appeals to this aspect of convenience. For those who shop on the Internet, convenience means that websites must be easy to locate and navigate, and image downloads must be fast. A commonly held view among website developers is the “eight second rule”: Consumers will abandon their efforts to enter or navigate a website if download time exceeds eight seconds.[8]

Variety reflects buyers’ interest in having numerous competing and complementary items from which to choose. Variety is evident in the breadth and depth of products and brands carried by intermediaries, which enhances their attraction to buyers. Thus, manufacturers of pet food and supplies seek distribution through pet superstores such as Petco and PetSmart, which offer a wide array of pet products and services.

Pre- or postsale services provided by intermediaries are an important buying requirement for products such as large household appliances that require delivery, installation, and credit. Therefore, Whirlpool seeks dealers that provide such services.

Profitability

The third consideration in choosing a channel is profitability, which is determined by the margins earned (revenue minus cost) for each channel member and for the channel as a whole. Channel cost is the critical dimension of profitability.

These costs include distribution, advertising, and selling expenses associated with different types of marketing channels. The extent to which channel members share these costs determines the margins received by each member and by the channel as a whole.

Companies routinely monitor the performance of their marketing channels. Read the Applying Marketing Metrics box to see how Charlesburg Furniture views the sales and profit performance of its marketing channels.

Applying **Marketing Metrics**

Channel Sales and Profit at Charlesburg Furniture

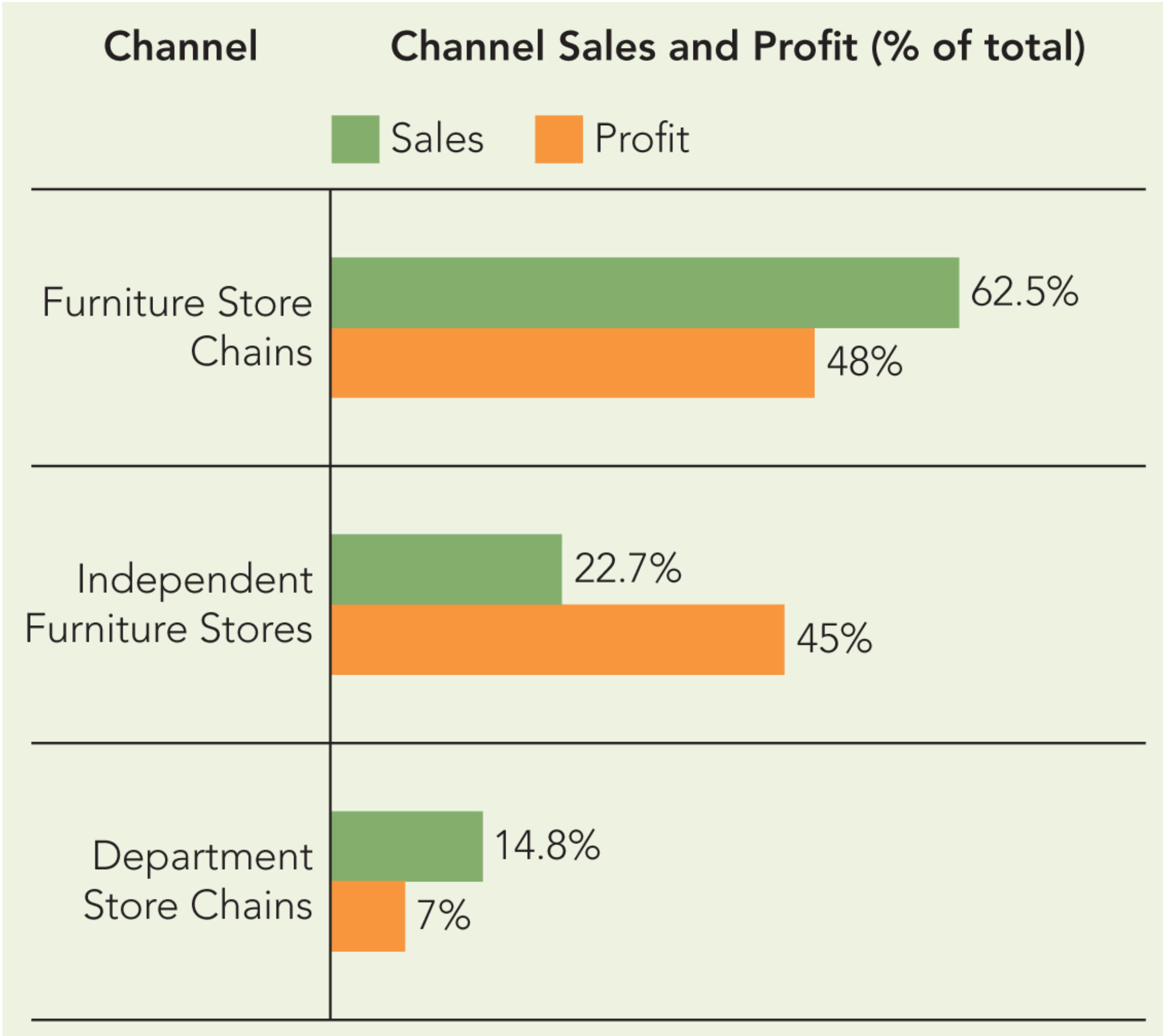
Charlesburg Furniture is one of 1,000 wood furniture manufacturers in the United States. The company sells its furniture through furniture store chains, independent furniture stores, and department store chains, mostly in the southern United States. The company has traditionally allocated its marketing funds for cooperative advertising, in-store displays, and retail sales support on the basis of dollar sales by channel.

Your Challenge

As the vice president of sales and marketing at Charlesburg Furniture, you have been asked to review the company's sales and profit in its three channels and recommend a course of action. The question: Should Charlesburg Furniture continue to allocate its marketing funds on the basis of channel dollar sales or profit?

Your Findings

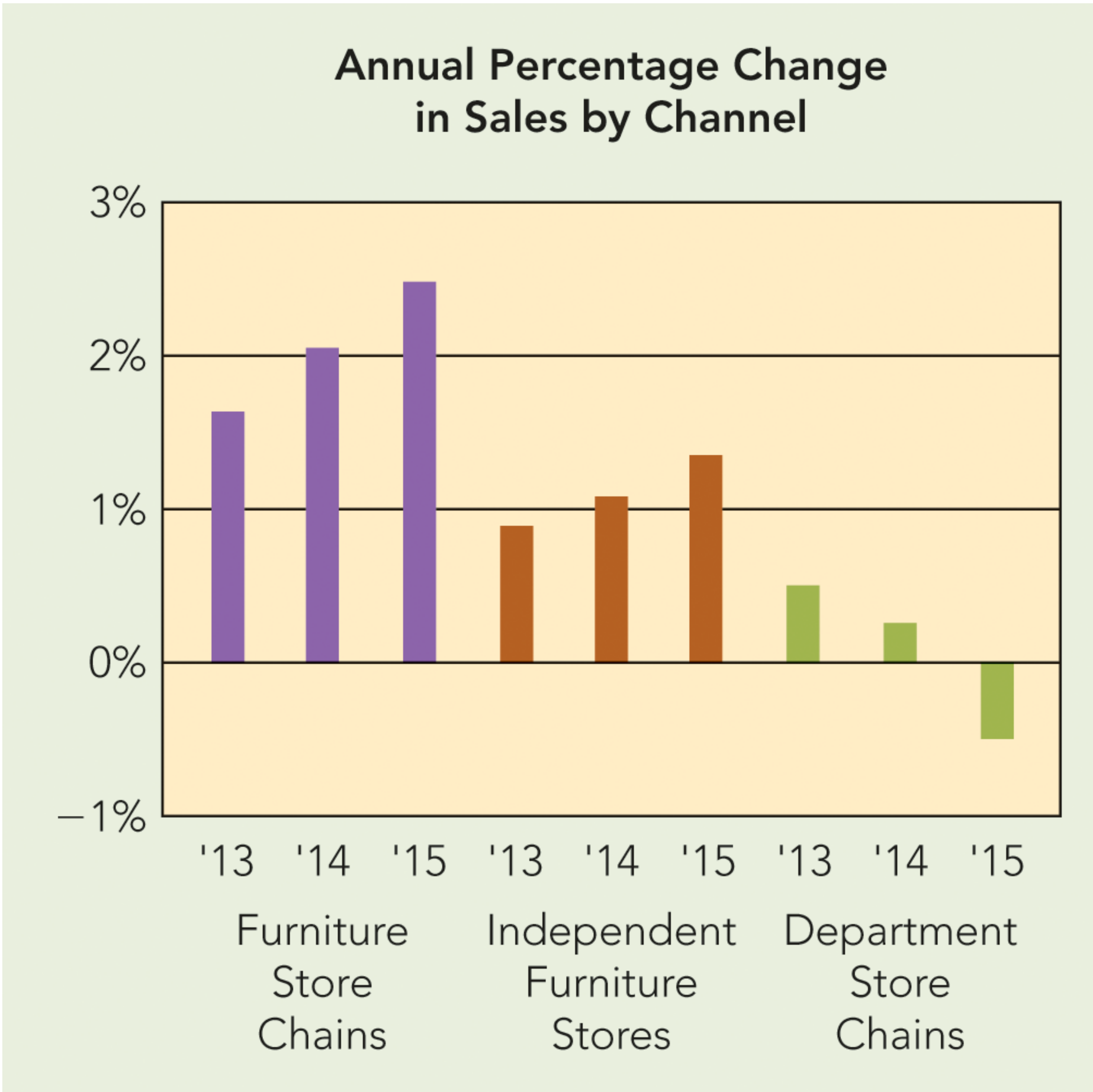
Charlesburg Furniture tracks the sales and profit from each channel (and individual customer) and the three-year trend of sales by channel on its marketing dashboard. This information is displayed in the marketing dashboards below.



Several findings stand out. Furniture store chains and independent furniture stores account for 85.2 percent of Charlesburg Furniture sales and 93 percent of company profit. These two channels also evidence growth as measured by annual percentage change in sales. By comparison, the annual percentage sales growth of department store chains has declined, recording negative growth in 2015. This channel accounts for 14.8 percent of company sales and 7 percent of company profit.

Your Action

Charlesburg Furniture should consider abandoning the practice of allocating marketing funds solely on the basis of channel sales volume. The importance of independent furniture stores to Charlesburg's profitability warrants further spending, particularly given this channel's favorable sales trend. Doubling the percentage allocation for marketing funds for this channel may be too extreme, however. Charlesburg Furniture might also consider the longer term role of department store chains as a marketing channel.



Managing Channel Relationships: Conflict and Cooperation

Unfortunately, because channels consist of independent individuals and firms, there is always the potential for disagreements concerning who performs which channel functions, how profits are allocated, which products and services will be provided by whom, and who makes critical channel-related decisions. These channel conflicts necessitate measures for dealing with them.

Sources of Conflict in Marketing Channels

Channel conflict arises when one channel member believes another channel member is engaged in behavior that prevents it from achieving its goals. Two types of conflict occur in marketing channels: vertical conflict and horizontal conflict.

Vertical conflict occurs between different levels in a marketing channel—for example, between a manufacturer and a wholesaler or retailer or between a wholesaler and a retailer. Three sources of vertical conflict are most common.[9] First, conflict arises when a channel member bypasses another member and sells or buys products direct, a practice called **disintermediation**. For example, conflict occurred when American Airlines decided to terminate its relationship with Orbitz and Expedia, two online ticketing and travel sites, and sell directly through AA Direct Connect. Second, conflict occurs due to disagreements over how profit margins are distributed among channel members. This happened when Amazon and the Hachette Book Group, the third-largest trade book and educational publisher, engaged in a seven-month dispute about how e-book revenue should be divided between the two companies. A third conflict situation arises when manufacturers believe wholesalers or retailers are not giving their products adequate attention. For example, Nike stopped shipping popular sneakers such as Nike Shox NZ to Foot Locker in retaliation for the retailer’s decision to give more shelf space to shoes costing under $120.

Horizontal conflict occurs between intermediaries at the same level in a marketing channel, such as between two or more retailers (Target and Kmart) or two or more wholesalers that handle the same manufacturer’s brands. Two sources of horizontal conflict are common.[10] First, horizontal conflict arises when a manufacturer increases its distribution coverage in a geographical area. For example, a franchised Cadillac dealer in Chicago might complain to General Motors that another franchised Cadillac dealer has located too close to its dealership. Second, dual distribution causes conflict when

Channel conflict is sometimes visible to consumers. Read the text to learn what type of channel conflict has antagonized this independent Goodyear tire dealer.

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different types of retailers carry the same brands. For instance, independent Goodyear tire dealers became irate when Goodyear Tire Company decided to sell its brands through Sears, Walmart, and Sam's Club. Many switched to competing tire makers.

Securing Cooperation in Marketing Channels

Conflict can have destructive effects on the workings of a marketing channel so it is necessary to secure cooperation among channel members. One means is through a *channel captain*, a channel member that coordinates, directs, and supports other channel members. Channel captains can be producers, wholesalers, or retailers. P&G assumes this role because it has a strong consumer following in brands such as Crest, Tide, and Pampers. Therefore, it can set policies or terms that supermarkets will follow. McKesson, a pharmaceutical drug wholesaler, is a channel captain because it coordinates and supports the product flow from numerous small drug manufacturers to drugstores and hospitals nationwide. Walmart is a retail channel captain because of its strong consumer image, number of outlets, and purchasing volume.

A firm becomes a channel captain because it is the channel member with the ability to influence the behavior of other members. Influence can take four forms.

First, economic influence arises from the ability of a firm to *reward* other members given its strong financial position or customer franchise. Microsoft Corporation and Walmart have such influence. *Expertise* is a second source of influence. For example, American Hospital Supply helps its customers (hospitals) manage inventory and streamline order processing for hundreds of medical supplies. Third, *identification* with a particular channel member can create influence for that channel member. For instance, retailers may compete to carry the Ralph Lauren line, or clothing manufacturers may compete to be carried by Neiman Marcus, Nordstrom, or Bloomingdale's. In both instances, the desire to be identified with a channel member gives that firm influence over others. Finally, influence can arise from the *legitimate right* of one channel member to direct the behavior of other members. This situation is likely to occur in contractual vertical marketing systems where a franchisor can legitimately direct how a franchisee behaves.

Legal Considerations

Conflict in marketing channels is typically resolved through negotiation or the exercise of influence by channel members. Sometimes conflict produces legal action. Therefore, knowledge of legal restrictions affecting channel strategies and practices is important. Some restrictions were described in **Chapter 14**, namely vertical price fixing and price discrimination. However, other legal considerations are unique to marketing channels.

In general, suppliers can select whomever they want as channel intermediaries and may refuse to deal with whomever they choose. However, the Federal Trade Commission and the Justice Department monitor channel practices that restrain competition, create monopolies, or otherwise represent unfair methods of competition under the Sherman Act (1890) and the Clayton Act (1914). Six channel practices have received the most attention (see **Figure 15–7**).

Dual distribution, although not illegal, can be viewed as anticompetitive in some situations. The most common situation arises when a manufacturer distributes through its own vertically integrated channel in competition with independent wholesalers and retailers that also sell its products. If the manufacturer's behavior is viewed as an attempt to lessen competition by eliminating wholesalers or retailers, then such action would violate both the Sherman and Clayton Acts.

Vertical integration is viewed in a similar light. Although not illegal, this practice is sometimes subject to legal action under the Clayton Act if it has the potential to lessen competition or foster monopoly.

The Clayton Act specifically prohibits exclusive dealing and tying arrangements when they lessen competition or create monopolies. *Exclusive dealing* exists when a supplier requires channel members to sell only its products or restricts distributors from selling directly competitive products. *Tying arrangements* occur when a supplier requires a distributor purchasing some products to buy others from the supplier. These arrangements often arise in franchising. They are illegal if the tied products could be purchased at fair market values from other suppliers at desired quality standards of the