**CHAPTER EIGHT: DISTRIBUTION**

**8.1 Meaning and Importance of Distribution**

Distribution channel is *a set of interdependent organizations involved in the process of making a product or service available for use or consumption by the consumer or business user*.

 A marketing channel performs the work of moving goods from producers to consumers. Channel members add value by bridging *the time, place, and possession gaps that separate goods and services from those who need or want them.* Members of the marketing channel perform a number of key functions.

**Importance of Distribution Channel**

* ***Information*:** gathering information about potential and current customers (what are their needs, what are they buying), competitors, the current economics of the marketing channel, new entrants, new technology and other actors and forces in the marketing environment.
* ***Promotion:*** develop and disseminate persuasive communications (about the performance of the product, special offers) to stimulate purchasing.
* ***Negotiation*:** reach agreements in price and other terms so that transfer of ownership or possession can be affected.
* ***Order processing*:** place order with manufacturers.
* ***Financing:*** acquire funds to finance inventories at different levels in the marketing channel.
* ***Risk taking:*** assume risks connected with carrying out channel work.
* ***Warehousing:*** provide for the successive storage and movement of physical products.
* ***Customization:*** shaping and fitting the offer to the buyer’s needs including manufacturing, grading, assembling and packaging products (e.g. fish processors) so that customers can purchase in a customized manner.

Some functions (e.g. physical title, promotion) takes place in the forward flow of activity from the company to the customer; some functions (such as, payment, ordering) occur in the backward flow of activity from customers to the company; and some functions (information, negotiation, financing and risk taking) occur in both directions.

**8.2 Channel levels**

*A layer of intermediaries that perform some work in bringing the product and its ownership closer to the final buyer constitutes a channel level.* Since the producer and the final customer both perform some work, they are part of every channel. The number of intermediary levels indicates the length of channel. The following figures show distribution channels of different lengths for both consumer and business market.

  **Fig-8.1 Consumer marketing channel**

Manufacturer

Consumer

Consumer

Retailer

Manufacturer

Manufacturer

Wholesaler

Retailer

Consumer

Manufacturer

Jobber

Retailer

Consumer

Wholesaler

**Fig-8.2 Business marketing channel**

Manufacturer

Industrial customer

Manufacturer

Industrial customer

Manufacturer

Business distributor

Manufacturer’s representative or sales branch

Industrial customer

Manufacturer

Manufacturer’s representative or sales branch

Business distributor

Industrial customer

From the figure above the first channel called *direct marketing channel* for both consumer and business marketing channel, have no intermediary levels, the manufacturers sell directly to users. The remaining channels for both markets, called *indirect marketing channels*, containing one or more intermediaries.

From producers’ point of view, a greater number of levels mean less control and greater channel complexity; moreover, several types of flows connect all the institutions in the channel. These include the physical flow of products, the flow of ownership, the payment flow, the information flow, and the promotion flow. These flows can make even channels with only one or a few levels very complex.

**8.3 Factors influencing Channel Decision**

A company has to take into account a number of variables that influence channel design decisions. *Market variables, Product variables, Company variables and Intermediary* variables can determine the channel structure.

**A. Market variables:** Market variables are the most fundamental variables affecting the channel structure. There are four basic subcategories of market variables.

* ***Market size:*** refers to the number of customers making up a market. The general rule about market size relative to channel structure is: if the market is large the use of intermediary is more likely to be needed.
* ***Market density:*** refers to the number of buyers located within Km2 or Mile2. The general rule is the less dense the market (buyers are widely scattered), the more likely it is that intermediaries.
* ***Geographic location of the market:*** refers to the geographical size of markets and their physical location and distance from the producer. The general rule is the greater the distance between the producer and its markets, the higher the probability that the use of intermediaries will be.
* ***Market behavior:*** refers to the types of buying behavior – that is how, when and where customers buy and who does the buying.

**B. Product variables include:**

* ***Unit value of the product:*** refers to the price per unit of the product. The lower the unit value of the product, the longer the channel should be.
* ***Perishability:*** products subject to rapid physical deterioration or spoilage (such as fish) are considered to be highly perishable. When products are highly perishable, channel structure should be shorter to provide for rapid delivery to producer to consumers.
* ***Technicality:*** refers to the nature of the product (technical versus non-technical). To the industrial market, a highly technical product such as machinery will be distributed through a direct channel since the manufacturer provides information about the product’s technical features, advices and after-sale services to customers.
* ***Newness:*** in the introductory stage, a shorter channel is generally viewed as an advantage for gaining product acceptance.
* ***Degree of standardization:*** refers to whether products are uniform (standardized) or custom-made (made according to customer order). Custom-made products go directly from producer to users; but as products become more standardized the channel will be long.
* ***Bulk and weight:*** heavy and bulky products have very large handling and shipping costs relative to their value, so that the channel should be as short as possible – usually direct from producer to user.

**C. Company variables include:**

* ***Financial capacity:*** in order to directly to consumers, a company needs its own sales force and support services like retail stores, warehousing and order processing capabilities. The greater the capital available to a company, the lower its dependence on intermediaries.
* ***Managerial expertise (capabilities and skills):*** when a company lacks the managerial expertise to perform distribution tasks, its dependence on intermediaries will be high. However, as the company gains experience and managerial skills, it may be feasible to change the structure to reduce the amount of reliance on intermediaries.
* ***Objectives and strategies:*** if the company has strong desire to control the channel, it may use direct or short channel.

**D. Intermediary variables**

* ***Availability:*** if there are sufficient numbers of middlemen, longer channel may be used.
* ***Attitude of middlemen:*** if the attitude of middlemen towards the product of the company is poor, it may try to change the negative attitude or use a direct selling.
* ***Cost:*** if the cost of using intermediaries is too high as compared to the service performed, the channel structure is likely to minimize the use of intermediaries.
	1. **Channel Design Decisions**

In designing marketing channels, manufacturers *have to decide what is ideal and what is practical*. A new firm with limited capital usually starts by selling in a limited market and it usually uses existing intermediaries. Deciding on the best channels might not be a problem. The problem might simply be how to convince one or a few good intermediaries to handle the line.

If the new firm is successful, it might branch out to new market through the existing intermediaries. In smaller markets, the firm might sell directly to retailers; in large markets, it might sell through distributors. In one part of the country, it might grant exclusive franchise; in another, it might sell through all available outlets. In one country it might use international sales agents; in another, it might partner with local firm. In short, the manufacturer’s channel systems often evolve to meet market opportunities and conditions.

Designing a channel system calls for *analyzing customer needs, establishing channel objectives and identifying and evaluating the major channel alternatives*.

**8.4.1 Analyzing customer service needs**

Designing the marketing channel starts with finding out what consumers want from the channel. Do customers want to buy from nearby locations or are they willing to travel to more distant, centralized locations? Would they rather buy in person or over the phone, through the mail or via the Internet? Do they value immediate delivery or are they willing to wait? Do they want breadth of assortment or do they prefer specialization? Do customers want many add-on services (delivery, credit, repairs, installation) or will they obtain these elsewhere? The faster the delivery, the greater the assortment provided, and the more add-on services supplied, the greater the channel’s service level.

However, *providing the fastest delivery, greatest assortment and most comprehensive services may not be possible or practical.* The company and its channel members may not have *the resources or skills needed* to provide all the desired services. Also, *providing higher levels of service results not only in higher costs for the channel, but also in higher prices for consumers*. The company must balance consumer service needs against the feasibility and costs of meeting these needs as well as customer price preferences. Generally, customers tend to make trade-offs between service quality and other purchase dimensions, such as price. The success of discount retailing – on and off the Web – shows that consumers are often willing to accept lower service levels in exchange for lower prices.

**8.4.2 Setting channel objectives**

Channel objectives should be stated in terms of *targeted levels of customer service*. The company can usually identify several segments wanting different levels of channel service. The company *should decide which segments to serve and the best channels to use in each case*. The company should aim to minimize *the total channel cost of meeting customer service requirements*. The company’s channel objectives are also influenced by *the nature of the company, its products, its marketing intermediaries, competitors and the environment.* For example, companies selling perishable products require more direct marketing to avoid delays and too much handling. The company’s size and financial situation determine which marketing functions it can handle itself and which it must give to intermediaries. In some cases, a company may want to compete in or near outlets that carry competitors’ products.

Finally, *environmental factors*, such as *economic conditions and legal constraints*, affect channel design decisions. For example, in a depressed economy, producers want to distribute their goods in the most economical way, using shorter channels and dropping unneeded services that add to the final price of the goods.

## 8.4.3 Identifying the major channel alternatives

When the company has defined its channel objectives, it should next identify its major channel alternatives in terms of *types of intermediaries, the number of intermediaries, and the responsibilities of each channel member*.

**8.4.3.1 Types of channel alternatives**

A number of options exist:

* *Direct marketing*. A number of direct marketing approaches can be used, ranging from direct-response selling via advertisements in print media, on radio or television, by mail order and catalogues to telephone and Internet selling.
* *Sales force*. The company can sell directly through its own sales force or deploy another firm’s sales force. Alternatively, a contract sales force might be used.
* *Intermediaries*. Intermediaries are independent organizations that will carry out a number of activities. They include *wholesalers* and *retailers* who buy, take title to and resell the goods.
* **Wholesaler**—A firm engaged primarily in selling goods and services to those buying for resale or business use.
* **Broker**—A wholesaler who does not take title to goods and whose function is to bring buyers and sellers together and assist in negotiation.
* **Agent**—A wholesaler who represents buyers or sellers on a relatively permanent basis, performs only a few functions, and does not take title to goods.
* **Retailers**—Businesses whose sales come primarily from retailing.

**8.4.3.2 Number of marketing intermediaries**

Companies have to decide on the number of intermediaries to use at each channel level. Three strategies are available: exclusive distribution, selective distribution, and intensive distribution.

1. **Exclusive distribution**

Exclusive distribution involves only one wholesaler, retailer or industrial distributors handling the company’s goods or services. It is used when the producer wants to maintain a great deal of control over the service level and service outputs offered by the resellers. Often it involves exclusive dealing arrangements, in which the resellers agree not to carry competing brands. It requires very close cooperation between producer and retailer over serving, pricing and promotion.

1. **Selective distribution**

 Market coverage may also be achieved through selective distribution, in which the producer uses a limited number of outlets in a geographical area to sell its products. The advantages to the best outlets to focus its efforts to build close working relationships with its selected intermediaries. Selective distribution *enables the producer to gain adequate market coverage with more control and less cost than intensive distribution*.

1. **Intensive distribution**

Intensive distribution aims to provide saturation coverage of the market by using all available outlets.

When the consumer requires a great deal of location convenience, it is important to offer greater intensity of distribution. This strategy is generally used for convenience items such as tobacco products, soap, beer, newspapers and foods.

**8.4.3.3 Terms and responsibilities of Channel members**

Relationship marketing is an important part of managing the marketing channel. The producer and intermediaries need to agree on the terms and responsibilities of each channel members. They should agree on: *price policies, condition of sales, territorial rights, and specific services to be performed by each party*.

*The producer should establish a price list and a fair set of discounts for intermediaries and establish a condition of sales as to the payment terms and producer guarantees.* Most producers grant cash discounts to their distributors for early payment. Producers might also guarantee distributors against defective merchandise or price declines. *A guarantee against price declines gives distributors as incentive to buy larger quantities.*

Distributors’ *territorial rights* are other elements in the trade-relation mix. Distributors want to know where and under what terms the producer will enfranchise other distributors. They would also like to receive full credit for all sales taking places in their territory, whether or not they did the selling.

*Mutual services and responsibilities* must be carefully spelled out, especially in franchised and exclusive distribution channels. For example, McDonald’s provides franchisees with a building, promotional support, a record-keeping system, and training and general administrative and technical assistance. In turn, franchisees must meet company standards for physical facilities, cooperate with new promotional programs, provide requested information, and buy specific food products.

## 8.4.4 Evaluation of the major alternatives

Once a company has identified several channel alternatives, it has to select the one that will best satisfy its long-run objectives. The firm must evaluate each alternative against *economic*, *control* and *adaptive* criteria.

Using *economic criteria*, the company compares the likely profitability of different channel alternatives. It estimates the sales that each channel would produce and the costs of selling different volumes through each channel. The company must also consider *control issues*. Using intermediaries usually means giving them some control over the marketing of the product, and some intermediaries take more control than others. Other things being equal, the company prefers to keep as much control as possible. Finally, the company must apply *adaptive criteria*. Channels often involve long-term commitments, yet the company wants to keep the channel flexible so that it can adapt to environmental changes. Thus, to be considered, a channel involving long-term commitment should be greatly superior on economic or control grounds.

**8.5 Channel management decisions**

Once the company has reviewed its channel alternatives and decided on the best channel design, it must *implement and manage the chosen channel*. Channel management calls for *selecting individual intermediaries, motivating and training them and evaluating their performance overtime.*

**8.5.1 Selecting Channel Members**

Producers vary in their ability to attract qualified marketing intermediaries. Some producers have no trouble signing up channel members. In some cases, the promise of exclusive or selective distribution for a desirable product will draw plenty of applicants. At the other extreme are producers that have to work hard to line up enough qualified intermediaries.

When selecting intermediaries, the company should determine what characteristics distinguish the better ones. It will want to evaluate the channel members’ *years in business, other lines carried, growth and profit record, level of cooperation and reputation*. If the intermediaries are sales agents, the company will want to evaluate *the number and character* of other lines carried and the size and quality of the sales force. If the intermediary is a retail store that wants exclusive or selective distribution, the company will want to evaluate the store’s customers, location and future growth potential.

**8.5.2 Managing and motivating channel members**

Once selected, *channel members must be continuously motivated to do their best job*. The key to effective motivation is to *understand the needs and problems of distributor* since needs and motivations are linked. Possible motivators include *financial rewards, territorial exclusivity, providing resources support (e.g. sales training, field sales assistance, provision of marketing research information, advertising and promotion support, financial assistance and management training) and developing strong work relationships (e.g. joint planning, assurance of long-term commitment, appreciation of effort and success, frequent interchange of views and arranging distributor conference).*

The most popular methods cited by export managers and directors to motivate their overseas distributors were *territory exclusivity, provision of up-to-date product and company information, regular personal contact, appreciation of effort and understanding of the distributors’ problems, attractive financial incentives, and provision of salespeople to support the distributors’ sales force.*

**8.5.3 Evaluating channel members**

The producer must regularly check channel member performance against agreed targets such as *sales quotas, average inventory levels, customer delivery time, treatment of damaged and lost goods, cooperation in company promotion and training programs, and services to the customer.* The company should recognize and reward intermediaries that are performing well. Those which are underperforming *should be helped, remedial actions should be taken or, as a last resort, the intermediary should be replaced.* The firm must periodically ‘requalify’ its intermediaries and prune the weak performers, allowing only the best ones to carry its products.

Finally, manufacturers need to be sensitive to their dealers. Those who treat their dealers poorly risk not only losing their support, but also causing legal problems. Disputes with dealers are counterproductive. The key to profitable channel management lies in creating win–win outcomes for all in the ***value delivery network*** – a mutually beneficial relationship that yields cooperation, not conflict, among channel participants will invariably result in higher channel performance.

**8.6 Channel Dynamics**

Distribution channels do not stand still. New types of intermediaries emerge and new channel systems evolve. In this section we will look at the recent growth of vertical, horizontal and multi-channel marketing system.

1. **Vertical Marketing system**

One of the most significant recent channel developments is the rise of vertical marketing system, which has emerged to challenge convectional marketing channels.

***Convectional marketing channel-*** A channel consisting of one or more independent producers, wholesalers and retailers, each a separate business seeking to maximize its own profits, even at the expense of profits for the system as a whole. No channel member has much control over the other members, and no formal means exists for assigning roles and resolving channels conflict. *Channel conflict* is disagreement among marketing channel members on goals and roles who should do what and for what rewards.

In contrast, a vertical marketing system (VMS) *consists of producers, wholesalers, and retailers acting as a unified system.* One channel member owns the other, has contracts with them, or has so much power they must all cooperate. VMSs arose as a result of strong channel members’ attempts to control channel behavior and eliminate the conflict that results when independent channel members that pursue their own objectives. They achieve economies through their size, bargaining power, and elimination of duplicated services.

1. **Horizontal Marketing System**

Another channel development is the horizontal marketing system, in *which two or more unrelated companies put together resources or programs to exploit an emerging marketing 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 with each other on temporary or permanent basis or create a separate company. Adler calls this “symbiotic marketing”.

1. **Multi-Channel Marketing System**

Multi-channel marketing system often called *hybrid marketing channels* – occurs when a single firm uses two or more marketing channels to reach one or more customer segments. Multi-channel distribution systems offer many advantages to companies facing large and complex markets. With each new channel, *the company expands its sales and market coverage, and gains opportunities to tailor its products and services to the specific needs of diverse customer segments.* But such hybrid channel systems are *harder to control, and they generate conflict as more channels compete for customers and sales*.

The End!