Chapter 1

MARKETING CHANNEL CONCEPTS

Chapter Objectives

This chapter introduces marketing channels as a competitive advantage to firms as other forms of traditional competitive differentiations such as price or promotion can be easily copied whereby channel management may not be so easily duplicated. This growing awareness of the importance of marketing channels, in the content of a firm's *overall* marketing objectives is deserving of emphasis and study. In addition, the author introduces key terms and definitions surrounding the topic of channel management and introduces channel management as a separate marketing function. The chapter closes with an examination of the flow in and the through marketing channels and how these channels are structured and how to recognize them and explains the ancillary function.

Learning objectives

1) Be aware of the growing importance of marketing channels in the larger content of overall marketing objectives.
2) Understand the definition of the marketing channel from a *managerial* perspective.
3) Show how marketing channels relate to the other strategic variables in the marketing mix.
4) Understand the *flow* in and through the marketing channels and how they relate to channel management.
5) Familiarize the concepts of channel structure and the ancillary structure and recognize their differences.

Chapter Topics

1) Growing Importance of Marketing Channels
2) The Marketing Channel Defined
3) Use of the term *Channel Manager*
4) Marketing Channels and Marketing Management Strategy
5) Channel Strategy versus Logistics Management
6) Flows in Marketing Channels
7) Distribution through Intermediaries
8) Channel Structure
9) Ancillary Structure

Chapter Outline

Growing Importance of Marketing Channels

A) Explosion of Information Technology and E-Commerce
The explosion of information technology and E-commerce in recent years has focused attention to "channel" as a means for sustainable competitive advantage. Marketing channel strategy and management must now deal with E-commerce technology as an integral part of marketing channels and distribution systems.

The reasons for this attention to channel, as a means of differentiation is a function of:

a) Explosion of information technology and E-commerce
b) Greater difficulty of gaining a sustainable competitive advantage
c) Growing power of distributors, especially retailers in marketing channels
d) The need to reduce distribution costs

Key Terms and Definitions

- Disintermediation: Shorthand for a metamorphosis that would allow hundreds of thousands of producers to be connected directly with millions of consumers without the help of middlemen. This phenomenon did not occur as predicted.

- Reintermediation: Occurred as new types of middlemen called *infomediaries* such as eBay and Yahoo! emerged to connect producers to consumers.

B) Difficulty in Gaining Sustainable Competitive Advantage
Companies struggle to find a sustainable competitive advantage that cannot be easily or quickly copied by competitors. In recent years, the finding of such an advantage is far more difficult using pricing, product, or promotion strategies.
Place or marketing channel strategy, does offer greater potential for a competitive advantage because *it is more difficult for competitors to copy.*

Key Terms and Definitions

- Sustainable competitive advantage: A competitive edge that cannot be quickly or easily copied by competitors.

- Product strategy: Whereby a company creates or modifies a product offering for new or current markets through the use of product innovation, augmentation or line extensions. Rapid technology transfer and global competition has made parity in product designs, features, and quality easier for competitors to copy thus reducing a firm's competitive advantage through product.

- Pricing strategy: Gaining a competitive advantage through pricing strategies is even less feasible than through product development. Pricing strategy is defined as using price as an element in the marketing strategy to gain or hold market share.

- Promotion: The integration of personal selling, advertising, public relations, price discounts, and trade allowances designed to entice the consumer to purchase. The sheer amount of advertising messages to which consumers are exposed to on a daily basis dramatically reduces the time limit promotion provides a firm a competitive advantage.

- Place: The where and how the product or service is delivered to the consumer, the fourth element in the marketing mix, does offer greater potential for a sustainable competitive advantage.

C) Growing Power of Distributors
Economic power has shifted from the producers of goods to the *distributors of goods*. These distributors now form and play a role as "gatekeepers" for the consumers acting as buying agents and selecting what products the consumer "sees". Examples include: Home Depot, Toys 'R' Us, and other "category killers".

D) Need to Reduce Distribution Costs
Distribution costs for many manufacturing firms often meet or exceed the costs of manufacturing or raw materials. In order to reduce these costs manufacturers must begin the process of focusing attention on marketing channel structure more than they have in the past.

The Marketing Channel Defined

The definition of "marketing channel" is based upon one's *perspective* – that of a consumer versus that of a manufacturer.

From the perspective of a marketing manager, the marketing channel is viewed and defined as: "the external contactual organization that management operates to achieve its distribution objectives".

Key Terms and Definitions
- External: Marketing channel exists outside of the firm. Firms must use interorganizational management rather than intraorganizational management.

- Contactual organization: Refers to those firms or parties who are involved in the negotiatory functions. Negotiatory functions include: buying, selling, or transferring title from one firm to another.

- Operates: Involvement by management in the affairs of the channel.

- Distribution objectives: Management has certain distribution goals in mind such as distribution to particular retail stores of key products at or near key times.

Use of the term *Channel Manager*

Few firms actually use this term in their job title descriptions. Figure 1.1 illustrates some of the titles used by selected U.S. firms that involve people in channel management. In fact, many different executives are involved in making channel decisions. In large consumer products companies, the people involved can include the V.P. of Marketing, general marketing manager, product or brand managers, sales managers, or regional sales manager. For industrial products, it might be the V.P. of Sales and V.P. of Marketing. For small business or franchisees, it might be the V.P. of Franchising or small business owner.

Key Term and Definition

- Channel Manager: Provides a sense of focus for referring to the important role of channel decision-making within the firm. Anyone in the firm who is making channel decisions is, while involved in that activity, a channel manager.

Marketing Channels and Marketing Management Strategy

The marketing mix model portrays the marketing management process as a "strategic blending" of the four controllable marketing variables (product, price, promotion, and place). External uncontrollable elements include the economy, technology, government, sociocultural patterns of buyer behavior and competition.

Channel strategy fits under "place" in the marketing management strategy and managers must operate their marketing channels in such a way as to *support and enhance* the other strategic variables in the marketing mix.

The example of Coors® used at this point in the chapter serves to illustrate the importance of *strategic alliances or partnerships* between manufacturer and distributor as a source of sustainable competitive advantages.

Strategic alliances or partnerships have specific advantages:

- Long-term viability
- Cannot be copied quickly
- Cannot be duplicated with price
- Cannot be substituted with a clever idea or short-term promotional program(s)

Channel Strategy versus Logistics Management

Channel strategy and logistics management comprise the distribution variable of the marketing mix.

Channel strategy is concerned with the *entire process* of setting up and operating the contactual organizations that are responsible for meeting the firm's distribution objectives.

Logistics management more narrowly focuses on providing product availability at the appropriate place and time in the marketing channel.

Channel strategy must *first* be established before logistics management should be considered. Logistic management is a subsidiary of channel management.

Flows in Marketing Channels

1. Product flow
2. Negotiation flow
3. Ownership flow
4. Information flow
5. Promotion flow

1. Product flow is the actual *physical* movement of the product from the manufacturer through all of the parties to the consumer.
2.
3. Negotiation flow represents the interplay of the buying and selling functions associated with the transfer of title or rights of ownership. Negotiation is a two-way process involving *mutual* exchange between buyer and seller.

4. Ownership flow is the movement of the *title* of the product from one stage in the process to another.

5. Information flow involves two directions – from the manufacturer to the consumer and from the consumer to the manufacturer. This flow includes transportation as information deemed necessary for the actual delivery of the product is communicated to the transportation agents.

6. Promotion flow refers to the flow of persuasive communication in the form of advertising, personal selling, sales promotion and publicity. This flow adds the advertising agency as an element of promotion.

Distribution through Intermediaries

Economic considerations are very important in determining what form intermediaries will have in their appearance in marketing channels. Two important concepts are introduced: specialization and division of labor and contactual efficiency.

- Specialization and Division of Labor
  When applied to distribution, the concept is that of breaking down complex tasks into smaller, less complex ones and allocating them to parties who are specialists at performing them at greater efficiencies.

- Contactual Efficiency
  From a channel manager's viewpoint, contactual efficiency is the level of negotiation effort between sellers and buyers relative to achieving a distribution objective.

Channel Structure

The concept of channel structure as shown in other marketing books (Figure 1.7) fails to suggest the *relationship* between channel structure and channel management.

Key Term and Definition
- Channel structure: The group of channel members to which a set of distribution tasks has been allocated.

The channel manager is faced with *allocation decisions*, how to allocate or structure the task of distribution.

Multi-channel strategy is when the firm has chosen to reach its target consumer through more than one channel. With the advent of E-commerce, many firms have opted to use multi-channel strategies to reach their target market.

Ancillary Structure

While so far we have included in the channel management only those participants who perform the negotiatory functions of channel management (buying, selling, transferring title, distribution, etc.). There are others that are *not* members of the channel structure that assist in the process. These other members will be defined as *ancillary structure.*

Key Term and Definition
- Ancillary structure: The group of institutions (facilitating agents) that assist channel members in performing distribution tasks.

These ancillary members provide services to the channel members *after the basic channel decisions have already been made.*

Examples of ancillary members include: banks, insurance agents, storage agents, contractors, repair shops, etc.

Channel management must also deal with these ancillary members who do not have as great a stake in the channel as channel members but who are nevertheless key components in ensuring that the product is available to the consumer.