When You Finish This Chapter, You Should

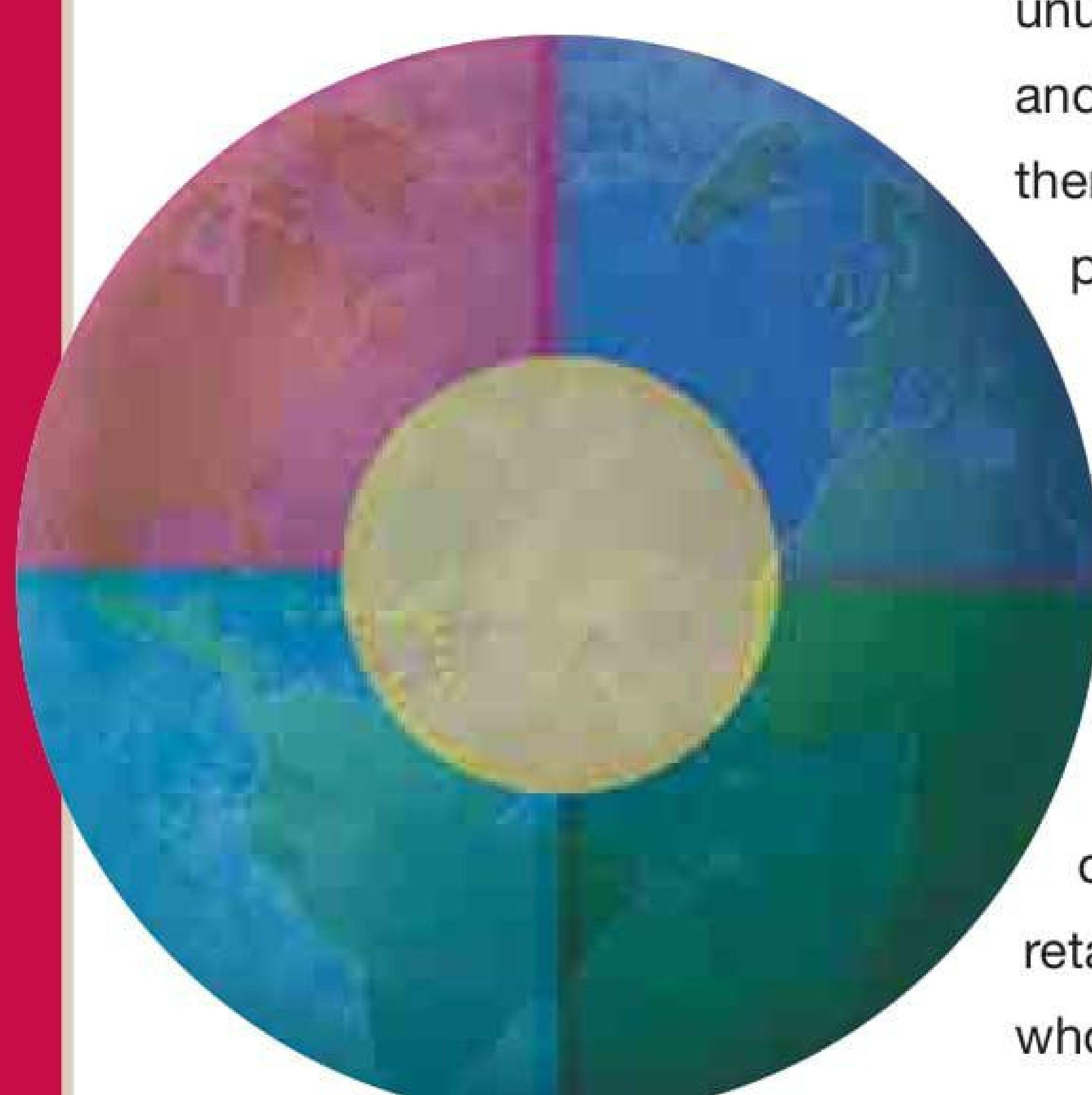
1. Understand how retailers plan their marketing strategies.
2. Know about the many kinds of retailers that work with producers and wholesalers as members of channel systems.
3. Understand the differences among the conventional and nonconventional retailers—including Internet merchants and others who accept the mass-merchandising concept.
4. Understand scrambled merchandising and the "wheel of retailing."
5. See why size or belonging to a chain can be important to a retailer.
6. Know what progressive wholesalers are doing to modernize their operations and marketing strategies.
7. Know the various kinds of merchant wholesalers and agent middlemen and the strategies that they use.
8. Understand why retailing and wholesaling have developed in different ways in different countries.
9. See why the Internet is impacting both retailing and wholesaling.
10. Understand the important new terms (shown in red).

Chapter Thirteen

Retailers, Wholesalers, and Their Strategy Planning

Frieda's, Inc., is a family-owned wholesale firm that each year supplies supermarkets with $30 million worth of exotic fruits and vegetables. It was started by Frieda Caplan in 1962; now, her daughters Karen and Jackie run the company. It is a sign of the marketing savvy of these women that kiwi fruit, artichokes, Chinese donut peaches, alfalfa sprouts, spaghetti squash, pearl onions, and mushrooms no longer seem very exotic. All of these crops were once viewed as unusual. Few farmers grew them, and consumers didn't know about them. Supermarkets and traditional produce wholesalers didn't want to handle them because they had a limited market. Frieda's helped to change all that.

Caplan realized that some supermarkets wanted to put more emphasis on their produce departments. These retailers were targeting consumers who were less price-sensitive and

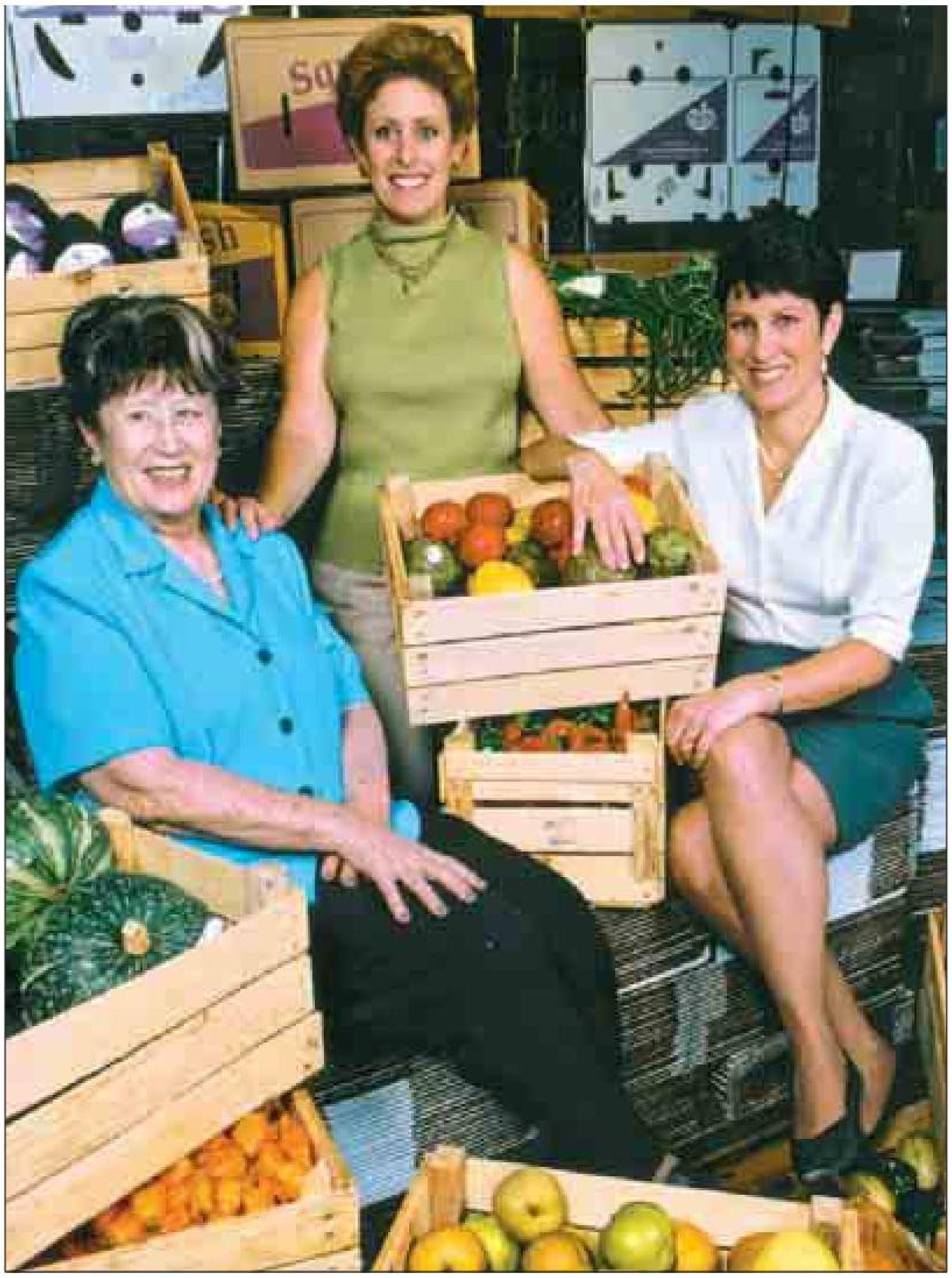


price

place

promotion

produc



wanted more choices in the hard-to-manage produce department. So she looked for products that would help her retailer-customers meet this need. For example, the funny looking, egg-shaped kiwi fruit with its fuzzy brown skin was popular in New Zealand but virtually unknown to consumers in other parts of the world. Caplan worked with a number of small farmer-producers to ensure that she could provide her retailer-customers with an adequate supply. She packaged kiwi with interesting recipes and promoted kiwi *and* her brand name to consumers. Because of her efforts, most supermarkets now carry kiwi—which has become a $40 million crop for California farmers.

Because demand for kiwi has grown, other larger wholesalers now handle kiwi. But that doesn't bother the Caplans. When one of Frieda's specialty items passes the point on the growth curve where it becomes a commodity with low profit margins, another new and novel item replaces it. In a typical year, Frieda's introduces about 40 new products. The Frieda's label, which was redesigned in 1998, is on 400 products—like Asian pears, kiwano melons (from New Zealand), sun-dried yellow tomatoes, and hot Asian chiles.

A few years ago, some skeptics said that specialty wholesalers like Frieda's would bite the dust because online market exchanges, like Produce.com, would make them obsolete. However, Produce.com is out of business and Frieda's is growing faster than ever—in part by taking advantage of its own website and in part by providing value-adding services that get supermarket buyers to think beyond just getting the lowest bid on some commodity.

The Caplans recently established a retail operation, Shop@Friedas, but it doesn't compete directly with supermarkets. Rather, it sells a limited-line of *gift* selections like the "Asian Basket," "Chile Lover's Basket," and other specialty items. Pictures and descriptions of the different baskets are on the firm's website at www.friedas.com, where consumers can order online. The website also has a Club Frieda section. Consumer-members of the club get recipes and advance notices of new products and local promotions. The website also invites consumers to be the "eyes and ears of the company" and send in ideas about interesting new products. Building relationships with consumers isn't new at Frieda's. Earlier the Caplans developed a database with detailed information about preferences and buying habits of 100,000 consumers. These consumers wrote the company in response to an invitation on Frieda's label.

Frieda's continues to have an advantage with many supermarkets because consumers love its products and it offers many special services. It was the first to routinely use airfreight for orders and to send produce managers a weekly "hot sheet" about the best sellers. The Caplans also use seminars and press releases to inform produce buyers about how to improve sales. For example, one attention-getting story was about Frieda's "El Mercado de Frieda" line, which helps retailers do a better job attracting and serving Hispanic customers—a growth segment in many locales. Now that more consumers are eating out, Frieda's is looking beyond the grocery store channel. It has also established a separate division to help the company grow by serving the special needs of food-service distributors. Frieda's has been successful for a long time, in part because it keeps reinventing itself to constantly find new ways to add value in the channel.[1]

Wholesalers and Retailers Plan Their Own Strategies

The Frieda's case shows that wholesalers are often a vital link in a channel system—and in the whole marketing process—helping both their suppliers and customers. It also shows that retailers and wholesalers, like other businesses, must select their target markets and marketing mixes carefully.

In Chapter 11, we discussed the functions that wholesalers and retailers perform as intermediaries in channel systems. In this chapter, we'll focus on the major decision areas that retailers and wholesalers consider in developing their own strategies. We'll also highlight how their strategies are changing.

Understand how retailing and wholesaling are evolving

In this chapter, we'll highlight how retailers and wholesalers, and their strategies, are evolving. It's important to understand this evolution. One basic reason is that the pace of change is accelerating. Some traditional approaches are being modified and newer approaches, like selling from online websites, are prompting marketers to come up with new and better ways to meet the needs of customers at the end of the channel. If you understand the evolution, you will be better prepared for changes that come in the future—and more change will come.

The other reason, perhaps even more basic, is that different types of retailers and wholesalers have evolved to meet different needs in the marketplace. As we emphasized from the start, not all customers have the same needs. Seeing the different ways that retailers and wholesalers have modified their strategies will make it clear that it is the whole strategy, not just one aspect of it, that ultimately is a success or failure. This may seem obvious, but apparently not to everyone.

A few years ago, some people were proclaiming that marketers needed to throw out all of the thinking that anyone had ever done about retailing and wholesaling because the Internet had changed everything. It is certainly true that the Internet has fostered dramatic innovations and that many benefits (for firms and for consumers) are yet to be realized. But that doesn't mean that the Internet changes customers' basic needs, or wants, or for that matter the role that any sort of specialized middleman (whether in a bricks-and-mortar facility, online, or both) plays in the Place system.

Unfortunately, people who forget the lessons of the past are condemned to repeat them. Many creative people who had exciting ideas for online retailing innovations failed precisely because they didn't learn that. Many fell into the trap of thinking that all customers were the same—or that customers would be satisfied just because some aspect of a firm's marketing mix met some needs really well—even if it ignored other needs. Yet it doesn't matter if an online retailer has an incredible assortment if there's no way for buyers to get live customer service when they can't get the order page to work. It doesn't matter if a seller posts a low price if the products are not actually available to ship or if shipping costs make the real price exorbitant. And it isn't convenient to return a green shirt that looked blue on the website, even if the website is conveniently available 24/7.

So in general, in this chapter we will concentrate on strategy decisions that apply to *all* retailers and wholesalers. But we will also highlight the differences that are most significant in terms of the ongoing evolution. We'll start with a closer look at retailing, and then cover wholesaling.

The Nature of Retailing

Retailing covers all of the activities involved in the sale of products to final consumers. Retailers range from large chains of specialized stores—like Toys "R" Us—to individual merchants like the woman who sells baskets from an open stall in the central market in Ibadan, Nigeria. Some retailers operate from stores and others operate without a store—by selling online, on TV, with a printed catalog, from vending machines, or even in consumers' homes. Most retailers focus on selling physical goods produced by someone else. But in the case of service retailing—like dry cleaning, fast food, tourist attractions, online bank accounts, or one-hour photo processing, for example—the retailer is also the producer. Because they serve individual consumers, even the largest retailers face the challenge of handling small transactions. And the total number of transactions with consumers is much greater than at other channel levels.

Retailing is crucial to consumers in every macro-marketing system. For example, consumers spend $3.2 *trillion* (that's $3,200,000,000,000!) a year buying goods and services from U.S. retailers.

The nature of retailing and its rate of change are generally related to the stage and speed of a country's economic development. In the U.S., retailing is more varied and more dynamic than in most other countries. By studying the U.S. system, and how it is changing, you will better understand where retailing is headed in other parts of the world.

Planning a Retailer's Strategy

Retailers interact directly with final consumers—so strategy planning is critical to their survival. If a retailer loses a customer to a competitor, the retailer is the one who suffers. Producers and wholesalers still make *their* sale regardless of which retailer sells the product.

Consumers have reasons for buying from particular retailers

Different consumers prefer different kinds of retailers. But many retailers either don't know or don't care why. All too often, beginning retailers just rent a store and assume customers will show up. As a result, in the U.S. about three-fourths of new retailing ventures fail during the first year. Even an established retailer can quickly lose its customers if they find a better way to meet their needs. To avoid this fate, a retailer should have a clear strategy. A retailer needs to carefully identify possible target markets and try to understand why these people buy where they do. That helps the retailer tune its marketing mix to the needs of specific target markets.[2]

Retailer's whole offering is its Product

Most retailers in developed nations sell more than one kind of product. So their product assortment (including brands carried) can be critical to their success. Yet it's best to take a broader view in thinking about the Product strategy decisions for a retailer's marketing mix. The retailer's *whole* offering—assortment of goods and services, advice from salesclerks, convenience, and the like—is its "Product."

Different consumers have different needs—and needs vary from one purchase situation to another. Which retailer's Product offers the best customer value depends on the needs that a customer wants to satisfy. Whatever the effect of other consumer needs, economic needs are usually very important in shaping the choice of a retailer. Social and individual needs may also come into play. Our discussion of consumer behavior and needs in Chapter 6 applies here.

Features of offering relate to needs

Features of a retailer's offering that relate to economic needs include

- *Convenience* (location, available hours, parking, finding needed products, fast checkout).
- *Product selection* (width and depth of assortment, quality).
- *Special services* (special orders, home delivery, gift wrap, entertainment).
- *Fairness in dealings* (honesty, correcting problems, return privileges, purchase risks).
- *Helpful information* (courteous sales help, displays, demonstrations, product information).
- *Prices* (value, credit, special discounts, taxes or extra charges).

Some features that relate to social and emotional factors include

- *Social image* (status, prestige, "fitting in" with other shoppers).
- *Shopping atmosphere* (comfort, safety, excitement, relaxation, sounds, smells).

In later chapters we'll go into much more detail on the price and promotion decisions that all firms—including retailers and wholesalers—make.

Strategy requires carefully set policies

At this point it is important to see that in developing a strategy a retailer should consciously make decisions that set policies on *all* of these factors. Each of them can impact a customer's view of the costs and benefits of choosing that retailer. And in combination they differentiate one retailer's offering and strategy from another. If the combination doesn't provide superior value to some target market, the retailer will fail.

It's best of think of a retailer's Product as its whole offering—including its assortment of goods and services, advice from salespeople, the convenience of shopping, and hours it is available.

Consumer needs relate to segmentation and positioning

As in other businesses, segmentation and positioning decisions are important to retailers. And ignoring either economic or social and emotional values in those decisions can lead to serious errors in a retailer's strategy planning.

Consider, for example, how the shopping atmosphere may have an emotional effect on a consumer's view of a retailer. How merchandise is displayed, what decorations, colors, and finishes are used, and even the temperature, sounds, and smell of a store all contribute to its "atmospherics" and store image. The right combination may attract more target customers and encourage them to spend more. Tiffany's, for example, offers luxury surroundings and inventive displays to attract upscale consumers. But Tiffany's may also appeal to consumers who get an ego boost from Tiffany's prestige image and very attentive staff. Of course, interesting surroundings are usually costly, and the prices that consumers pay must cover that expense. An online jewelry retailer avoids those costs but offers a completely different shopping experience and deals with a different set of needs. So a retailer's atmosphere and image may be a plus or a minus, depending on the target market. And there's no single right answer about which target market is best. Like Tiffany's, Dollar General has been very profitable. But it has a "budget" image and atmosphere that appeals to working-class customers, many of whom just prefer to shop where they don't feel out of place.[3]

Different types of retailers emphasize different strategies

Retailers have an almost unlimited number of ways in which to alter their offerings—their marketing mixes—to appeal to a target market. Because of all the variations, it's oversimplified to classify retailers and their strategies on the basis of a single characteristic—such as merchandise, services, sales volume, or even whether they operate in cyberspace. But a good place to start is by considering basic types of retailers and some differences in their strategies.

Let's look first at conventional retailers. Then we'll see how other retailers successfully modify conventional offerings to better meet the needs of *some* consumers. Think about *why* the changes take place. That will help you identify opportunities and plan better marketing strategies.

Conventional Retailers—Try to Avoid Price Competition

Single-line, limited-line retailers specialize by product

A hundred and fifty years ago, **general stores**—which carried anything they could sell in reasonable volume—were the main retailers in the United States. But with the growing number of consumer products after the Civil War, general stores couldn't offer enough variety in all their traditional lines. So some stores began specializing in dry goods, apparel, furniture, or groceries.

In spite of consumer interest in Western products and new retailing formats, most retailing in Asia is still handled by small limited-line stores, like the independently owned Filipino store on the left and the Japanese electronics one on the right.

Now most conventional retailers are **single-line** or **limited-line stores**—stores that specialize in certain lines of related products rather than a wide assortment. Many stores specialize not only in a single line, such as clothing, but also in a *limited-line* within the broader line. Within the clothing line, a retailer might carry *only* shoes, formal wear, men's casual wear, or even neckties but offer depth in that limited line.

Single-line, limited-line stores are being squeezed

The main advantage of such retailers is that they can satisfy some target markets better. Perhaps some are just more conveniently located near their customers. But for most it's because they adjust to suit specific customers. They try to build a long-term relationship with their customers and earn a position as *the* place to shop for a certain type of product. But single-line and limited-line stores face the costly problem of having to stock some slow-moving items in order to satisfy the store's target market. Many of these stores are small—with high expenses relative to sales. So they try to keep their prices up by avoiding competition on identical products.

Conventional retailers like this have been around for a long time and are still found in every community. Many now face stiff competition from other types of retailers. Even so, they are a durable lot and clearly satisfy some people's needs. In fact, in most countries conventional retailers still handle the vast majority of all retailing sales.

However, this situation is changing fast. Nowhere is the change clearer than in the United States. Conventional retailers are being squeezed by retailers who modify their mixes in the various ways suggested in Exhibit 13-1. Let's look closer at some of these other types of retailers.

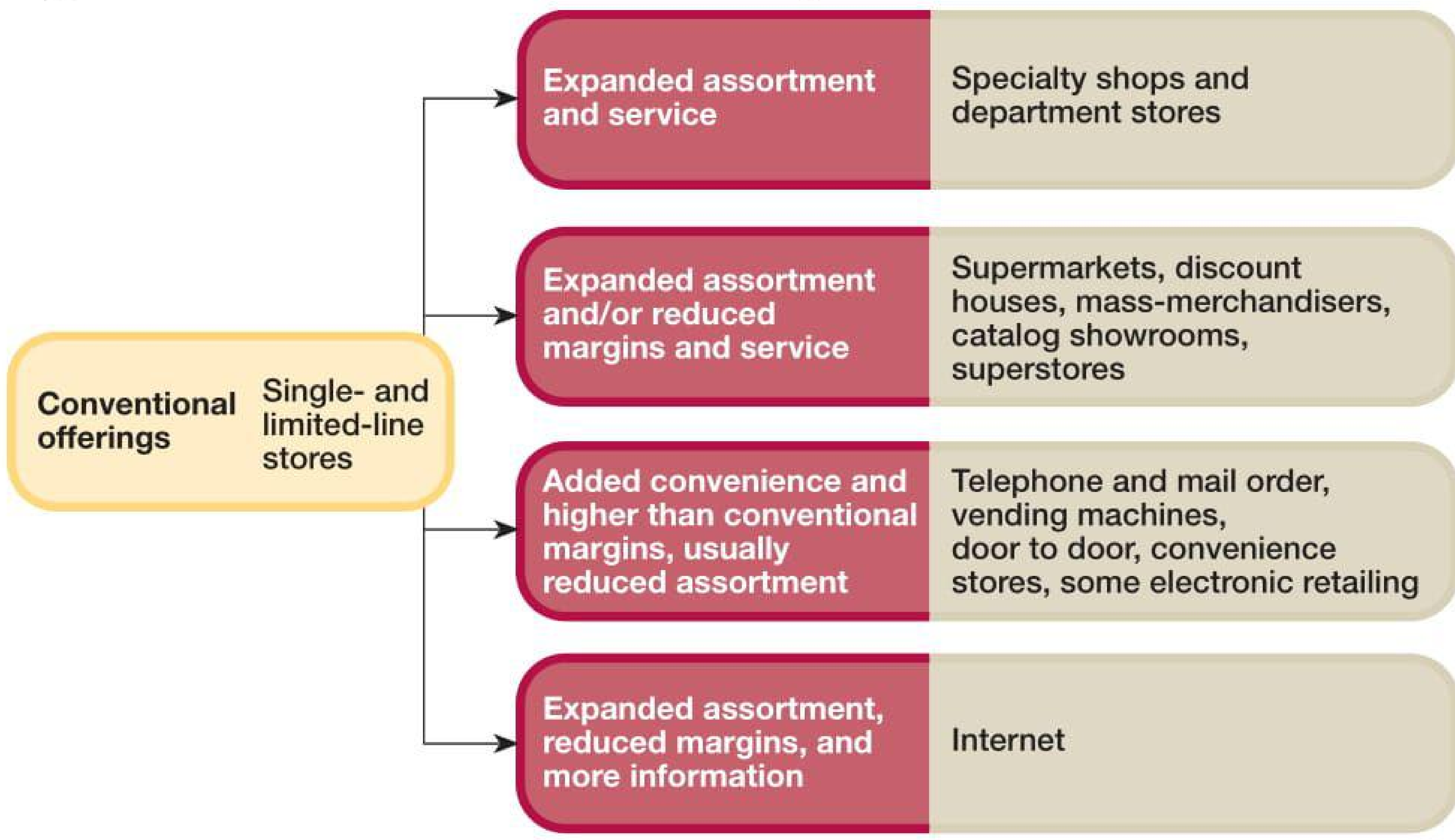
Expand Assortment and Service—To Compete at a High Price

Specialty shops usually sell shopping products

A **specialty shop**—a type of conventional limited-line store—is usually small and has a distinct "personality." Specialty shops sell special types of shopping products—such as high-quality sporting goods, exclusive clothing, cameras, or even antiques. They aim at a carefully defined target market by offering a unique product assortment, knowledgeable salesclerks, and better service.

The specialty shop's major advantage is that it caters to certain types of customers whom the management and salespeople come to know well. This simplifies buying,

Exhibit 13-1 Types of Retailers and the Nature of Their Offerings



speeds turnover, and cuts costs due to obsolescence and style changes. Specialty shops probably will continue to be a part of the retailing scene as long as customers have varied tastes and the money to satisfy them.[4]

Department stores combine many limited-line stores and specialty shops

Department stores are larger stores that are organized into many separate departments and offer many product lines. Each department is like a separate limited-line store and handles a wide variety of shopping products—such as men's wear or housewares. They are usually strong in customer services—including credit, merchandise return, delivery, and sales help on the floor.

Department stores are still a major force in big cities. But in the U.S., the number of department stores, the average sales per store, and their share of retail business has declined continuously since the 1970s. Well-run limited-line stores compete with good service and often carry the same brands. In the U.S. and many other countries, mass-merchandising retailers have posed an even bigger threat. We'll discuss them next.[5]

Evolution of Mass-Merchandising Retailers

Mass-merchandising is different from conventional retailing

So far we've been describing retailers primarily in terms of their product *assortment*. This reflects traditional thinking about retailing. We could talk about supermarkets, discount houses, or online retailers in these terms too. But then we would miss some important differences—just as some conventional retailers did when mass-merchandising retailers first appeared.

Conventional retailers think that demand in their area is fixed—and they have a "buy low and sell high" philosophy. Many modern retailers reject these ideas. They accept the **mass-merchandising concept**—which says that retailers should offer low prices to get faster turnover and greater sales volumes—by appealing to larger markets. The mass-merchandising concept applies to many types of retailers—including both those that operate stores and those that sell online. But to understand mass-merchandising better, let's look at its evolution from the development

Although U.S. supermarkets were the first mass-merchandisers, the mass-merchandising concept has now been introduced by many retailers. Single-line mass-merchandisers like Office Depot offer selections and prices that make it difficult for traditional retailers to compete.

of supermarkets and discounters to modern mass-merchandisers like Wal-Mart in the U.S., Tesco in the U.K., and Amazon.com on the Internet.

Supermarkets started the move to mass-merchandising

From a world view, most food stores are relatively small single- or limited-line operations, a situation that makes shopping for food inconvenient and expensive. Many Italians, for example, still go to one shop for pasta, another for meat, and yet another for milk. Although this seems outdated, keep in mind that many of the world's consumers don't have access to **supermarkets**—large stores specializing in groceries with self-service and wide assortments.

The basic idea for supermarkets developed in the U.S. during the early Depression years. Some innovators felt they could increase sales by charging lower prices. They introduced self-service to cut costs but provided a broad product assortment in large bare-bones stores. Success and profits came from large-volume sales—not from high traditional markups.[6]

Newer supermarkets carry 40,000 product items and stores average around 45,000 square feet. To be called a supermarket, a store must have annual sales of at least $2 million, but the average supermarket sells much more, an average of about $17 million a year. In the U.S., the number of supermarkets has continued to grow and it is now about 32,000. In most areas they are at the saturation level and competition is intense. In many other countries, however, they are just becoming a force.[7]

To outsell competitors, supermarkets try to differentiate their offerings. Some have better produce, others have lower prices, some offer a deli or cleaner store, and so forth. But there are many things they all have to offer—like milk and eggs and cereal. In fact, an average family gets about 80 percent of its needs from only about 150 skus. The rub is that particular 150 skus vary from family to family. In the end, a consumer makes a single choice in deciding to shop at a particular supermarket. But to come out on top in *that* choice, the supermarket must offer consumers many thousands of choices and at the same time keep costs low.[8]

Modern supermarkets are planned for maximum efficiency. Scanners at checkout counters make it possible to carefully analyze the sales and profit of each item and allocate more shelf space to faster-moving and higher-profit items. This helps sell more products—faster. It also reduces the investment in inventory, makes stocking easier, and minimizes the cost of handling products. *Survival* depends on such efficiency. Net profits in supermarkets usually run a thin 1 percent of sales *or less!*

To increase sales volume and turnover, some supermarket operators open "super warehouse" stores. These 50,000- to 100,000-square-foot stores carry more items than supermarkets, but they usually put less emphasis on perishable items like produce or meat. These efficiently run, warehouse-like facilities sell groceries at about 25 percent off the typical supermarket price.[9]

Catalog showroom retailers preceded discount houses

Catalog showroom retailers sell several lines out of a catalog and display showroom—with backup inventories. Before 1940, most catalog sellers were wholesalers who also sold at discounted prices to friends and members of groups—such as labor unions or church groups. In the 1970s, however, these operations expanded rapidly by aiming at final consumers and offering attractive catalogs and improved facilities. Catalog showroom retailers—like Service Merchandise—offer price savings and deliver almost all the items in their catalogs from backroom warehouses. They emphasize well-known manufacturer brands of jewelry, gifts, luggage, and small appliances but offer few services.[10]

Early catalog retailers didn't bother conventional retailers because they weren't well publicized and accounted for only a small portion of total retail sales. If those catalog retailers had moved ahead aggressively, the current retailing scene might be different. But instead, discount houses developed and now most catalog showroom retailers have gone out of business.

Discount houses upset some conventional retailers

Right after World War II, some retailers moved beyond offering discounts to selected customers. These **discount houses** offered "hard goods" (cameras, TVs, appliances) at substantial price cuts to customers who would go to the discounter's low-rent store, pay cash, and take care of any service or repair problems themselves. These retailers sold at 20 to 30 percent off the list price being charged by conventional retailers.

In the early 1950s, with war shortages finally over, manufacturer brands became more available. The discount houses were able to get any brands they wanted and to offer wider assortments. At this stage, many discounters turned respectable—moving to better locations and offering more services and guarantees. It was from these origins that today's mass-merchandisers developed.

Mass-merchandisers are more than discounters

Mass-merchandisers are large, self-service stores with many departments that emphasize "soft goods" (housewares, clothing, and fabrics) and staples (like health and beauty aids) but still follow the discount house's emphasis on lower margins to get faster turnover. Mass-merchandisers—like Wal-Mart and Target—have checkout counters in the front of the store and little sales help on the floor. Today the average mass-merchandiser has nearly 60,000 square feet of floor space, but many new stores are 100,000 square feet or more.

Mass-merchandisers grew rapidly—and they've become the primary nonfood place to shop for many frequently purchased consumer products. By itself, Wal-Mart handles a whopping 20 percent or more of the total national sales for whole categories of products. Even if you don't shop at Wal-Mart, Sam Walton (who started the company) has had a big impact on your life. He pioneered the use of high-tech systems to create electronic links with suppliers and take inefficiencies out of retailing logistics. That brought down costs *and* prices and attracted more customers, which gave Wal-Mart even more clout in pressuring manufacturers to lower prices. Other retailers are still scrambling to catch up. It was competition from Wal-Mart on staples such as health and beauty aids and household cleaning products that prompted firms in the supermarket supply chain to start the Efficient Consumer Response movement we discussed in Chapter 12. Many catalog showroom retailers didn't adjust fast enough and went bust. Many conventional retailers are adjusting their strategies—just to survive. And it's Wal-Mart's phenomenal growth and success that motivates many new online retailers to think that their innovations can do the same thing. But this dynamic change is what marketing is all about—and it is providing consumers with superior value.

Although these mass-merchandisers are the driving force in much of retailing in the U.S. today, they've expanded so rapidly in many areas that they're no longer just taking customers from conventional retailers but instead are locked in head-to-head competition with each other. So their growth rate in the U.S. has slowed substantially and, for future growth, they're expanding internationally.[11]

Supercenters meet all routine needs

Some supermarkets and mass-merchandisers have moved toward becoming **supercenters (hypermarkets)**—very large stores that try to carry not only food and drug items but all goods and services that the consumer purchases *routinely*. These superstores look a lot like a combination of the supermarkets, drugstores, and mass-merchandisers from which they have evolved, but the concept is different. A supercenter is trying to meet *all* the customer's routine needs at a low price. Supercenter operators include Wal-Mart, Meijer, Fred Meyer, and Super Target.

Supercenters average more than 150,000 square feet and carry about 50,000 items. In addition to foods, a supercenter carries personal care products, medicine, some apparel, toys, some lawn and garden products, gasoline, and services such as dry cleaning, travel reservations, bill paying, and banking. Growth in the number of supercenters seems to be slowing. Their assortment in one place is convenient, but many time-pressured consumers think that the crowds, lines, and "wandering around" time in the store are not. Expect someone to see this as an opportunity—perhaps for a new type of fast-service mass-merchandiser with stores in the 30,000- to 40,000-square-foot range.[12]

New mass-merchandising formats keep coming

The warehouse club is another retailing format that quickly gained popularity. Sam's Club and Costco are two of the largest. Consumers usually pay an annual membership fee to shop in these large, no-frills facilities. Among the 3,500 items per store, they carry food, appliances, yard tools, tires, and other items that many consumers see as homogeneous shopping items and want at the lowest possible price. The rapid growth of these clubs has also been fueled by sales to small-business customers. That's why some people refer to these outlets as wholesale clubs. However, when half or more of a firm's sales are to final consumers, it is classified as a retailer, not a wholesaler.[13]

Single-line mass-merchandisers are coming on strong

Since 1980 some retailers—focusing on single product lines—have adopted the mass-merchandisers' approach with great success. Toys "R" Us pioneered this trend. Similarly, PayLess Drugstores, B. Dalton Books, Ikea (furniture), Home Depot (home improvements), Circuit City (electronics), and Office Depot attract large numbers of customers with their large assortment and low prices in a specific product category. These stores are called category killers because it's so hard for less specialized retailers to compete.[14]

It's reasonable to think about the move to 24-hours-a-day online selling—by the established retailers, new firms that never relied on stores, or both—as a next step in the evolution of mass-merchandising. But we'll have a more complete basis for evaluating the strengths and limitations of selling and shopping on the Web if we first look at some retailers who have targeted consumers who want more convenience, even if the price is higher.

Some Retailers Focus on Added Convenience

Convenience (food) stores must have the right assortment

Convenience (food) stores are a convenience-oriented variation of the conventional limited-line food stores. Instead of expanding their assortment, however, convenience stores limit their stock to pickup or fill-in items like bread, milk, beer, and eat-on-the-go snacks. Stores such as 7-Eleven and Stop-N-Go aim to fill consumers' needs between major shopping trips to a supermarket and many of them are competing with fast-food outlets. They offer convenience, not assortment, and often charge prices 10 to 20 percent higher than nearby supermarkets. However, as many gas stations have been converted to convenience stores and other retailers have expanded their hours, intense competition is driving down convenience store prices and profits.[15]

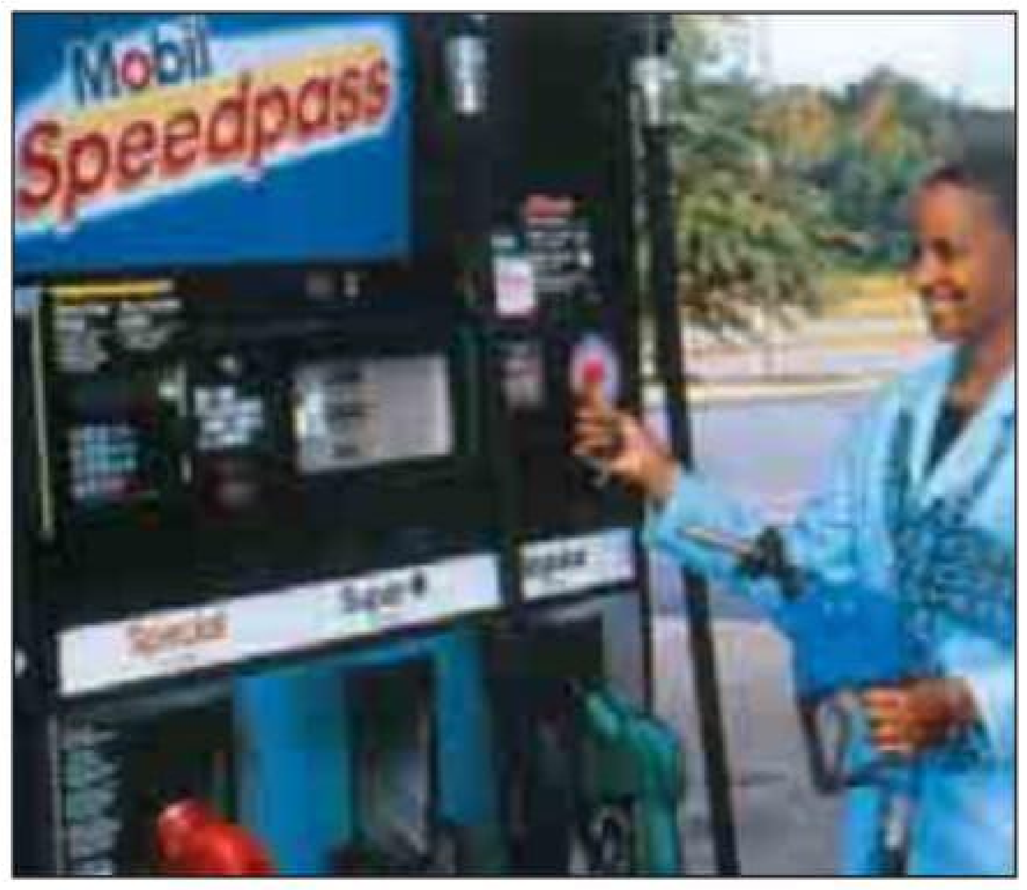
Vending machines are convenient

Automatic vending is selling and delivering products through vending machines. Although the growth in vending machine sales is impressive, such sales account for only about 1.5 percent of total U.S. retail sales. Yet for some target markets this retailing method can't be ignored.

The major disadvantage to automatic vending is high cost. The machines are expensive to buy, stock, and repair relative to the volume they sell. Marketers of similar nonvended products can operate profitably on a margin of about 20 percent. The vending industry requires about 41 percent to cover costs—so they must charge higher prices.[16]

Shop at home—in a variety of ways

In-home shopping has been around for a long time, but it's become a lot more varied and a lot more popular over the years. In the U.S., it started in the pioneer days with **door-to-door selling**—a salesperson going directly to the consumer's home. Variations on this approach are still important for firms like Amway and Mary Kay. It meets some consumers' need for convenient personal



Many retailers are looking for ways to make shopping faster and more convenient. With Mobil's SpeedPass system, a miniature electronic device identifies the driver and turns on the pump; the customer doesn't even need a credit card.

attention. It is also growing in popularity in some international markets, like China, where it provides salespeople with a good income. In the U.S., it now accounts for less than 1 percent of retail sales. It's getting harder to find someone at home during the day.

On the other hand, time-pressured dual-career families are a prime target market for **telephone and direct-mail retailing** that allow consumers to shop at home—usually placing orders by mail or a toll-free long-distance telephone call and charging the purchase to a credit card. Typically, catalogs and ads on TV let customers see the offerings, and purchases are delivered by UPS. Some consumers really like the convenience of this type of retailing—especially for products not available in local stores.

This approach reduces costs by using computer mailing lists to help target specific customers and by using warehouse-type buildings and limited sales help. And shoplifting—a big expense for most retailers—isn't a problem. After-tax profits for successful mail-order retailers average about 7 percent of sales—more than twice the profit margins for most other types of retailers. However, with increasing competition and slower sales growth, these margins have been eroding. As we will discuss, however, the Internet is opening up new growth opportunities for many of these firms.[17]

Put the catalog on cable TV or computer

QVC, Home Shopping Network, and others are succeeding by devoting cable TV channels to home shopping. Some experts think that the coming explosion in the number of available cable channels and interactive cable services will make sales from this approach grow even faster. In addition, QVC has opened a major website on the Internet. However, selling on the Internet is turning into something much more than just a variation of selling on TV or from a catalog.[18]

Retailing on the Internet

Until now, as we've talked about the evolution of retailers and the varied ways they have innovated to respond to consumer demand and meet needs, we've not devoted much attention to retailing on the Internet. It's reasonable to ask why. As we said earlier, Wal-Mart and other mass-merchandisers now sell on the Web, so one could view that development as just another aspect of how low-margin mass-merchandisers are trying to appeal to a large target market with wide (or deep) assortments of products at discount prices. Or one might view the Internet as just another way to add convenient in-home shopping, with an electronic catalog and ordering on a remote computer. After all, that's the way most people saw earlier pre-Internet dial-up systems such as Prodigy—a joint venture between Sears and IBM that fizzled because it was too complicated.

Both of these views make some sense, yet they are incomplete and probably misleading. The fact is that almost *all* types of retailers are now establishing a presence on the Internet. It has the potential over time to dramatically reshape many aspects of retail selling. So rather than just treat it as a new way that some types of retailers are incrementally varying their old strategies, let's look at it in terms of what it is likely to become—something that is *really* different.

It's still in its infancy

Despite all the attention, Internet retailing is still in the early growth stages. On the one hand, Internet usage continues to rise and consumer e-commerce sales have grown at an exceptionally fast rate. In 1997, consumers spent about $2.7 billion on the Internet. To put that in perspective, it took about 3 percent of Wal-Mart's stores to rack up the same sales. By 2001 that number leaped to about $144 billion. But don't confuse growth or the "big bang" that the Internet may have on retailing and consumer shopping behavior with the reality of its immediate economic impact on the retail system. So far, all of that spending is less than 5 percent of retailing sales dollars. Further, the numbers are as high as they are because a lot of expensive computer equipment has been sold that way. So in absolute dollars, retailing on the Internet is in its infancy. However, it has the potential to continue to grow. Taking these two vantage points in combination, it's useful to consider what's different about it today and how it will evolve. See Exhibit 13-2.

Moving information versus moving goods

Stripped to its essence, the Internet dramatically lowers the cost of communication while making it faster. So it can radically alter activities that depend on the flow of information. The Internet has produced the biggest gains in businesses where better information results in more efficient restructuring of tasks. As we discussed in Chapter 7, that's what happens in much online B2B e-commerce. On the other hand, Place decisions for consumer markets need to deal with the challenge of handling truckloads of products and getting them to the *consumer's* place. Much of the investment in Internet retailing systems has been directed toward moving information (like orders), not physical goods. It takes, for example, about $15 to $25 million to build a world-class website for consumer e-commerce. But it costs about $150 million to build a distribution center and systems to support a large-scale consumer Web operation. Therefore, much of the attention so far has been on the "front door"

Exhibit 13-2 Some Illustrative Differences between Online and In-Store Shopping

Characteristics	Online Shopping	In-Store Shopping
Customer characteristics	Younger, better educated, more upscale	Cross section; depends on store
Day-of-week emphasis	Higher percent of purchases during weekdays	Higher percent of purchases on the weekend
Customer service	Weak but improving	Varies, but usually better than online
Products purchased	More emphasis on one-time purchases	More emphasis on routine purchases
Availability of product	Not available for inspection or immediate use	Usually available for inspection and immediate use
Comparative information about products	Much more extensive, but sometimes poorly organized	Often weak (for example, limited to what is on packages)
Entertainment value	A media experience	Often a social experience
Charges	Product prices often lower, but shipping and handling costly	Product prices and taxes higher, but usually no delivery expense
Shopping hours and preparation	Completely flexible if online access is available	Depends on store and available transportation

of the Internet "store" and not on the back end of retailing operations where more of the big costs accumulate.

The investment and innovations will come into balance over time, just as they have with other retailing innovations. But demand is what will shape investments in new supply capabilities. So far, the basic patterns of consumer demand have not changed that much. There are, of course, exceptions. For example, more consumer financial services companies are selling on the Web than are retailers in any other industry—but that is an information-intensive service business rather than one that adjusts physical discrepancies.

Now, let's take a closer look at some of the communication aspects of Internet retailing from the consumer's point of view.

Product assortments are not limited by location

As we noted earlier, traditional thinking about retailing looks at product assortments from the perspective of location and shopping convenience. On the Internet, by contrast, a consumer can get to a very wide assortment, perhaps from different sellers, by clicking from one website to another. The assortment moves toward being unlimited.

Convenience takes on new meanings

If the Internet makes it very convenient to shop, it is very inconvenient in other ways. You have to plan ahead. You can't touch or inspect a product. When you buy something from the Internet, you've actually just ordered it. You don't have it to hold. Someone has to deliver it, and that involves delays and costs.

Surfing around the Internet is convenient for people who are facile with computers, but many consumers are not. At present, people who actually shop on the Web are better educated, younger, and more well to do. It should be no surprise that the majority of retail dollars spent via the Internet so far are for computer-related stuff. That target market visits the Internet store. But many people don't.

Of course, access to and use of the Internet is evolving quickly. Cable operators and telephone companies are in a race to provide more consumers with faster access. Other firms and new technologies are being developed all the time. WebTV already makes it easy, but it is just the start. Costs will continue to come down, and within a decade most U.S. homes will have *routine* access to the Internet.

More and less information at the same time

On the Internet a consumer can't touch a product or really inspect it. For many products consumers want to be able to do that, or at least they're used to doing it. On the other hand, when a consumer is in a retail store it's often hard to get any information—say nothing about good information. At a website it's often possible to get much more information with just a mouse-click, even though only the product and a brief description is presented on the initial page.

It's also possible to access a much broader array of information. Ziff-Davis Publishing, for example, has a comprehensive website (www.zdnet.com) with product reviews, feature comparisons, performance tests, and other data on every computer-related product imaginable. Similar sites are being developed for everything from automobiles to vitamins. Better information will make many consumers better shoppers, even if they buy in a store rather than online. That's what many Web surfers do now. That reduces the risk of not getting what they thought they were buying and the hassles of returning it if there's a problem.

More powerful computers are also opening up many more possibilities for multimedia information—not just pictures but full-motion product-demo videos and audio explanations. The Internet is also quickly turning into a medium for video conferencing; many computers come with a videocam as an inexpensive accessory. So it is likely that in the near future consumers will not only be able to get computer-provided help during a visit to a website but also help from a real person. Many failed dot-com retailers figured out too late that their website operations could cut some types of costs, but failing to provide human customer service support was a big mistake. They ignored the lessons learned by mass-merchandisers in their early days when they tried to do the same thing.

Why eToys.com Is eToys.Gone

eToys was founded in 1997 with the dream of becoming the premier site on the Internet for the kids' product market. Many investors shared its vision of unlimited growth; at one time its stock market value was 35 percent greater than its long-established profitable competitor, Toys "R" Us. eToys did deliver in producing one of the slickest e-commerce websites. Parents could search for toys by age group or theme or product. Kids could create and send "gift wish lists." But eToys failed to consider some basic marketing ideas. For example, toys are a mature category, so a user-friendly website doesn't increase total consumer demand. eToys also underestimated how competitors would react to its plan to take most of their customers—which is what it would have taken to even cover eToys' costs. Wal-Mart copied some of eToys' best ideas but also had the buying clout to create its own brands and sell toys cheaper. Toy "R" Us teamed up with Amazon. Worse, eToys assumed that once it got customers to its site—by spending huge amounts on advertising—those customers would be loyal. When 5 percent of its orders didn't go out on time during the 1999 holiday season, customers bolted. Every parent who let a kid down told everyone they knew. When eToys tried to improve its distribution systems, costs spiraled out of control because of the hassles of handling breakable toys that come in all sorts of sizes and shapes. In the end, the total costs of efforts were so high that it would have taken four or five years of constantly improving sales just to break even on operations—say nothing about making up millions in losses. You can build a better mousetrap, but if it doesn't meet customer needs at a profit you're in trouble.[19]

Lost in the "aisles" of the Internet

If you know what you want, and it's one thing, you can usually find it fast on the Internet. You can look for "Revo sunglasses" with a search engine and get a list of sellers and see pictures of every style made. It's quick and easy. If you don't know exactly what you've looking for, however, you may get too much information or the wrong information. It's hard to narrow a search when you don't know what you're looking for. Clearly, for the appeal of Internet retailing to spread there will need to be better "virtual malls"—databases with lots of information that can be viewed lots of ways—to make it easier to get information you want and avoid the clutter that is, at best, irrelevant. Retailers like Amazon and Wal-Mart have constantly revised and improved their websites to address this issue, but more progress will be needed.

Internet

Internet Exercise INTERSHOP Communications develops and sells software that companies use to create "virtual stores" for Internet retailing. For example, it allows a seller to create an online catalog that is easy for consumers to use, and it has tools for analyzing sales and keeping track of customers. Go to the firm's website (www.intershop.com) and select *Products* and then *Enfinity*. Review the information provided. Do you think it would be easier for consumers if all Internet sellers used a common system, such as this one, rather than coming up with many different arrangements? Briefly explain your thinking.

The costs are still deceptive

The Internet makes it easy to do comparison shopping and to compare prices from different sellers. That already is putting price pressure on Internet sellers, in part because few have figured out how else to differentiate what they offer. On the other hand, as we emphasized at the start of the chapter, the customer's total cost of shopping is more than just the purchase price. For more expensive items, a discount price may offset delivery costs. That often isn't the case with less expensive items. Low-cost ways of handling post-purchase deliveries will need to be developed for the Internet to be really practical for everyday purchases. We'll return to this issue at the end of the chapter. For now, though, we should note that a large number of people are working on that problem. Some firms have developed partial solutions. For example, Tesco sells groceries from a website and delivers them within 24 hours. But other firms, like Webvan, have collapsed under the problems of trying to do that in a way that satisfies consumers' needs.

Many established retailers, like Barnes & Noble, are trying to figure out how to combine "clicks and mortar" to meet consumers' needs better than would be possible with only an online website or only a store.

Another possible set of costs occurs if a product must be returned. That, of course, assumes you get what you order. The Internet is the ultimate weapon for fly-by-night operators. Fraud is already a big problem.

Competitive effects will influence other retailers

Retailers of every description are experimenting with selling on the Internet. They range from department stores like Bloomingdale's and Dillard's to discounters like Target and Wal-Mart to limited-line retailers like Virtual Vineyards (wine) and the Disney Store (apparel, toys) to service providers like American Express and FTD (flower deliveries). You can even buy virtual underwear from Joe Boxer.

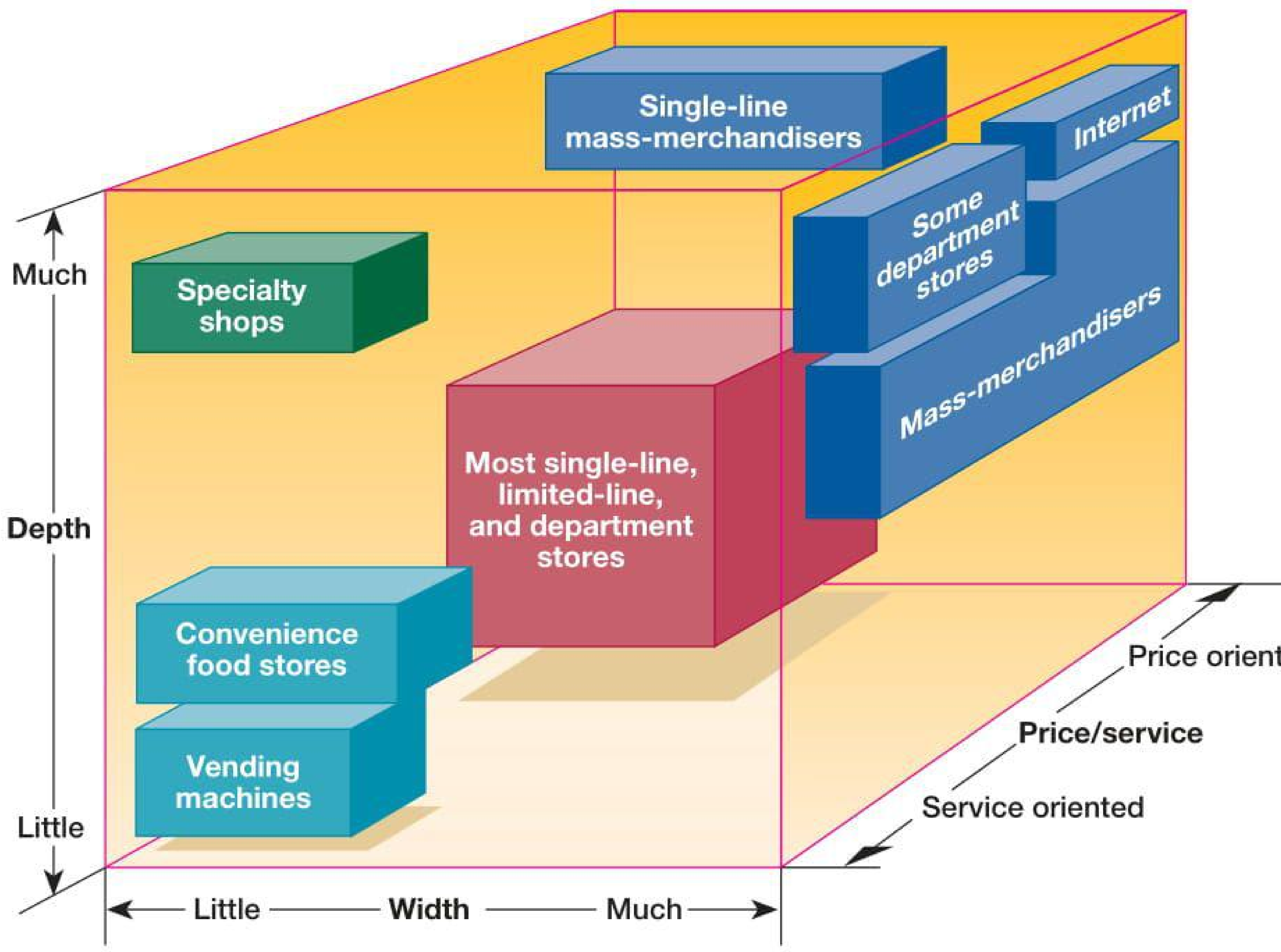
None of these retailers knows what will come of Internet selling. And some of the initial results have been surprises. For example, many orders on Wal-Mart's website are from U.S. citizens who are in the military overseas. Regardless of surprises, retailers need to work to understand the longer-term impact Internet selling will have on their market. In retailing, as new formats and concepts are refined, they often quickly have an impact on existing companies. It is very likely that the Internet will do just that, as it has already done with many types of wholesaling.[20]

Retailing Types Are Explained by Consumer Needs Filled

We've talked about many different types of retailers and how they evolved. Earlier, we noted that no single characteristic provided a good basis for classifying all retailers. Now it helps to see the three-dimensional view of retailing presented in Exhibit 13-3. It positions different types of retailers in terms of three consumer-oriented dimensions: (1) width of assortment desired, (2) depth of assortment desired, and (3) a price/service combination. Price and service are combined because they are often indirectly related. Services are costly to provide. So a retailer that wants to emphasize low prices usually has to cut some services—and retailers with a lot of service must charge prices that cover the added costs.

We can position most existing retailers within this three-dimensional market diagram. Exhibit 13-3, for example, suggests the *why* of vending machines. Some

Exhibit 13-3 A Three-Dimensional View of the Market for Retail Facilities and the Probable Position of Some Present Offerings



people—in the front upper left-hand corner—have a strong need for a specific item and are not interested in width of assortment, depth of assortment, or price. Note where Internet retailers are placed in the diagram. Does that position make sense to you?

Why Retailers Evolve and Change

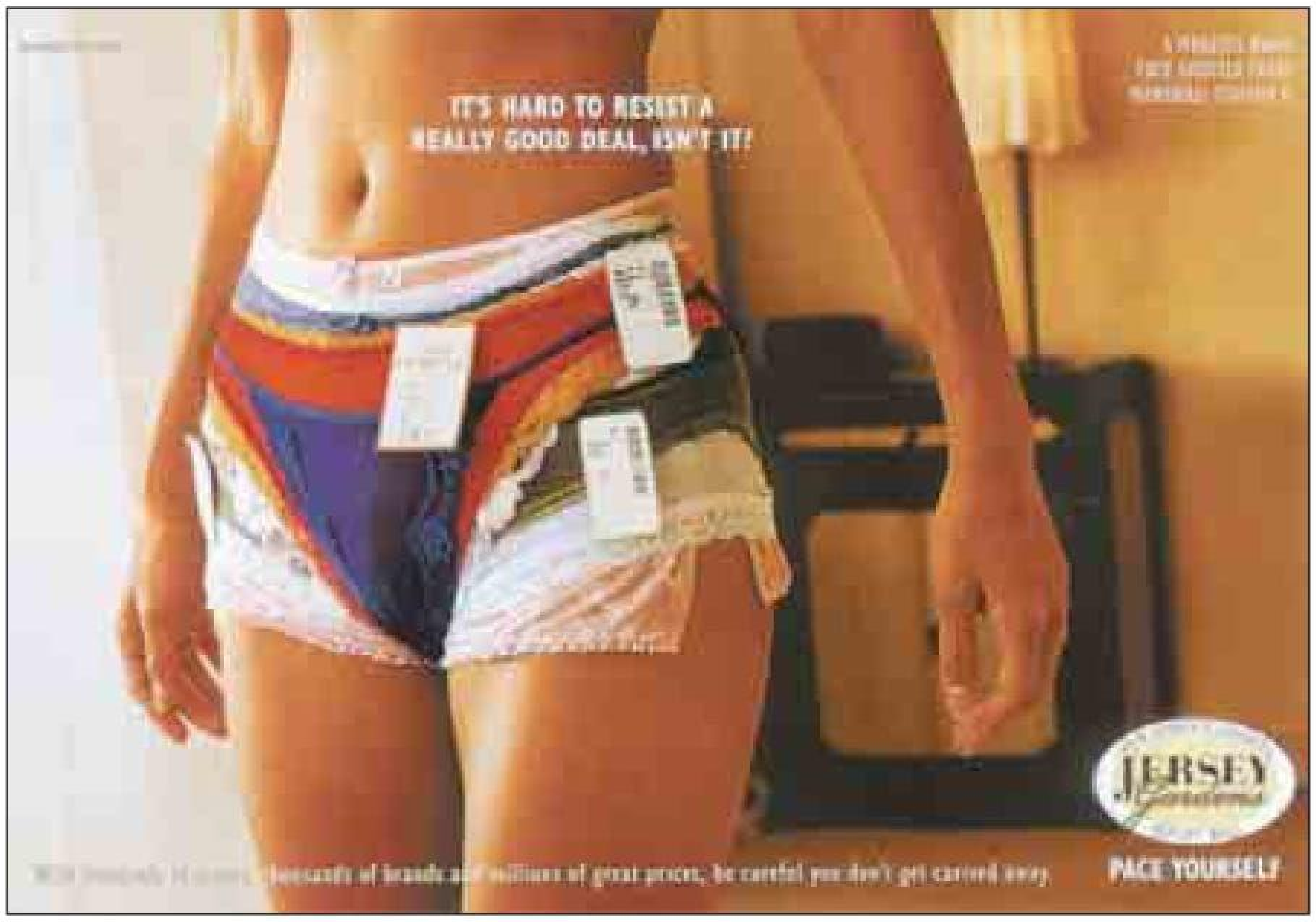
The wheel of retailing keeps rolling

The **wheel of retailing theory** says that new types of retailers enter the market as low-status, low-margin, low-price operators and then—if successful—evolve into more conventional retailers offering more services with higher operating costs and higher prices. Then they're threatened by new low-status, low-margin, low-price retailers—and the wheel turns again. Department stores, supermarkets, and mass-merchandisers went through this cycle.

The wheel of retailing theory, however, doesn't explain all major retailing developments. Vending machines entered as high-cost, high-margin operations. Convenience food stores are high-priced. Suburban shopping centers don't emphasize low price. Current retailers who are adding websites are likely to face competitors who cut operating expenses even deeper.

Scrambled merchandising—mixing product lines for higher profits

Conventional retailers tend to specialize by product line. But most modern retailers are moving toward **scrambled merchandising**—carrying any product lines they think they can sell profitably. Supermarkets and drugstores sell anything they can move in volume—panty hose, phone cards, one-hour photo processing, motor oil, potted plants, and computer software. Mass-merchandisers don't just sell everyday items but also cellular phones, computer printers, and jewelry.[21]



Some manufacturers have always had outlet stores near their factories, but outlet malls are emerging as a new retailing format that is popular with some consumers.

Product life cycle concept applies to retailer types too

We've seen that consumers' needs help explain why some kinds of retailers developed. But we can apply the product life cycle concept to understand this process better. A retailer with a new idea may have big profits—for a while. But if it's a really good idea, the retailer can count on speedy imitation and a squeeze on profits. Other retailers will copy the new format or scramble their product mix to sell products that offer them higher margins or faster turnover. That puts pressure on the original firm to change or lose its market.

Some conventional retailers are in decline as these life and death cycles continue. Recent innovators, like the Internet merchants, are still in the market growth stage. See Exhibit 13-4. Some retailing formats that are mature in the United States are only now beginning to grow in other countries.

Exhibit 13-4
Retailer Life Cycles—Timing and Years to Market Maturity

Ethical issues may arise

Most retailers face intense competitive pressure. The desperation that comes with such pressure has pushed some retailers toward questionable marketing practices.

Critics argue, for example, that retailers too often advertise special sale items to bring price-sensitive shoppers into the store or to a website but then don't stock enough to meet demand. Other retailers are criticized for pushing consumers to trade up to more expensive items. What is ethical and unethical in situations like these, however, is subject to debate. Retailers can't always anticipate demand perfectly, and deliveries may not arrive on time. Similarly, trading up may be a sensible part of a strategy—if it's done honestly.

In retailing, as in other types of business, the marketing concept should guide firms away from unethical treatment of customers. However, a retailer on the edge of going out of business may lose perspective on the need to satisfy customers in both the short and the long term.[22]

Retailer Size and Profits

A few big retailers do most of the business

The large number of retailers (1,113,137) might suggest that retailing is a field of small businesses. To some extent this is true. As shown in Exhibit 13-5, when the last census of retailers was published over 62 percent of all the retail stores in the United States had annual sales of less than $1 million. But that's only part of the story. Those same retailers accounted for only about 10 cents of every $1 in retail sales!

The larger retail stores—those selling more than $5 million annually—do most of the business. Less than 10 percent of the retail stores are this big, yet they account for over 65 percent of all retail sales. Many small retailers are being squeezed out of business. On the other hand, they do reach many consumers and often are valuable channel members. But their large number and relatively small sales volume make working with them expensive. They often require separate marketing mixes.[23]

Big chains are building market clout

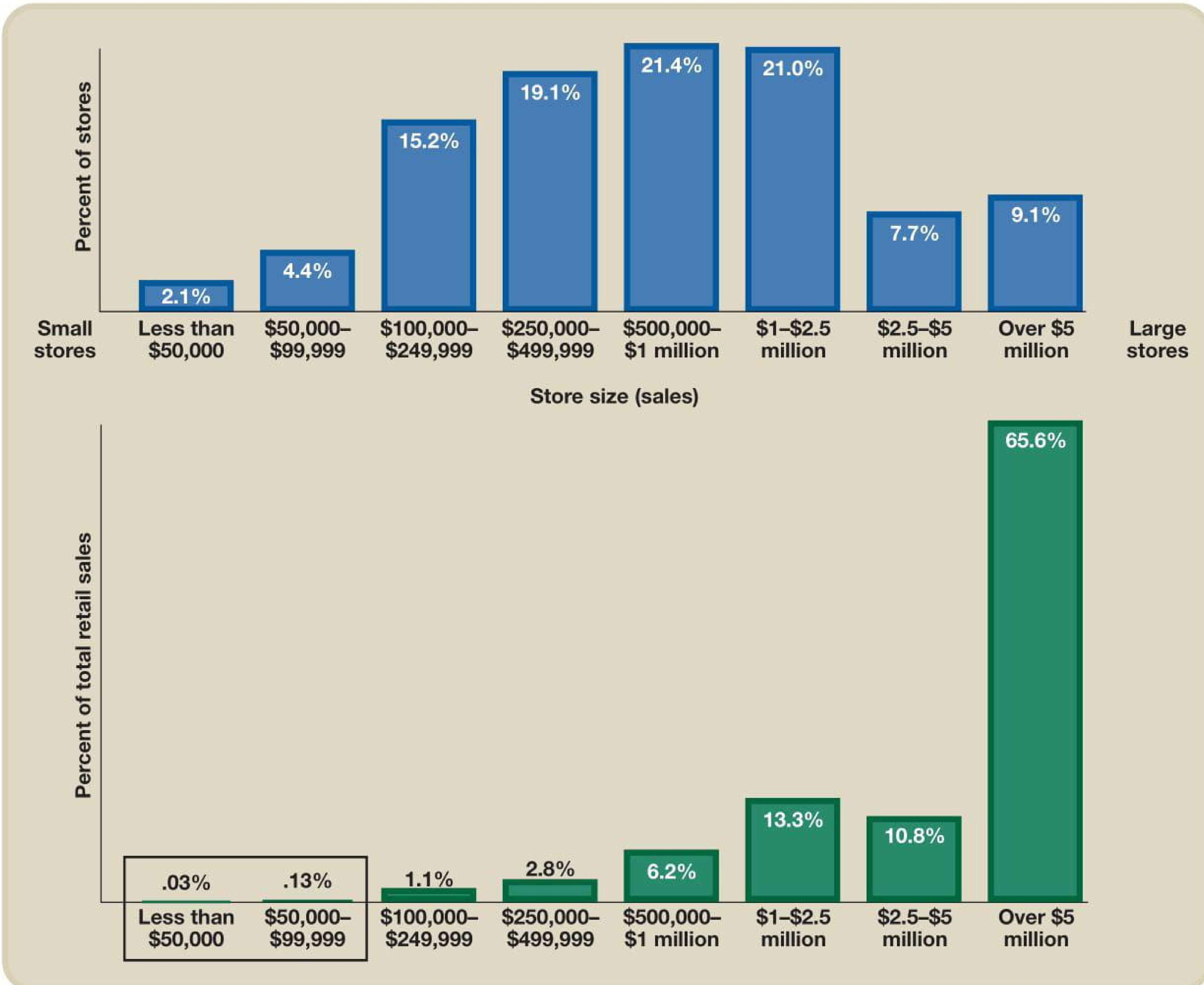
The main way for a retailer to achieve economies of scale is with a corporate chain. A **corporate chain** is a firm that owns and manages more than one store—and often it's many. Chains have grown rapidly and now account for about half of all retail sales. You can expect chains to continue to grow and take business from independent stores. The reason is simple: Size matters.

Large chains use central buying for different stores. This allows them to take advantage of quantity discounts or opportunities for vertical integration—including developing their own efficient distribution centers. They can use EDI and computer networks to control inventory costs and stock-outs. They may also spread promotion, information technology, and management costs to many stores. Retail chains also have their own dealer brands. Many of these chains are becoming powerful members—or channel captains—in their channel systems. In fact, the most successful of these big chains—like Home Depot and Wal-Mart—control access to so many consumers that they have the clout to dictate almost every detail of relationships with their suppliers.[24]

Independents form chains too

Competitive pressure from corporate chains encouraged the development of both cooperative chains and voluntary chains. **Cooperative chains** are retailer-sponsored groups—formed by independent retailers—that run their own buying organizations and conduct joint promotion efforts. Cooperative chains face a tough battle. Some, like True Value Hardware, are still adapting as they identify the weakness of corporate chains. For example, ads remind consumers that they don't need to waste a half-hour lost in a big store to pick up some simple item.

Exhibit 13-5 Distribution of Stores by Size and Share of Total U.S. Retail Sales



Voluntary chains are wholesaler-sponsored groups that work with "independent" retailers. Some are linked by contracts stating common operating procedures and requiring the use of common storefront designs, store names, and joint promotion efforts. Examples include SuperValu in groceries and Ace in hardware.

Franchisors form chains too

In a **franchise operation,** the franchisor develops a good marketing strategy, and the retail franchise holders carry out the strategy in their own units.

The franchisor acts like a voluntary chain operator—or a producer. Each franchise holder benefits from its relationship with the larger company and its experience, buying power, promotion, and image. In return, the franchise holder usually signs a contract to pay fees and commission and to strictly follow franchise rules designed to continue the successful strategy. Voluntary chains tend to work with existing retailers, while some franchisors like to work with, and train, newcomers. For newcomers, a franchise often reduces the risk of starting a new business. Only about 5 percent of new franchise operations fail in the first few years—compared to about 70 percent for other new retailers.

Franchise holders' sales have grown fast and now account for about half of all retail sales. One reason is that franchising is especially popular with service retailers, a fast-growing sector of the economy. You can expect more growth in franchising, but the rate will be slower than during the last 20 years.[25]

Differences in Retailing in Different Nations

New ideas spread across countries

New retailing approaches that succeed in one part of the world are often quickly adapted to other countries. Self-service approaches that started with supermarkets in the United States are now found in retail operations worldwide. Similarly, mass-merchandising approaches are popular in many countries. In 1969, for example, Kmart entered into a joint venture with Australia's largest department store chain to pioneer mass-merchandising there. The supercenter concept, on the other hand, initially developed in Europe.

Mass-merchandising requires mass markets

The low prices, selections, and efficient operations offered by mass-merchandisers and other large chains might be attractive to consumers everywhere. But consumers in less-developed nations often don't have the income to support mass distribution. The small shops that survive in these economies sell in very small quantities, often to a small number of consumers.

Consumer cooperatives are popular in some countries

Retailing in the United States is more diverse than in most other countries. Even so, some retailing formats, notably consumer cooperatives, are more prominent in other countries. Switzerland's Migros is the most successful example. Its stores—ranging from supermarkets to appliance centers—account for 16 percent of Swiss retail sales.[26]

Some countries block change

The political and legal environment severely limits the evolution of retailing in some nations. Japan is a prime example. For years its Large Store Law—aimed at protecting the country's politically powerful small shopkeepers—has been a real barrier to retail change. The law restricts development of large stores by requiring special permits, which are routinely denied.

Japan is taking steps to change the Large Store Law. One such change allowed Toys "R" Us to move into the Japanese market. Even so, most experts believe that it will be years before Japan moves away from its system of small, limited-line shops. To put this in perspective, a typical "mom and pop" grocery store in Japan is only about 250 square feet. The inefficiency of that retail distribution system is an important reason why Japanese consumers pay very high prices for consumer products. Many countries in other parts of Asia and South America impose similar restrictions. On the other hand, the European Union is prompting member countries to drop such rules and let competition determine what types of retailing will give customers superior value.

Some mass-merchandiser chains, like Tesco in the U.K., are looking for growth by opening small stores—which will put even more pressure on conventional retailers.

Retailing may not have moved as fast in other parts of the world as it has in the U.S., but change is coming. And in these other countries, retailers who cannot adapt with new strategies will be passed over by those who do.[27]

What Is a Wholesaler?

It's hard to define what a wholesaler is because there are so many different wholesalers doing different jobs. Some of their activities may even seem like manufacturing. As a result, some wholesalers describe themselves as "manufacturer and dealer." Some like to identify themselves with such general terms as *merchant, jobber, dealer,* or *distributor.* And others just take the name commonly used in their trade—without really thinking about what it means.

To avoid a long technical discussion on the nature of wholesaling, we'll use the U.S. Bureau of the Census definition:

Wholesaling is concerned with the *activities* of those persons or establishments that sell to retailers and other merchants, and/or to industrial, institutional, and commercial users, but that do not sell in large amounts to final consumers.

So **wholesalers** are firms whose main function is providing wholesaling activities. Wholesalers sell to all of the different types of organizational customers shown in Exhibit 7-1.

Wholesaling activities are just variations of the basic marketing functions—gathering and providing information, buying and selling, grading, storing, transporting, financing, and risk taking—we discussed in Chapter 1. You can understand wholesalers' strategies better if you look at them as members of channels. They add value by doing jobs for their customers and for their suppliers. In Chapter 11, we considered some of the ways they provide value when we discussed why a producer might want to use indirect distribution and include an intermediary in the channel. Now we'll develop these ideas in more detail.

Wholesaling Is Changing with the Times

A hundred years ago wholesalers dominated distribution channels in the United States and most other countries. The many small producers and small retailers needed their services. This situation still exists in many countries, especially those with less-developed economies. However, in the developed nations, as producers became larger many bypassed the wholesalers. Similarly, large retail chains often take control of functions that had been handled by wholesalers. Now e-commerce is making it easier for producers and consumers to "connect" without having a wholesaler in the middle of the exchange. In light of these changes, many people have predicted a gloomy future for wholesalers.

There certainly is reason to expect the worst for some types of wholesalers. With all the changes taking place, one could assume that wholesaling won't adapt fast enough. In the 1970s and 1980s that seemed to be the pattern. Now, however, rapid changes are underway. Even big changes are not always visible to consumers because they're hidden in the channel. But many wholesalers are adapting rapidly and finding new ways to add value in the channel. For example, some of the biggest B2B e-commerce sites on the Internet are wholesaler operations.

Producing profits, not chasing orders

Partly due to new management and new strategies, many wholesalers are enjoying significant growth. You saw a good example of this in the opening case

Many modern wholesalers are adopting new technologies to become more effective. For example, CrossLink's satellite communication system tracks the temperature of refrigerated deliveries and notifies the central office if there is any risk that products will be spoiled.

in Chapter 11. Progressive wholesalers are becoming more concerned with their customers and with channel systems. Many are using technology to offer better service. Others develop voluntary chains that bind them more closely to their customers.

Modern wholesalers no longer require all customers to pay for all the services they offer simply because certain customers use them. Many offer a basic service at minimum cost—then charge additional fees for any special services required.

Most modern wholesalers have streamlined their operations to cut unnecessary costs and improve profits. In fact, wholesalers pioneered many of the recent logistics innovations we discussed in Chapter 12. They use computers to track inventory and reorder only when it's really needed. Computerized sales analysis helps them identify and drop unprofitable products and customers. This sometimes leads to a selective distribution policy—when it's unprofitable to build relationships with too many small customers. Then they can fine-tune how they add value for their profitable customers.

Progress—or fail

Many wholesalers are also modernizing their warehouses and physical handling facilities. They mark products with bar codes that can be read with hand-held scanners—so inventory, shipping, and sales records can be easily and instantly updated. Computerized order-picking systems speed the job of assembling orders. New storing facilities are carefully located to minimize the costs of both incoming freight and deliveries. Delivery vehicles travel to customers in a computer-selected sequence that reduces the number of miles traveled. And wholesalers who serve manufacturers are rising to the challenge of just-in-time delivery.

Perhaps good-bye to some

Not all wholesalers are progressive, and some less efficient ones will fail. Efficiency and low cost, however, are not all that's needed for success. Some wholesalers will disappear as the functions they provided in the past are shifted and shared in different ways in the channel. Cost-conscious buyers for Wal-Mart, Lowe's, and other chains are refusing to deal with some of the middlemen who represent small producers. They want to negotiate directly with the producer—not just accept the wholesaler's price. Similarly, more producers see advantages in having closer direct relationships with fewer suppliers—and they're paring out weaker vendors. Efficient delivery services like UPS and Federal Express are also making it easy and inexpensive for many producers to ship directly to their customers—even ones in foreign markets. The Internet is putting pressure on wholesalers whose primary role is providing information to bring buyers and sellers together.[28]

Is it an ethical issue?

All of this is squeezing some wholesalers out of business. Some critics—including many of the wounded wholesalers—argue that it's unethical for powerful suppliers or customers to simply cut out wholesalers who spend money and time, perhaps decades, developing markets. Contracts between channel members and laws sometimes define what is or is not legal. But the ethical issues are often more ambiguous.

For example, as part of a broader effort to improve profits, Amana notified Cooper Distributing Co. that it intended to cancel their distribution agreement in 10 days. Cooper had been handling Amana appliances for 30 years, and Amana products represented 85 percent of Cooper's sales. Amana's explanation to Cooper? "It's not because you're doing a bad job: We just think we can do it better."

Situations like this arise often. They may be cold-hearted, but are they unethical? We argue that it isn't fair to cut off the relationship with such short notice. But most wholesalers realize that their business is *always* at risk—if they don't perform channel functions better or cheaper than what their suppliers or customers can do themselves.[29]

Survivors will need effective strategies

To survive, each wholesaler must develop a good marketing strategy. Profit margins are not large in wholesaling—typically ranging from less than 1 percent to 2 percent. And they've declined as the competitive squeeze has tightened.

The wholesalers who do survive will need to be efficient, but that doesn't mean they'll all have low costs. Some wholesalers' higher operating expenses result from the strategies they select—including the special services they offer to *some* customers.

Wholesalers Add Value in Different Ways

Exhibit 13-6 compares the number, sales volume, and operating expenses of some major types of wholesalers. The differences in operating expenses suggest that each of these types performs, or does not perform, certain wholesaling functions. But which ones and why? And why do manufacturers use merchant wholesalers—costing 14.1 percent of sales—when agent middlemen cost only 4.2 percent?

Exhibit 13-6 U.S. Wholesale Trade by Type of Wholesale Operation

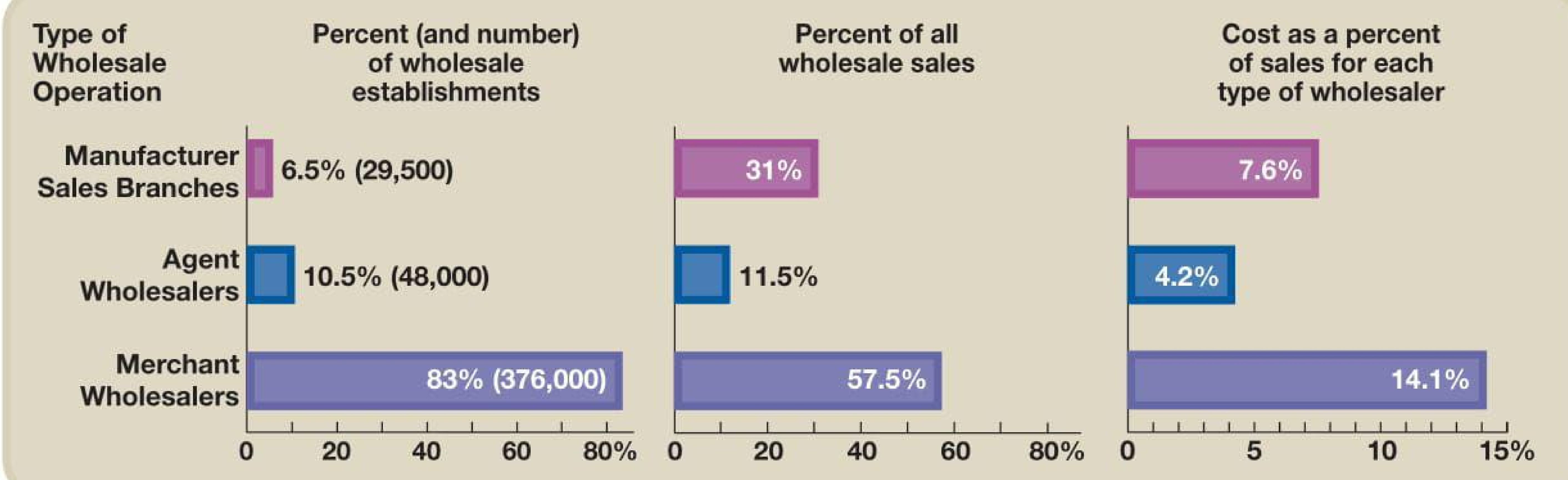
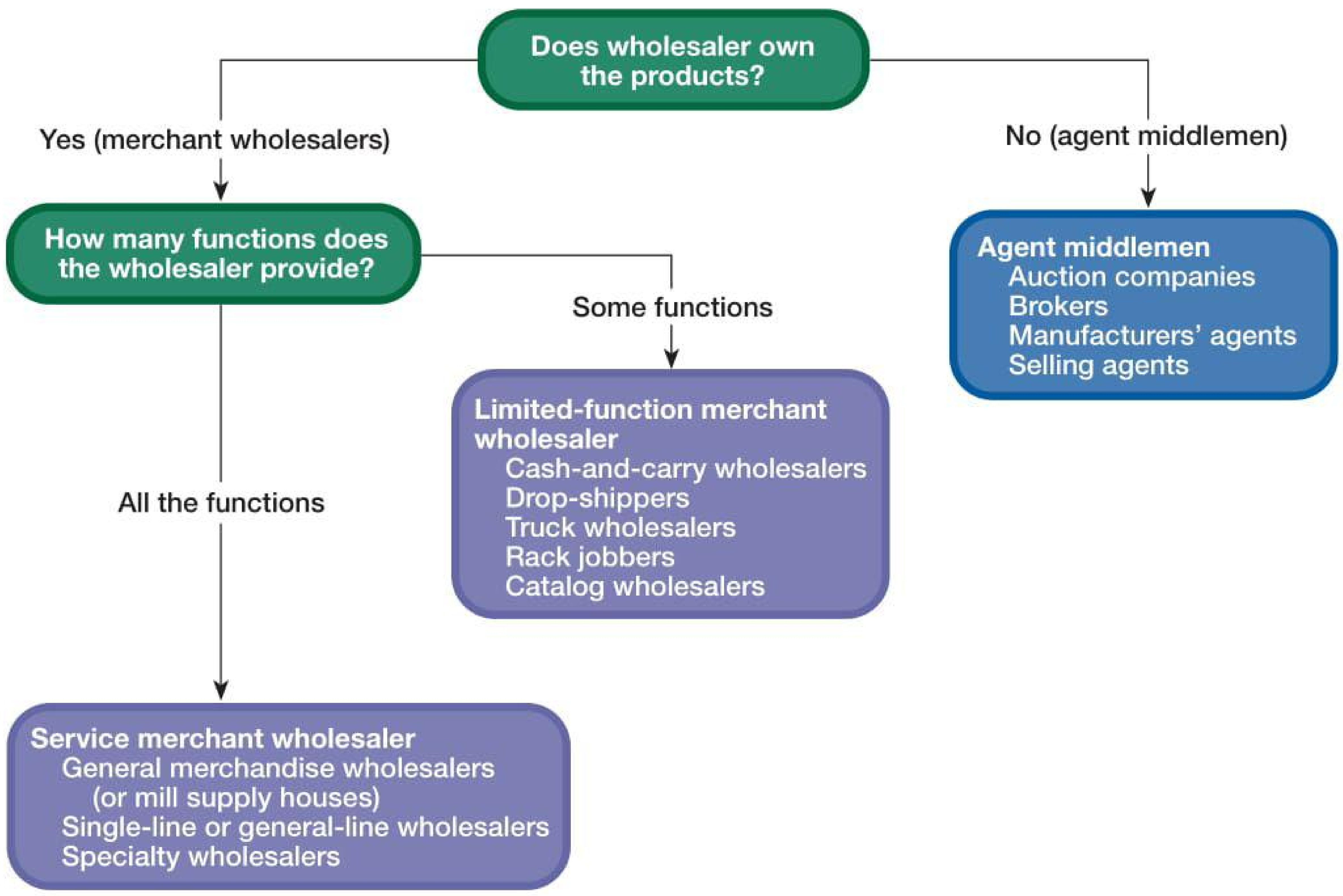


Exhibit 13-7 Types of Wholesalers



To answer these questions, we must understand what these wholesalers do and don't do. Exhibit 13-7 gives a big-picture view of the major types of wholesalers we'll be discussing. There are lots more specialized types, but our discussion will give you a sense of the diversity. Note that a major difference between merchant and agent wholesalers is whether they *own* the products they sell. Before discussing these wholesalers, we'll briefly consider producers who handle their own wholesaling activities.

Manufacturers' sales branches are considered wholesalers

Manufacturers who just take over some wholesaling activities are not considered wholesalers. However, when they set up **manufacturers' sales branches**—warehouses that producers set up at separate locations away from their factories—these establishments basically operate as wholesalers. In fact, they're classified as wholesalers by the U.S. Census Bureau and by government agencies in many other countries.

In the United States, these manufacturer-owned branch operations account for about 6.5 percent of wholesale facilities—but they handle 31 percent of total wholesale sales. One reason sales per branch are so high is that the branches are usually placed in the best market areas. This also helps explain why their operating costs, as a percent of sales, are often lower. Another reason is that coordination is easier within a single firm. Manufacturers can more quickly set up efficient network systems for sharing information and logistics functions with their own branch operations than with independent wholesalers.[30]

Merchant Wholesalers Are the Most Numerous

Merchant wholesalers own (take title to) the products they sell. They often specialize by certain types of products or customers. For example, Fastenal is a wholesaler that specializes in distributing threaded fasteners used by a variety of manufacturers. It owns (takes title to) the fasteners for some period before selling to

Merchant wholesalers in Africa are often smaller, carry narrower product lines, and deal with fewer customers than their counterparts in North America.

its customers. If you think all merchant wholesalers are fading away, Fastenal is proof that they can serve a needed role. In the last decade Fastenal's profits have grown at about the same pace as Microsoft's.

Internet

Internet Exercise Check out the different aspects of the Fastenal website (www.fastenal.com). Give examples of ways that the website is intended to help Fastenal's customers and suppliers.

Exhibit 13-6 shows that over 80 percent of the wholesaling establishments in the United States are merchant wholesalers—and they handle over 57 percent of wholesale sales. Merchant wholesalers are even more common in other countries. Japan is an extreme example. In its unusual multitiered distribution system, products are often bought and sold by a series of merchant wholesalers on their way to the business user or retailer.[31]

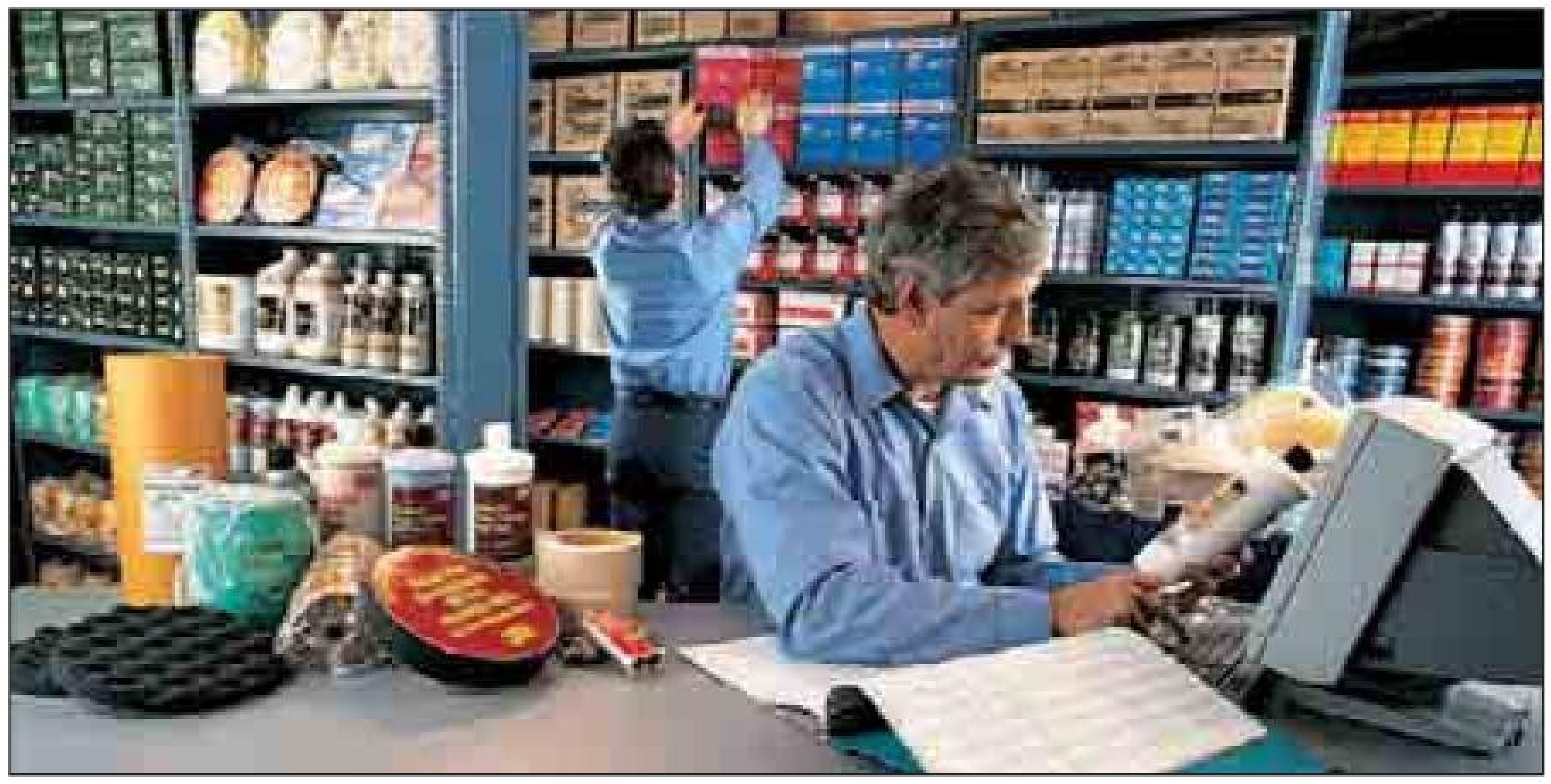
Service wholesalers provide all the functions

Service wholesalers are merchant wholesalers who provide all the wholesaling functions. Within this basic group are three types: (1) general merchandise, (2) single-line, and (3) specialty.

General merchandise wholesalers are service wholesalers who carry a wide variety of nonperishable items such as hardware, electrical supplies, plumbing supplies, furniture, drugs, cosmetics, and automobile equipment. With their broad line of convenience and shopping products, they serve hardware stores, drugstores, and small department stores. *Mill supply houses* operate in a similar way, but they carry a broad variety of accessories and supplies to serve the needs of manufacturers.

Single-line (or general-line) wholesalers are service wholesalers who carry a narrower line of merchandise than general merchandise wholesalers. For example, they might carry only food, apparel, or certain types of industrial tools or supplies. In consumer products, they serve the single- and limited-line stores. In business products, they cover a wider geographic area and offer more specialized service.

Specialty wholesalers are service wholesalers who carry a very narrow range of products and offer more information and service than other service wholesalers. A consumer products specialty wholesaler might carry only health foods or oriental foods instead of a full line of groceries. Some limited-line and specialty wholesalers are growing by helping independent retailer-customers find better ways to compete



3M produces 1,600 products that are used by auto body repair shops in the U.S., Europe, Japan, and other countries. To reach this target market, 3M works with hundreds of specialty wholesalers.

with mass-merchandisers. But in general, many consumer-products wholesalers have been hit hard by the growth of retail chains that set up their own distribution centers and deal directly with producers.

A specialty wholesaler of business products might limit itself to fields requiring special technical knowledge or service. Richardson Electronics is an interesting example. It specializes in distributing replacement parts, such as electron tubes, for old equipment that many manufacturers still use on the factory floor. Richardson describes itself as "on the trailing edge of technology," but its unique products, expertise, and service are valuable to its target customers. Many of its customers operate in countries where new technologies are not yet common, but Richardson gives them easy access to information from its website (www.rell.com) and makes its products available quickly by stocking them in locations around the world.[32]

Limited-function wholesalers provide some functions

Limited-function wholesalers provide only *some* wholesaling functions. In the following paragraphs, we briefly discuss the main features of these wholesalers. Although less numerous in some countries, these wholesalers are very important for some products.

Cash-and-carry wholesalers want cash

Cash-and-carry wholesalers operate like service wholesalers—except that the customer must pay cash. In the U.S., big warehouse clubs have taken much of this business. But cash-and-carry operators are common in less-developed nations where very small retailers handle the bulk of retail transactions. Full-service wholesalers often refuse to grant credit to small businesses that may have trouble paying their bills.

Drop-shippers do not handle the products

Drop-shippers own (take title to) the products they sell—but they do *not* actually handle, stock, or deliver them. These wholesalers are mainly involved in selling. They get orders and pass them on to producers. Then the producer ships the order directly to the customer. Drop-shippers commonly sell bulky products (like lumber) for which additional handling would be expensive and possibly damaging. Drop-shippers in the U.S. are already feeling the squeeze from buyers and sellers connecting directly via the Internet. But the progressive ones are fighting back by setting up their own websites and getting fees for referrals.

Truck wholesalers deliver—at a cost

Truck wholesalers specialize in delivering products that they stock in their own trucks. By handling perishable products in general demand—tobacco, candy, potato chips, and salad dressings—truck wholesalers may provide almost the same functions as full-service wholesalers. Their big advantage is that they promptly deliver perishable products that regular wholesalers prefer not to carry. A 7-Eleven store that runs out of potato chips on a busy Friday night doesn't want to be out of stock all weekend! They help retailers keep a tight rein on inventory, and they seem to meet a need.

Rack jobbers sell hard-to-handle assortments

Rack jobbers specialize in hard-to-handle assortments of products that a retailer doesn't want to manage—and rack jobbers usually display the products on their own wire racks. For example, a grocery store or mass-merchandiser might rely on a rack jobber to decide which paperback books or magazines it sells. The wholesaler knows which titles sell in the local area and applies that knowledge in many stores. Historically, rack jobbers were paid cash for what sold or was delivered. Now that they are working with big chains, they've joined other wholesalers in waiting until the "accounts receivables" are paid at the end of the month.

Catalog wholesalers reach outlying areas

Catalog wholesalers sell out of catalogs that may be distributed widely to smaller industrial customers or retailers who might not be called on by other middlemen. Customers place orders at a website or by mail, e-mail, fax, or telephone. These wholesalers sell lines such as hardware, jewelry, sporting goods, and computers. For example, Inmac uses a printed catalog and a website (www.inmac.com) to sell a complete line of computer accessories. Inmac's catalogs are printed in six languages and distributed to business customers in the U.S., Canada, and Europe. Many of these customers don't have a local wholesaler, but they can place orders from anywhere in the world. Most catalog wholesalers quickly adapted to the Internet. It fits what they were already doing and makes it easier. But they're facing more competition too; the Internet allows customers to compare prices from more sources of supply.[33]

Agent Middlemen Are Strong on Selling

They don't own the products

Agent middlemen are wholesalers who do *not* own the products they sell. Their main purpose is to help in buying and selling. Agent middlemen normally specialize by customer type and by product or product line. But they usually provide even fewer functions than the limited-function wholesalers. They operate at relatively low cost—sometimes 2 to 6 percent of their selling price—or less in the case of website-based agents who simply bring buyers and sellers together. Worldwide, the role of agent middlemen is rapidly being transformed by the Internet. Those who didn't get on board this fast-moving train were left behind.

They are important in international trade

Agent middlemen are common in international trade. Many markets have only a few well-financed merchant wholesalers. The best many producers can do is get local representation through agents and then arrange financing through banks that specialize in international trade.

Agent middlemen are usually experts on local business customs and rules concerning imported products in their respective countries. Sometimes a marketing manager can't work through a foreign government's red tape without the help of a local agent.

Manufacturers' agents—free-wheeling sales reps

A **manufacturers' agent** sells similar products for several noncompeting producers—for a commission on what is actually sold. Such agents work almost as members of each company's sales force—but they're really independent middlemen. More than half of all agent middlemen are manufacturers' agents.

Their big plus is that they already call on some customers and can add another product line at relatively low cost—and at no cost to the producer until something sells! If an area's sales potential is low, a company may use a manufacturers' agent

Innovative wholesalers are using multilingual bar codes to reduce costs and errors in overseas markets.

because the agent can do the job at low cost. Small producers often use agents everywhere because their sales volume is too small to justify their own sales force.

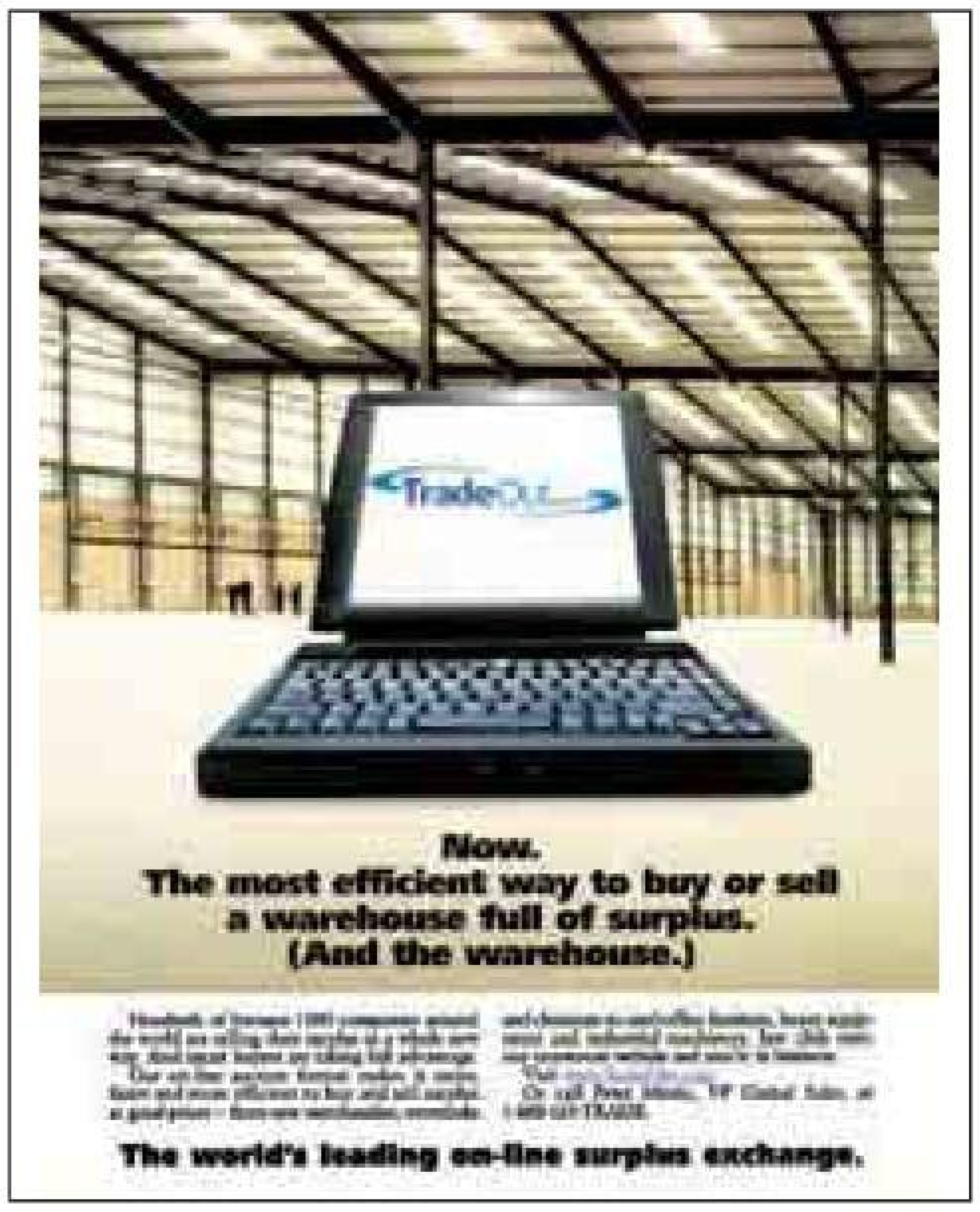
Agents can be especially useful for introducing new products. For this service, they may earn 10 to 15 percent commission. (In contrast, their commission on large-volume established products may be quite low—perhaps only 2 percent.) A 10 to 15 percent commission rate may seem small for a new product with low sales. Once a product sells well, however, a producer may think the rate is high and begin using its own sales reps. Agents are well aware of this possibility. That's why most try to work for many producers and avoid being dependent on only one line.

Manufacturers' agents may cover a very narrow geographic area, such as a city or state. However, they are also very important in international marketing, and an agent may take on responsibility for a whole country. **Export or import agents** are basically manufacturers' agents who specialize in international trade. These agent middlemen operate in every country and help international firms adjust to unfamiliar market conditions in foreign markets.

Manufacturers' reps will continue to play an important role in businesses that need an agent to perform order-getting tasks. But manufacturers' reps everywhere are feeling pressure when it comes to routine business contacts. More producers are turning to telephone selling, websites, e-mail, teleconferencing, and faxes to contact customers directly. This hits these agents where it hurts.[34]

Brokers provide information

Brokers bring buyers and sellers together. Brokers usually have a *temporary* relationship with the buyer and seller while a particular deal is negotiated. They are especially useful when buyers and sellers don't come into the market very often. The broker's product is information about what buyers need and what supplies are available. They may also aid in buyer-seller negotiation. If the transaction is completed, they earn a commission from whichever party hired them. **Export and import brokers** operate like other brokers, but they specialize in bringing together buyers and sellers from different countries. Smart brokers quickly saw new opportunities to



A few years ago wholesale brokers typically focused on a few specialized product categories, but now online brokers are finding markets for almost every sort of product.

expand their reach by using the Internet. As the Internet causes consolidation, it will also provide more value. A smaller number of cyber-brokers will cut costs and dominate the business with larger databases of buyers and sellers.

Selling agents—almost marketing managers

Selling agents take over the whole marketing job of producers—not just the selling function. A selling agent may handle the entire output of one or more producers—even competing producers—with almost complete control of pricing, selling, and advertising. In effect, the agent becomes each producer's marketing manager.

Financial trouble is one of the main reasons a producer calls in a selling agent. The selling agent may provide working capital but may also take over the affairs of the business. But selling agents also work internationally. A **combination export manager** is a blend of manufacturers' agent and selling agent—handling the entire export function for several producers of similar but noncompeting lines.

Auction companies—speed up the sale

Auction companies provide a place where buyers and sellers can come together and bid to complete a transaction. There aren't many auction companies. Traditionally they have been important in certain lines—such as livestock, fur, tobacco, and used cars. For these products, demand and supply conditions change rapidly—and the product must be seen to be evaluated. The auction company brings buyers and sellers together. Buyers inspect the products—then demand and supply interact to determine the price.

Aucnet is a good example of a progressive auction company that put the bid process on the Internet. Its very successful used car auction runs from a website (www.aucnet.com). The key to its success is that it provides bidders with a very thorough online rating of the quality of each car. In the past, most auction companies said "What you see is what you get." Because the ratings add value and are credible, Aucnet attracts dealers from all over the country. That results in higher bid prices and better profits for Aucnet. But it also saves dealers the cost and hassle of going to smaller local auctions that don't have what they want. The Internet has spurred growth of all sorts of auction companies in lines of business where auctions have previously not been common.[35]

What Will Happen to Retailers and Wholesalers in the Future?

A common theme in this chapter—and the two before it—is that channels of distribution are in the midst of dynamic changes. There have been dramatic improvements due to more efficient ways to coordinate logistics. The Internet, as the backbone for e-commerce, is another force for change. But before all of this, the evolution of retailing and wholesaling was ongoing. Middlemen that find new and better ways to add value prosper. They find target segments that they serve very well by differentiating their services and doing something better than producers or customers can do without them.

It can't be overemphasized that such changes are ongoing. Clearly, we have just seen the tip of the iceberg when it comes to the impact that the Internet, and related technologies that will evolve in the future, will have on Place. There is an explosion in the number and variety of firms that are trying to figure out how to have a presence on the Web. Many of them are reshaping competition in the product-markets in which they compete.

On the other hand, the adoption process that is underway is typical of other innovations. Much of the initial change has simply been an adjustment to what was done in the past. The catalog becomes electronic. E-mail supplements toll-free phone orders. A retailer opens a new website instead of a new store. The technology is revolutionary and exciting, but much of what firms are doing with it so far is evolutionary. In time, revolutionary change will come and bring greater rewards to the innovators.

Imagine, for example, what it would take for you—and everyone you know—to do most of your routine shopping on the Internet. What new marketing functions would be needed, and who would provide them? What would the channel system look like? What new kind of intermediary will develop and what will it do? Let's consider one scenario.

After you surf the Internet and put products in your virtual shopping basket at one or more websites, what should happen next? Perhaps the seller would start by assembling your items in a carton with a bar code for your personal name, address, and account. Then that carton and cartons for all of the other orders that come into that website would be quickly taken in large economical batches to an intermediary. The computer-controlled sorting system going into the intermediary's 5-acre facility would scan each carton's bar code and route it to the sorting area for a truck that serves you and each of your neighbors. After a night of accumulating all the cartons that are directed to you from different sellers, the intermediary would place the cartons on a delivery vehicle in the right sequence so they can be efficiently unloaded as the truck passes each customer on its route. Of course, you're not home. With money you've saved by not running all over town burning gas you're off on a vacation; you have time to take off because day after day you're not waiting in traffic and checkout lines. Although you're not home, you have a special cabinet—with a lock activated by a bar code printed on the package—mounted to the side of your house where the delivery person leaves your purchases.[36]

This little drama may seem far-fetched today. But it, or something like it, probably isn't far off. Specialist-intermediaries will develop to make distribution *after* an Internet purchase more efficient, just as middlemen developed to make distribution more efficient *prior* to purchases in retail stores. What is described above isn't very different from what UPS does, one package at a time, when it makes deliveries from manufacturers to retailers. But the cost per package is much higher than it would be if everybody got deliveries everyday. It's like the difference between the cost of a special delivery and regular mail.

If the after-purchase distribution problem is handled, who will the seller be? Will the Internet merchants of tomorrow be an evolved form of the retailers of today? Or will current-day wholesalers be in a better position to catch that prize? Some wholesalers are already working with very large assortments. Or, in a world where you can conveniently surf from one specialized seller to another, will the breadth of assortment from any one seller be irrelevant? That could put producers in a stronger position. Perhaps none of these traditional forms of business will lead the way, but rather it will be a firm that is born on the Internet to meet customers' needs in a completely new and unique way. The answers to these questions will take time, but they are taking shape even as you read. Already new intermediaries are coming on the scene.

Let's admit it. You can only speculate about where e-commerce will lead. But perhaps it's good to speculate a little. The way markets work in the future will depend on people like you, and the creative innovations that you speculate about, study, analyze, and ultimately turn into profitable marketing strategies. The competition will be tough, but hopefully you're now on your way to being up to the challenge.

Conclusion

Modern retailing is scrambled—and we'll probably see more changes in the future. In such a dynamic environment, a producer's marketing manager must choose very carefully among the available kinds of retailers. And retailers must plan their marketing mixes with their target customers' needs in mind—while at the same time becoming part of an effective channel system.

We described many types of retailers—and we saw that each has its advantages and disadvantages. We also saw that modern retailers have discarded conventional practices. The old "buy low and sell high" philosophy is no longer a safe guide. Lower margins with faster turnover is the modern philosophy as more retailers move into mass-merchandising. But even this is no guarantee of success as retailers' life cycles move on.

Growth of chains and scrambled merchandising will continue as retailing evolves to meet changing consumer demands. But important breakthroughs are possible—perhaps with the Internet—and consumers probably will continue to move away from conventional retailers.

Wholesalers can provide functions for those both above and below them in a channel of distribution. These services are closely related to the basic marketing functions. There are many types of wholesalers. Some provide all the wholesaling functions—while others specialize in only a few. Eliminating wholesalers does not eliminate the need for the functions they now provide, but technology is helping firms to perform these functions in more efficient ways.

Merchant wholesalers are the most numerous and account for the majority of wholesale sales. Their distinguishing characteristic is that they take title to (own) products. Agent middlemen, on the other hand, act more like sales representatives for sellers or buyers—and they do not take title.

Despite dire predictions, wholesalers continue to exist. The more progressive ones are adapting to a changing environment. But some less progressive wholesalers will fail. The Internet is already taking its toll. On the other hand, new types of intermediaries are evolving. Some are creating new ways of helping producers and their customers achieve their objectives by finding new ways to add value.

Questions and Problems

1. What sort of a "product" are specialty shops offering? What are the prospects for organizing a chain of specialty shops?
2. Distinguish among discount houses, price-cutting by conventional retailers, and mass-merchandising. Forecast the future of low-price selling in food, clothing, and appliances. How will the Internet affect that future?

3. Discuss a few changes in the marketing environment that you think help to explain why telephone, mail-order, and Internet retailing have been growing so rapidly.
4. What are some advantages and disadvantages to using the Internet for shopping?
5. Apply the wheel of retailing theory to your local community. What changes seem likely? Will established retailers see the need for change, or will entirely new firms have to develop?
6. What advantages does a retail chain have over a retailer who operates with a single store? Does a small retailer have any advantages in competing against a chain? Explain your answer.
7. Many producers are now seeking new opportunities in international markets. Are the opportunities for international expansion equally good for retailers? Explain your answer.
8. Discuss how computer systems affect wholesalers' and retailers' operations.
9. Consider the evolution of wholesaling in relation to the evolution of retailing. List several changes that are similar, and several that are fundamentally different.
10. Do wholesalers and retailers need to worry about new-product planning just as a producer needs to have an organized new-product development process? Explain your answer.
11. How do you think a retailer of Maytag washing machines would react if Maytag set up a website, sold direct to consumers, and shipped direct from its distribution center? Explain your thinking.
12. What risks do merchant wholesalers assume by taking title to goods? Is the size of this risk about constant for all merchant wholesalers?
13. Why would a manufacturer set up its own sales branches if established wholesalers were already available?
14. What is an agent middleman's marketing mix?
15. Why do you think that many merchant middlemen handle competing products from different producers, while manufacturers' agents usually handle only noncompeting products from different producers?
16. What alternatives does a producer have if it is trying to expand distribution in a foreign market and finds that the best existing merchant middlemen won't handle imported products?
17. Discuss the future growth and nature of wholesaling if chains, scrambled merchandising, and the Internet continue to become more important. How will wholesalers have to adjust their mixes? Will wholesalers be eliminated? If not, what wholesaling functions will be most important? Are there any particular lines of trade where wholesalers may have increasing difficulty?

Suggested Cases

11. Runners World
14. Mixed Media Technologies, Inc.
15. Modern Horizons, Inc.
16. Morgan Company

Computer-Aided Problem

13. **Selecting Channel Intermediaries**

Art Glass Productions, a producer of decorative glass gift items, wants to expand into a new territory. Managers at Art Glass know that unit sales in the new territory will be affected by consumer response to the products. But sales will also be affected by which combination of wholesalers and retailers Art Glass selects. There is a choice between two wholesalers. One wholesaler, Giftware Distributing, is a merchant wholesaler that specializes in gift items; it sells to gift shops, department stores, and some mass-merchandisers. The other wholesaler, Margaret Degan & Associates, is a manufacturers' agent that calls on many of the gift shops in the territory.

Art Glass makes a variety of glass items, but the cost of making an item is usually about the same—$5.20 a unit. The items would sell to Giftware Distributing at $12.00 each—and in turn the merchant wholesaler's price to retailers would be $14.00—leaving Giftware with a $2.00 markup to cover costs and profit. Giftware Distributing is the only reputable merchant wholesaler in the territory, and it has agreed to carry the line only if

Art Glass is willing to advertise in a trade magazine aimed at retail buyers for gift items. These ads will cost $8,000 a year.

As a manufacturers' agent, Margaret Degan would cover all of her own expenses and would earn 8 percent of the $14.00 price per unit charged the gift shops. Individual orders would be shipped directly to the retail gift shops by Art Glass, using United Parcel Service (UPS). Art Glass would pay the UPS charges at an average cost of $2.00 per item. In contrast, Giftware Distributing would anticipate demand and place larger orders in advance. This would reduce the shipping costs, which Art Glass would pay, to about $.60 a unit.

Art Glass' marketing manager thinks that Degan would only be able to sell about 75 percent as many items as Giftware Distributing—since she doesn't have time to call on all of the smaller shops and doesn't call on any department stores. On the other hand, the merchant wholesaler's demand for $8,000 worth of supporting advertising requires a significant outlay.

The marketing manager at Art Glass decided to use a spreadsheet to determine how large sales would have to be to make it more profitable to work with Giftware and to see how the different channel arrangements would contribute to profits at different sales levels.

a. *Given the estimated unit sales and other values shown on the initial spreadsheet, which type of wholesaler would contribute the most profit to Art Glass Productions?*

b. *If sales in the new territory are slower than expected, so that the merchant wholesaler was able to sell only 3,000 units—or the agent 2,250 units—which wholesaler would contribute the most to Art Glass' profits? (Note: Assume that the merchant wholesaler only buys what it can sell; that is, it doesn't carry extra inventory beyond what is needed to meet demand.)*

c. *Prepare a table showing how the two wholesalers' contributions to profit compare as the quantity sold varies from 3,500 units to 4,500 units for the merchant wholesaler and 75 percent of these numbers for the manufacturers' agent. Discuss these results. (Note: Use the analysis feature to vary the quantity sold by the merchant wholesaler, and the program will compute 75 percent of that quantity as the estimate of what the agent will sell.)*

For additional questions related to this problem, see Exercise 13-4 in the *Learning Aid for Use with Basic Marketing*, 14th edition.

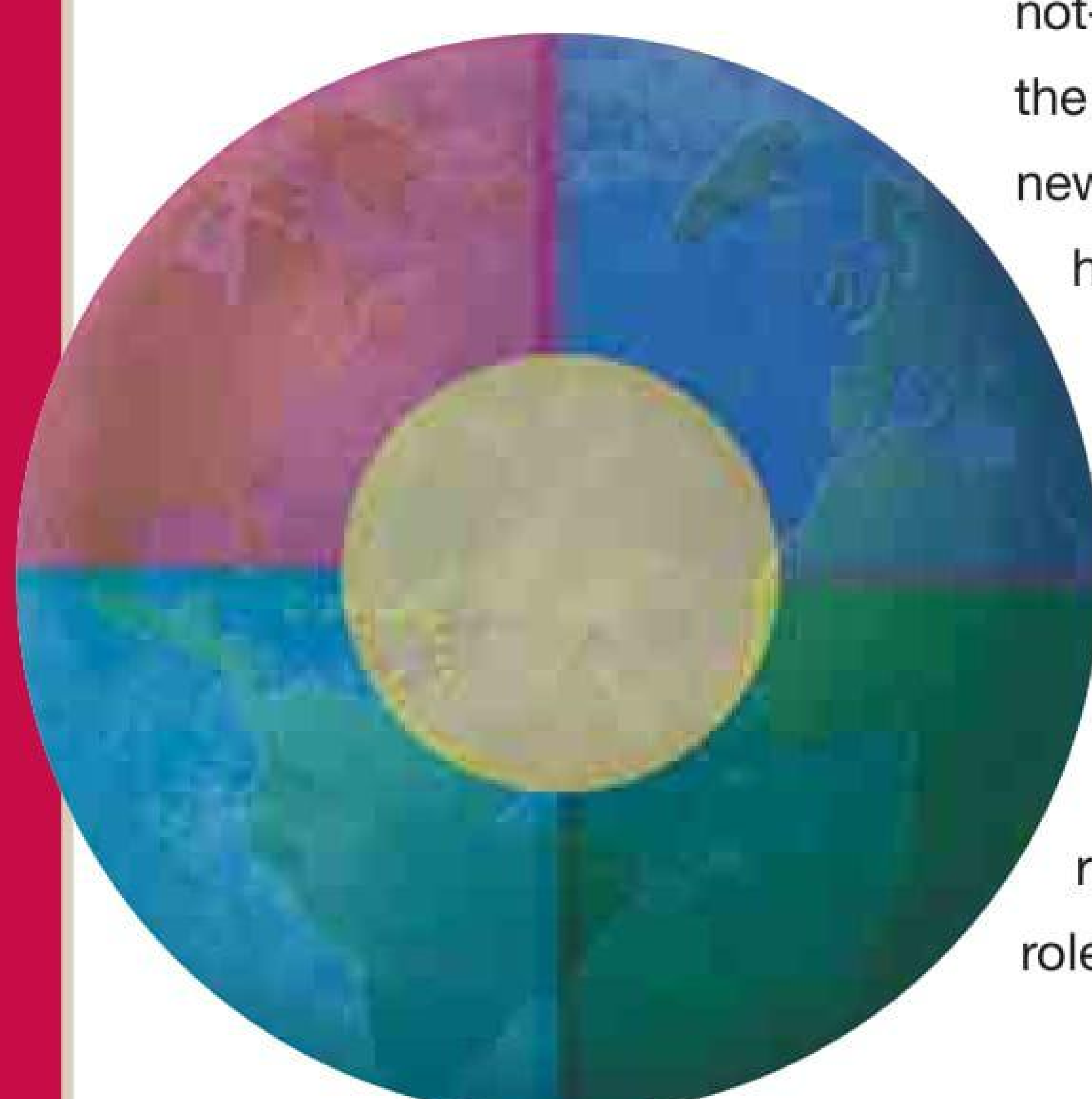
Chapter Fourteen

Promotion—Introduction to Integrated Marketing Communications

When You Finish This Chapter, You Should

1. Know the advantages and disadvantages of the promotion methods a marketing manager can use in strategy planning.
2. Understand the integrated marketing communications concept and why most firms use a blend of different promotion methods.
3. Understand the importance of promotion objectives.
4. Know how the communication process affects promotion planning.
5. Understand how direct-response promotion is helping marketers develop more targeted promotion blends.
6. Understand how new customer-initiated interactive communication is different.
7. Know how typical promotion plans are blended to get an extra push from middlemen and help from customers in pulling products through the channel.
8. Understand how promotion blends typically vary over the adoption curve and product life cycle.
9. Understand how to determine how much to spend on promotion efforts.
10. Understand the important new terms (shown in red).

Chrysler's new-product development team faced a challenge. They needed to come up with an exciting vehicle that would generate a lot of interest and draw consumers into Chrysler showrooms. The objective wasn't just to sell the new car but to get a positive halo that would improve the image and sales of other cars in the line. In addition, top management wanted the new design to cut costs and use capacity by sharing parts with other products—like the Dodge Neon, a not-so-popular economy sedan. By the way, Chrysler also wanted the new vehicle to qualify as a truck to help meet government gas mileage requirements for its truck line. That's a tall order, but out of this porridge came the idea for the PT Cruiser, a big marketing success.



The PT Cruiser's unique retro-look styling played a big role in generating baby-boomer

place price promotion produc

interest. And if the design was the bait, the interior is the hook. It's very flexible—with 26 different seat configurations, a flat cargo area, and easy hatchback access. The Cruiser really came across as something different—a "personal transportation" (PT) vehicle unlike any other small sedan or truck. But carefully planned promotion leveraged the whole PT strategy to earn more profit than was originally expected.

Chrysler marketers introduced a concept car version of the PT Cruiser at the 1999 Detroit Auto Show. To take advantage of the heavy news coverage the show generates, they also staged a surprise event to announce that a production version would be available for the 2000 model year. Immediately, the funky new car got free publicity in national news media that would have cost many millions of dollars. As the concept car made the car show circuit, it drew in large crowds and interested consumers registered to receive more information. Chrysler also ran teaser-type print ads. The simple ads showed a picture of the Cruiser and a big Chrysler logo. Simple copy positioned the Cruiser as "an antidote for the daily grind" and listed both a toll-free number and website for consumers to contact.

Before the car was even available, 225,000 people who had asked for more information were in the Cruiser direct-response promotion database. Chrysler sent these "hand raisers" a series of three mail brochures highlighting different benefits of the Cruiser and inviting them to visit a dealer. They were also invited to special previews to see the car in person. For example, 10 of these were scheduled at major sporting events and each attracted over 10,000 consumers in a single weekend. People hired to staff the previews were trained on the whole Chrysler line; they were ready to answer questions, refer consumers to local dealers, and get visitors started with interactive digital kiosks that provided in-depth multimedia promotion on every Chrysler model.

Chrysler marketers also worked on many other special sales promotions to build interest, prompt word of mouth among consumers, and encourage dealer visits. For instance, they offered consumers a $50 gift certificate to Macy's department store and promised to make charity contributions for each test drive.

By the time Cruisers were shipped from the factory, dealer sales reps had closed sales on almost all of the year's production capacity. Dealers couldn't even keep copies of promotional brochures in stock. In light of the overwhelming demand, Chrysler cut back on some of its planned spending for TV ads. It also had its agency's creative people change ads to put even more emphasis on the whole Chrysler line. Similarly, more ads targeted the West Coast, where Chrysler was having trouble selling against imports.

When Cruiser demand continued to grow for the 2001 model, Chrysler expanded production capacity and added a plant in Austria to serve the European market. It also raised price—especially on fancy options like heated seats—to improve margins and profits on units it was selling. And to take advantage of the investments in Cruiser development and promotion, and to keep the buzz going, Chrysler marketers added a new convertible for 2003 (www.chrysler.com/pt-cruiser).

While the promotion blend is selling Cruisers and pulling customers into dealerships, sales on the rest of the Chrysler line have not picked up. Alas, promotion can't carry the whole load of the marketing mix. So marketing managers at Chrysler will have to adjust other aspects of their marketing program if they are going to achieve similar success with other products in its line.[1]

Several Promotion Methods Are Available

Promotion is communicating information between seller and potential buyer or others in the channel to influence attitudes and behavior. The marketing manager's main promotion job is to tell target customers that the right Product is available at the right Place at the right Price.

As the PT Cruiser example shows, a marketing manager can choose from several promotion methods—personal selling, mass selling, and sales promotion (see Exhibit 14-1). Further, because the different promotion methods have different strengths and limitations, a marketing manager usually uses them in combination. And, as with other marketing mix decisions, it is critical that the marketer manage and coordinate the different promotion methods as an integrated whole, not as separate and unrelated parts.

Colgate-Palmolive's director of promotions holds meetings to help managers see how to match promotion techniques to marketing objectives.

Personal selling—flexibility is its strength

Personal selling involves direct spoken communication between sellers and potential customers. Face-to-face selling provides immediate feedback—which helps salespeople to adapt. Although some personal selling is included in most marketing mixes, it can be very expensive. So it's often desirable to combine personal selling with mass selling and sales promotion.

Mass selling involves advertising and publicity

Mass selling is communicating with large numbers of potential customers at the same time. It's less flexible than personal selling, but when the target market is large and scattered, mass selling can be less expensive.

Advertising is the main form of mass selling. **Advertising** is any *paid* form of nonpersonal presentation of ideas, goods, or services by an identified sponsor. It includes the use of traditional media like magazines, newspapers, radio and TV, signs, and direct mail as well as new media such as the Internet. While advertising must be paid for, another form of mass selling—publicity—is "free."

Publicity avoids media costs

Publicity is any *unpaid* form of nonpersonal presentation of ideas, goods, or services. Of course, publicity people are paid. But they try to attract attention to the firm and its offerings *without having to pay media costs*. For example, movie studios try to get celebrities on TV talk shows because this generates a lot of interest and sells tickets to new movies without the studio paying for TV time.

Exhibit 14-1
Basic Promotion Methods and Strategy Planning

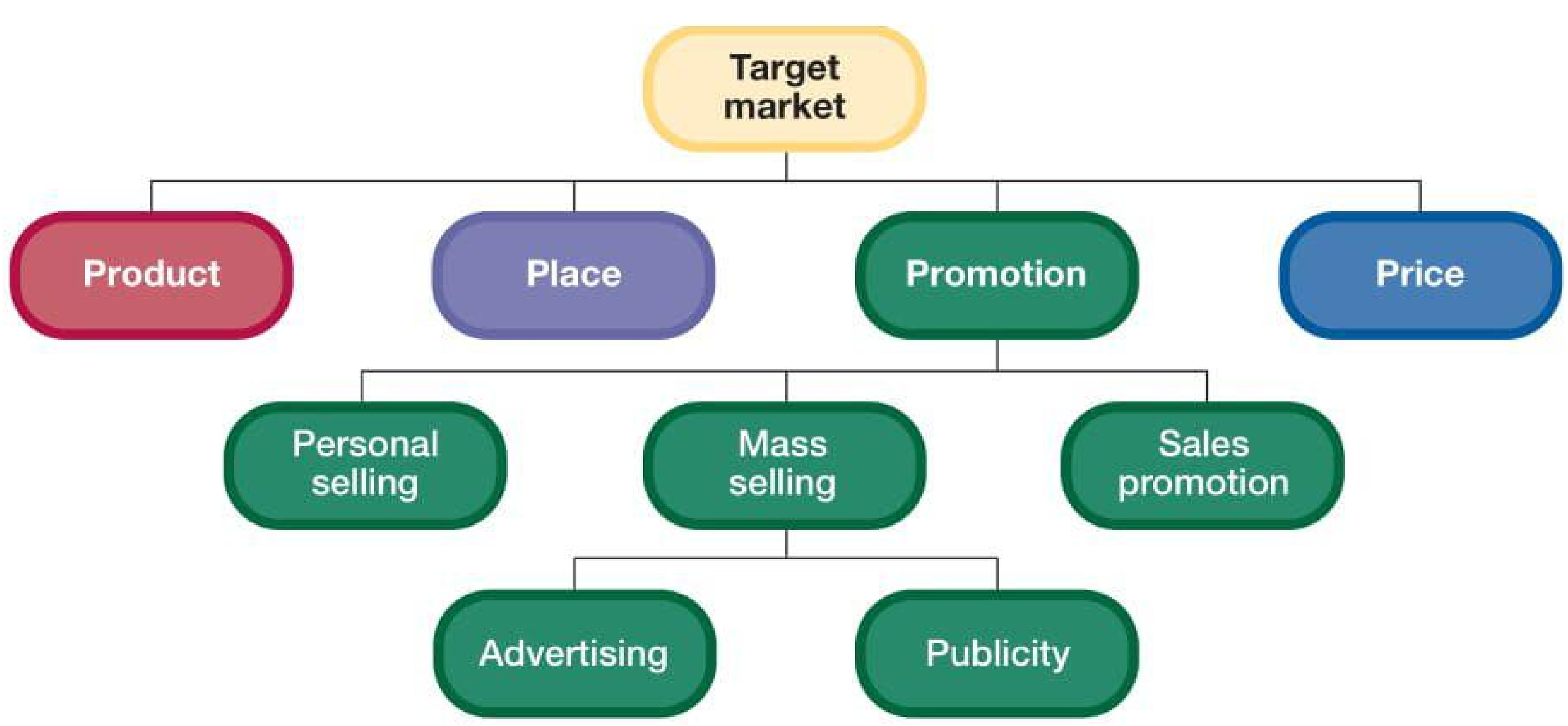


Exhibit 14-2
Example of Sales Promotion Activities

Aimed at final consumers or users	Aimed at middlemen	Aimed at company's own sales force
Contests Coupons Aisle displays Samples Trade shows Point-of-purchase materials Banners and streamers Frequent buyer programs Sponsored events	Price deals Promotion allowances Sales contests Calendars Gifts Trade shows Meetings Catalogs Merchandising aids	Contests Bonuses Meetings Portfolios Displays Sales aids Training materials

Publicity generated by Scholastic, Inc., the distributor of *Harry Potter and the Goblet of Fire,* is a classic example. Scholastic knew that there was already interest in the book; each previous book in the Potter series had increased sales. But Scholastic got a bigger bang, and worldwide media coverage, by notifying bookstores and the media that no store could sell the book before July 8. Deliveries were scheduled to make that stick. And Scholastic kept the title, cover, and plot shrouded in secrecy. As word of the secrecy spread, national media picked up on the story and devoted a huge amount of attention to it. For example, Harry was on the cover of *Newsweek* and a feature article explained all of the reasons why it was going to be one of the fastest-selling books in history. With publicity like that, even people who had never heard of the series wanted to find out what they were missing.[2]

If a firm has a really new message, publicity may be more effective than advertising. Trade magazines, for example, may carry articles featuring the newsworthy products of regular advertisers—in part because they *are* regular advertisers. The firm's publicity people write the basic copy and then try to convince magazine editors to print it. Each year, magazines print photos and stories about new cars—and often the source of the information is the auto producers. A consumer might not pay any attention to an ad but might carefully read a long magazine story with the same information.

Some companies prepare videotapes designed to get free publicity for their products on TV news shows. For example, after learning that Seattle Mariner Jay Buhner loves Cheerios, a General Mills marketing manager had 162 boxes of the cereal stuffed into his spring-training locker. Then he made a videotape of Buhner's surprise on opening his locker. When the videotape was offered to TV stations, it was shown on news programs in 12 major markets around the country. It cost little to produce the video, but it would have cost hundreds of thousands of dollars to get as much attention with advertising on the evening news.[3]

Sales promotion tries to spark immediate interest

Sales promotion refers to promotion activities—other than advertising, publicity, and personal selling—that stimulate interest, trial, or purchase by final customers or others in the channel. Sales promotion may be aimed at consumers, at middlemen, or at a firm's own employees. Examples are listed in Exhibit 14-2. Relative to other promotion methods, sales promotion can usually be implemented quickly and get results sooner. In fact, most sales promotion efforts are designed to produce immediate results.

Less is spent on advertising than personal selling or sales promotion

Many people think that promotion money gets spent primarily on advertising—because advertising is all around them. The many ads you see on the Web, in magazines and newspapers, and on TV are impressive—and costly. But all the special sales promotions—coupons, sweepstakes, trade shows, sporting events sponsored by firms, and the like—add up to even more money. Similarly, salesclerks complete most retail sales. And behind the scenes, much personal selling goes on in the channels and in other business markets. In total, firms spend less money on advertising than on personal selling or sales promotion.

We'll talk about individual promotion methods in more detail in the next two chapters. First, however, you need to understand the role of the whole promotion blend—personal selling, mass selling, and sales promotion combined—so you can see how promotion fits into the rest of the marketing mix.

Someone Must Plan, Integrate, and Manage the Promotion Blend

Each promotion method has its own strengths and weaknesses. Each method also involves its own distinct activities and requires different types of expertise. As a result, it's usually the responsibility of specialists—such as sales managers, advertising managers, and promotion managers—to develop and implement the detailed plans for the various parts of the overall promotion blend.

Sales managers manage salespeople

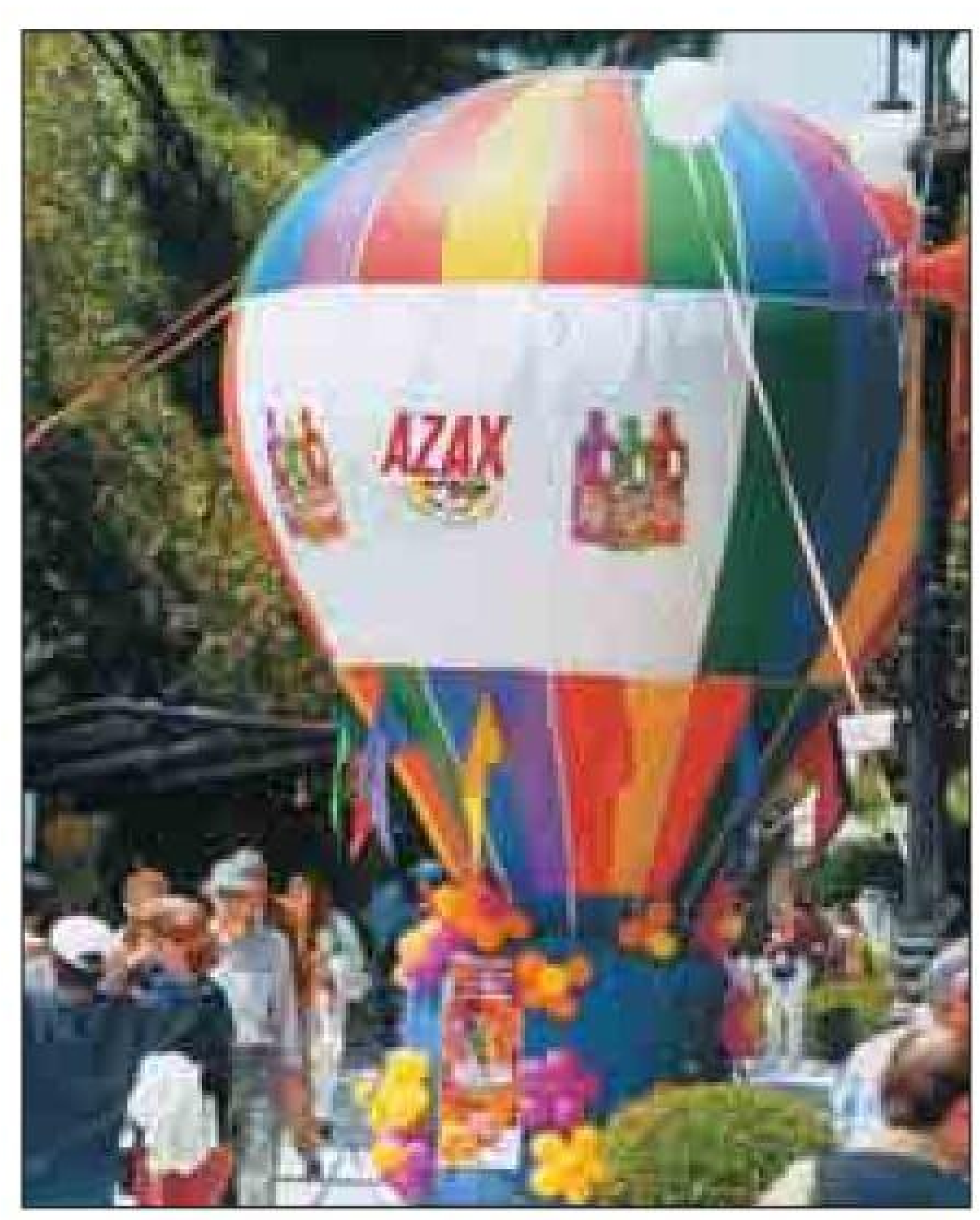
Sales managers are concerned with managing personal selling. Often the sales manager is responsible for building good distribution channels and implementing Place policies. In smaller companies, the sales manager may also act as the marketing manager and be responsible for advertising and sales promotion.

Advertising managers work with ads and agencies

Advertising managers manage their company's mass-selling effort—in television, newspapers, magazines, and other media. Their job is choosing the right media and developing the ads. Advertising departments within their own firms may help in these efforts—or they may use outside advertising agencies. The advertising manager may handle publicity too. Or it may be handled by an outside agency or by whoever handles **public relations**—communication with noncustomers, including labor, public interest groups, stockholders, and the government.

Sales promotion managers need many talents

Sales promotion managers manage their company's sales promotion effort. In some companies, a sales promotion manager has independent status and reports directly to the marketing manager. If a firm's sales promotion spending is substantial,



Sales promotions such as the price-off coupon from Soft Scrub in the U.S. and the free product samples and coupons from Ajax in Greece prompt consumers to try a product—and a consumer who is satisfied with the trial is likely to become a regular customer.

Stanley Works depends on a blend of integrated marketing communications, including sales presentations and product demonstration tours, trade ads focused on retailers, ads targeted at end-users, and a website that provides information on the whole line.

it probably *should* have a specific sales promotion manager. Sometimes, however, the sales or advertising departments handle sales promotion efforts—or sales promotion is left as a responsibility of individual brand managers. Regardless of who the manager is, sales promotion activities vary so much that many firms use both inside and outside specialists.

Marketing manager talks to all, blends all

Although many specialists may be involved in planning for and implementing specific promotion methods, determining the blend of promotion methods is a strategy decision—and it is the responsibility of the marketing manager.

The various promotion specialists tend to focus on what they know best and their own areas of responsibility. A creative web page designer or advertising copywriter in New York may have no idea what a salesperson does during a call on a wholesale distributor. In addition, because of differences in outlook and experience, the advertising, sales, and sales promotion managers often have trouble working with each other as partners. Too often they just view other promotion methods as using up budget money they want.

The marketing manager must weigh the pros and cons of the various promotion methods, then devise an effective promotion blend—fitting in the various departments and personalities and coordinating their efforts. Then the advertising, sales, and sales promotion managers should develop the details consistent with what the marketing manager wants to accomplish.

Send a consistent and complete message with integrated marketing communications

Effective blending of all of the firm's promotion efforts should produce **integrated marketing communications**—the intentional coordination of every communication from a firm to a target customer to convey a consistent and complete message.

The PT Cruiser case at the start of this chapter is a good example of integrated marketing communications. Different promotion methods handle different parts of the job. Yet the methods are coordinated so that the sum is greater than the parts. The separate messages are complementary, but also consistent.

Internet

Internet Exercise Sony produces a very wide variety of products. Does the information available on its website (www.sony.com) appear to be part of an integrated marketing communications effort? Explain your thinking.

It seems obvious that a firm's different communications to a target market should be consistent. However, when a number of different people are working on different promotion elements, they are likely to see the same big picture only if a marketing manager ensures that it happens. Getting consistency is harder when different firms in the distribution channel handle different aspects of the promotion effort. Different channel members may have conflicting objectives—especially if they don't have a common focus on the customer at the end of the channel.

To get effective coordination, everyone involved with the promotion effort must clearly understand the plan for the overall marketing strategy. They all need to understand how each promotion method will contribute to achieve specific promotion objectives.[4]

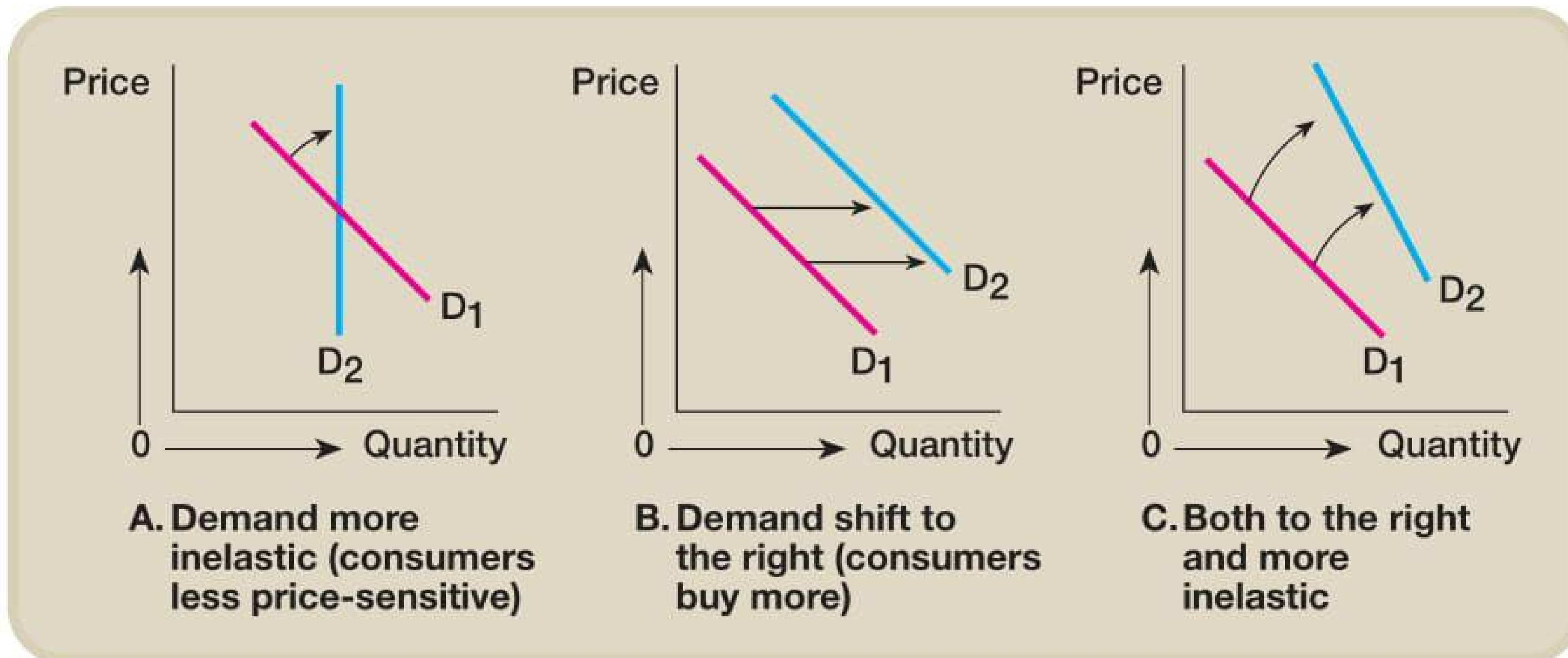
Which Methods to Use Depends on Promotion Objectives

Overall objective is to affect behavior

The different promotion methods are all different forms of communication. But good marketing managers aren't interested in just communicating. They want communication that encourages customers to choose a *specific* product. They know that if they have a better offering, informed customers are more likely to buy. Therefore, they're interested in (1) reinforcing present attitudes or relationships that might lead to favorable behavior or (2) actually changing the attitudes and behavior of the firm's target market.

In terms of demand curves, promotion may help the firm make its present demand curve more inelastic, or shift the demand curve to the right, or both. These possibilities are shown in Exhibit 14-3. The buyer behavior model introduced in Chapter 6 showed the many influences on buying behavior. You saw there that affecting buyer behavior is a tough job—but that is exactly the objective of Promotion.

Exhibit 14-3
Promotion Seeks to Shift the Demand Curve



Informing, persuading, and reminding are basic promotion objectives

A firm's promotion objectives must be clearly defined—because the right promotion blend depends on what the firm wants to accomplish. It's helpful to think of three basic promotion objectives: *informing, persuading,* and *reminding* target customers about the company and its marketing mix. All try to affect buyer behavior by providing more information.

Even more useful is a more specific set of promotion objectives that states *exactly who* you want to inform, persuade, or remind, and *why*. This is unique to each company's strategy—and specific objectives vary by promotion method. We'll talk about more specific promotion objectives in the next two chapters. Here we'll limit ourselves to the three basic promotion objectives and how you can reach them.

Informing is educating

Potential customers must know something about a product if they are to buy at all. A firm with a really new product may not have to do anything but inform consumers about it and show that it meets consumer needs better than other products.

Persuading usually becomes necessary

When competitors offer similar products, the firm must not only inform customers that its product is available but also persuade them to buy it. A *persuading* objective means the firm will try to develop a favorable set of attitudes so customers will buy, and keep buying, its product. A persuading objective often focuses on reasons why one brand is better than competing brands. To convince consumers to buy Tylenol rather than some other firm's brand, Johnson & Johnson's ads position Tylenol as the safe and effective pain relief medicine that is typically used by hospitals.

Reminding may be enough, sometimes

If target customers already have positive attitudes about a firm's marketing mix—or a good relationship with a firm—a *reminding* objective might be suitable. This objective can be extremely important in some cases. Even though customers have been attracted and sold once, they are still targets for competitors' appeals. Reminding them of their past satisfaction may keep them from shifting to a competitor. Campbell realizes that most people know about its soup—so much of its advertising is intended to remind.

Promotion objectives relate to adoption process

In Chapter 6, we looked at consumer buying as a problem-solving process in which buyers go through six steps—awareness, interest, evaluation, trial, decision, and confirmation—on the way to adopting (or rejecting) an idea or product. Now

This trade ad for Kellogg's new Snack 'Ums informs potential channel members that the new product is available and that market testing gives evidence that it will be profitable for the retailer. With its ad Beech-Nut wants to persuade parents that its natural baby food is superior to other products.

we see that the three basic promotion objectives relate to these six steps. See Exhibit 14-4. *Informing* and *persuading* may be needed to affect the potential customer's knowledge and attitudes about a product and then bring about its adoption. Later promotion can simply *remind* the customer about that favorable experience and confirm the adoption decision.

The AIDA model is a practical approach

The basic promotion objectives and adoption process fit very neatly with another action-oriented model—called AIDA—that we will use in this and the next two chapters to guide some of our discussion.

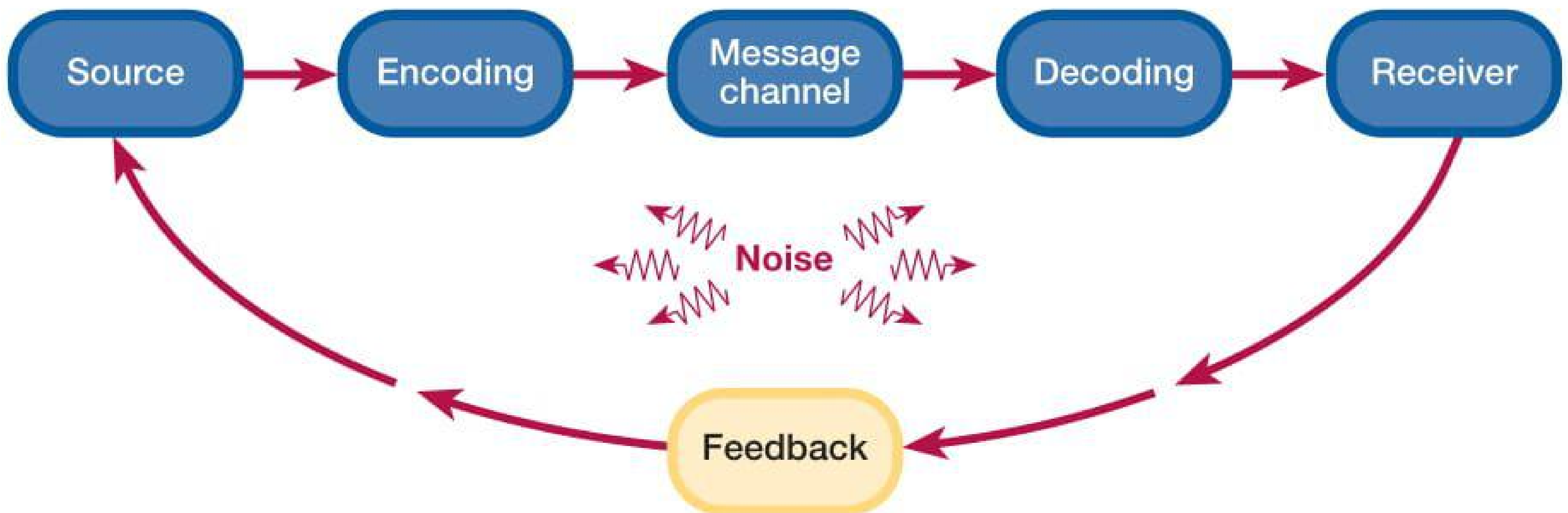
The **AIDA model** consists of four promotion jobs: (1) to get *Attention,* (2) to hold *Interest,* (3) to arouse *Desire,* and (4) to obtain *Action.* (As a memory aid, note that the first letters of the four key words spell AIDA, the well-known opera.)

Exhibit 14-4 shows the relationship of the adoption process to the AIDA jobs. Getting attention is necessary to make consumers aware of the company's offering. Holding interest gives the communication a chance to build the consumer's interest in the product. Arousing desire affects the evaluation process—perhaps building preference. And obtaining action includes gaining trial, which may lead to a purchase decision. Continuing promotion is needed to confirm the decision and encourage an ongoing relationship and additional purchases.

Exhibit 14-4
Relation of Promotion Objectives, Adoption Process, and AIDA Model

Promotion Objectives	Adoption Process (Chapter 6)	AIDA Model
Informing	Awareness Interest Evaluation	Attention Interest
Persuading	Evaluation Trial	Desire
Reminding	Decision Confirmation	Action

Exhibit 14-5
The Traditional Communication Process



Promotion Requires Effective Communication

Communication can break down

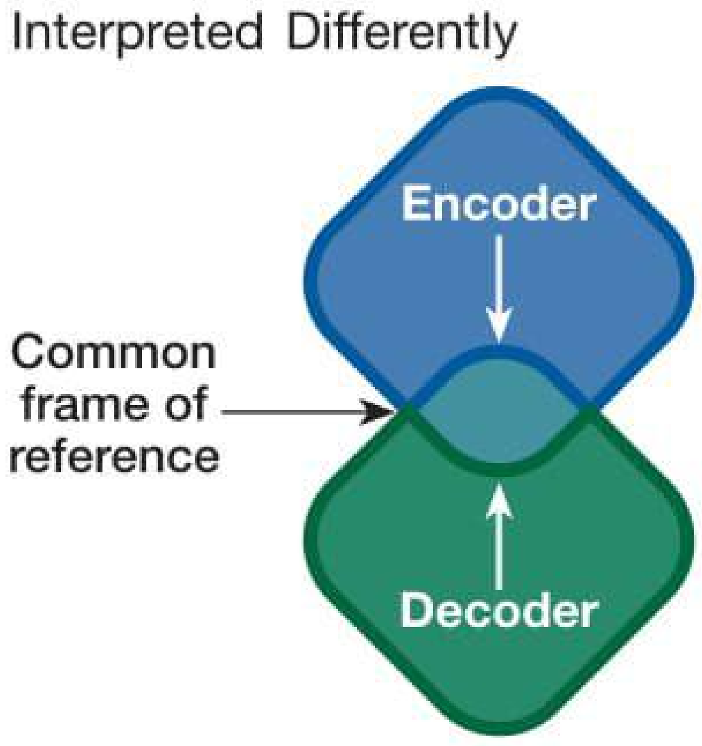
Promotion is wasted if it doesn't achieve its objectives. And that happens when it doesn't communicate effectively. There are many reasons why a promotion message can be misunderstood or not heard at all. To understand this, it's useful to think about a whole **communication process**—which means a source trying to reach a receiver with a message. Exhibit 14-5 shows the elements of the communication process. Here we see that a **source**—the sender of a message—is trying to deliver a message to a **receiver**—a potential customer. Research shows that customers evaluate not only the message but also the source of the message in terms of trustworthiness and credibility. For example, American Dental Association (ADA) studies show that Listerine mouthwash helps reduce plaque buildup on teeth. Listerine mentions the ADA endorsement in its promotion to help make the promotion message credible.

A major advantage of personal selling is that the source—the seller—can get immediate feedback from the receiver. It's easier to judge how the message is being received and to change it if necessary. Mass sellers usually must depend on marketing research or total sales figures for feedback—and that can take too long. As we'll discuss later in this chapter, this has prompted many marketers to include toll-free telephone numbers and website addresses as ways of building direct-response feedback from consumers into their mass-selling efforts.

The **noise**—shown in Exhibit 14-5—is any distraction that reduces the effectiveness of the communication process. Conversations and snack-getting during TV ads are noise. The clutter of competing ads on the Internet is noise. Advertisers planning messages must recognize that many possible distractions—noise—can interfere with communications.

Encoding and decoding depend on a common frame of reference

Exhibit 14-6
This Same Message May Be Interpreted Differently



The basic difficulty in the communication process occurs during encoding and decoding. **Encoding** is the source deciding what it wants to say and translating it into words or symbols that will have the same meaning to the receiver. **Decoding** is the receiver translating the message. This process can be very tricky. The meanings of various words and symbols may differ depending on the attitudes and experiences of the two groups. People need a common frame of reference to communicate effectively. See Exhibit 14-6. Maidenform encountered this problem with its promotion aimed at working women. The company ran a series of ads depicting women stockbrokers and doctors wearing Maidenform lingerie. The men in the ads were fully dressed. Maidenform was trying to show women in positions of authority, but some women felt the ad presented them as sex objects. In this case, the promotion people who encoded the message didn't understand the attitudes of the target market and how they would decode the message.[5]

Message channel is important too

The communication process is complicated even more because the receiver knows the message is not only coming from a source but also through some **message channel**—the carrier of the message. A source can use many message channels to deliver a message. The salesperson does it in person with voice and action. Advertising must do it with magazines, newspapers, radio, and TV, or with media such as e-mail or Internet websites. A particular message channel may enhance or detract from a message. A TV ad, for example, can *show* that Dawn dishwashing detergent "takes the grease away"; the same claim might not be very convincing—or might be resented—if it arrived in a consumer's e-mail. On the other hand, a receiver may attach value to a product if the message comes in a well-respected newspaper or magazine. Some consumers buy products advertised in *Good Housekeeping* magazine, for example, because they have faith in its seal, which carries a two-year limited warranty to replace a product (or refund the purchase price) if the product is defective.[6]

The same message may be interpreted differently

Different audiences may see the same message in different ways or interpret the same words differently. Such differences are common in international marketing when cultural differences or translation are problems. In Taiwan, the translation of the Pepsi slogan "Come alive with the Pepsi Generation" came out as "Pepsi will bring your ancestors back from the dead." When Frank Perdue said, "It takes a tough man to make a tender chicken," Spanish speakers heard "It takes a sexually stimulated man to make a chicken affectionate." Worse, a campaign for Schweppes Tonic Water in Italy translated the name into Schweppes Toilet Water. Many firms run into problems like this.[7]

Problems occur even when there is no translation. For example, a new children's cough syrup was advertised as extra strength. The advertising people thought they were assuring parents that the product worked well. But Moms and Dads avoided the product because they feared that it might be too strong for their children.

Ethical issues in marketing communications

Promotion is one of the most often criticized areas of marketing, and many of the criticisms focus on whether communications are honest and fair. Marketers must sometimes make ethical judgments in considering these charges and in planning their promotion.

Video publicity releases provide an interesting example. When a TV news program broadcasts a video publicity release, consumers don't know it was prepared to

Good Housekeeping is taking advantage of consumer confidence in its seal and has developed a new program for website certification.

achieve marketing objectives; they think the news staff is the source. That may make the message more credible, but is it fair? Many say yes—as long as the publicity information is truthful. But gray areas still remain. Consider, for example, a SmithKline Beecham video about a prescription heart attack drug. An estimated 27 million consumers saw the video on various TV news programs. The video included a laundry list of possible side effects and other warnings, just as is required for normal drug advertising. But there's never any guarantee that the warnings won't be edited out by local TV stations.

Critics raise similar concerns about the use of celebrities in advertisements. A person who plays the role of an honest and trustworthy person on a popular TV series may be a credible message source in an ad, but is using such a person misleading to consumers? Some critics believe it is. Others argue that consumers recognize advertising when they see it and know celebrities are paid for their endorsements.

The most common criticisms of promotion relate to promotional messages that make exaggerated claims. What does it mean for an ad or a salesperson to claim that a product is the "best available"? Is that the personal opinion of people in the firm, or should every statement—even very general ones—be backed up by objective proof? What type of proof should be required? Some promotional messages do misrepresent the benefits of a product. However, most marketing managers want to develop ongoing relationships with, and repeat purchases from, their customers. They realize that customers won't come back if the marketing mix doesn't deliver what the promotion promises. Further, consumers are becoming more skeptical about all the claims they hear and see. As a result, most marketing managers work to make promotion claims specific and believable.[8]

Integrated Direct-Response Promotion Is Very Targeted

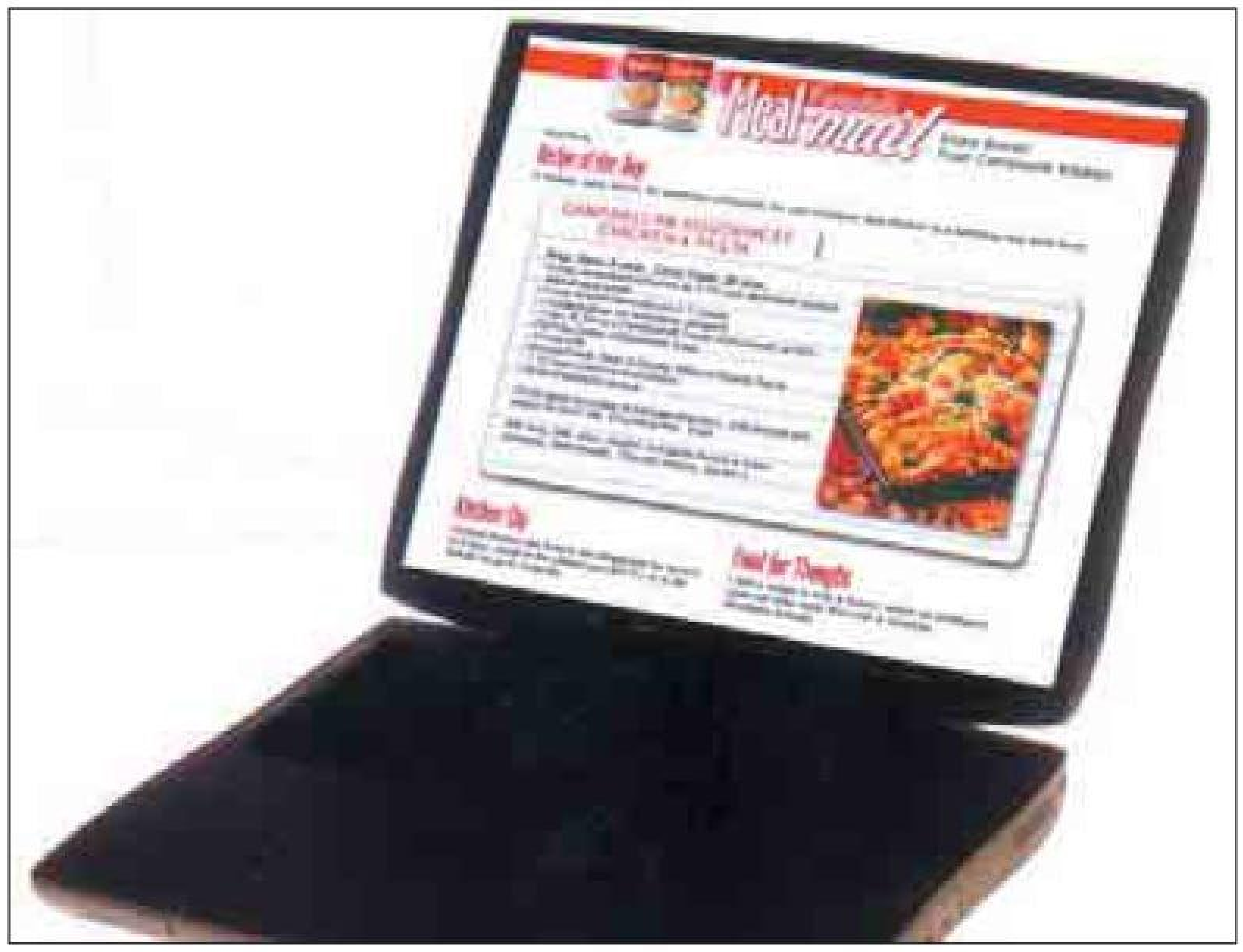
The challenge of developing promotions that reach *specific* target customers has prompted many firms to turn to direct marketing—direct communication between a seller and an individual customer using a promotion method other than face-to-face personal selling. Most direct marketing communications are designed to prompt immediate feedback—a direct response—by customers. That's why this type of communication is often called *direct-response promotion*.

Early efforts in the direct-response area focused on direct-mail advertising. A carefully selected mailing list—perhaps from the firm's customer relationship management (CRM) database—allowed advertisers to reach a specific target audience with specific interests. And direct-mail advertising proved to be very effective when the objective was to get a direct response from the customer.

Now it's more than direct-mail advertising

Achieving a measurable, direct response from specific target customers is still the heart of direct promotion. But the promotion medium is evolving to include not just mail but telephone, print, e-mail, a website, broadcast, and even interactive video. The customer's response may be a purchase (or donation), a question, or a request for more information. At a website, the response may be a simple mouse-click to link to more information, a click to put an item in a virtual shopping cart, or a click to purchase.

Often the customer responds by calling a toll-free telephone number or, in the case of business markets, by sending a fax or an e-mail. A knowledgeable salesperson talks with the customer on the phone and follows up. That might involve filling an order and having it shipped to the customer or putting an interested prospect in touch with a salesperson who makes a personal visit. There are, however, many



FTD's website encourages a direct response from consumers, starting with a personalized calendar where the customer can enter dates for important flower-giving occasions. Similarly, Campbell's Soup encourages consumers to sign up to receive free recipes that are e-mailed each week.

variations on this approach. For example, some firms route incoming information-request calls to a computerized answering system. The caller indicates what information is required by pushing a few buttons on the telephone keypad. Then the computer instantly sends requested information to the caller's fax machine.

Direct-response promotion is often an important component of integrated marketing communications programs and is closely tied to other elements of the marketing mix. However, what distinguishes this general approach is that the marketer targets more of its promotion effort at specific individuals who respond directly.[9]

A promotion campaign that marketing managers developed for Ryder Systems' move-it-yourself rental trucks illustrates these ideas. Ryder's marketing strategy focused on quality trucks and service rather than bargain-basement prices. Ryder's objective was to increase truck rentals and sales of supplies while maintaining its premium prices. Most other rental firms were competing with lower prices—hoping for gains in market share to offset a market that was shrinking because of a weak economy.

To reach the target market—consumers who were considering a move—Ryder placed 60-second ads on popular TV shows whose audience demographics matched Ryder's target market. The ads touted Ryder quality and also offered consumers a free home-moving guide and planning kit. All the consumer had to do to get the promotional brochure was call a toll-free telephone number. The brochure provided useful information about moving—including details on how Ryder's comfortable trucks and helpful services could make the move easier. It also included a discount coupon for Ryder supplies—like furniture pads and locks—that consumers could redeem at any Ryder dealer. Equally important, the computerized mailing list (database) of people who called for the brochure served as a targeted list of prospects for Ryder's telemarketing salespeople. When one of them identified a good prospect, the final personal selling job was turned over to a local Ryder dealer. The dealer's personal attention helped to resolve consumer questions and get rental contracts. Further, because the whole promotion effort was consistent in differentiating Ryder's quality services, the dealers were able to charge a higher price than competitors.[10]

Target customer directly with a database

As the Ryder case suggests, direct-response promotion usually relies on a customer (or prospect) database to target specific individuals. The computerized database includes customers' names and addresses (or telephone numbers) as well as past purchases and other segmenting characteristics. Greenpeace and the Cousteau Society send mail advertisements to people interested in environmental issues. They ask for donations or other types of support. Individuals (or segments) who respond to direct promotion are the target for additional promotion. For example, a customer who buys lingerie from a catalog or a website once is a good candidate for a follow up. The follow up might extend to other types of clothing.

BMW and other car companies found that videotapes are a good way to provide consumers with a lot of information about a new model. However, it's too expensive to send tapes to everyone. To target the mailing, BMW first sends likely car buyers (high-income consumers who own a BMW or competing brand) personalized direct-mail ads that offer a free videotape. Interested consumers send back a return card. Then BMW sends the advertising tape and updates its database so a dealer will know to call the consumer.

Direct-response methods raise ethical concerns

Direct-response promotion and customer relationship management database targeting have become an important part of many marketing mixes—and more and more customers find it very convenient. But not everyone is enthusiastic. Some critics argue that thousands of acres of trees are consumed each week—just to make the paper for direct response "junk mail" that consumers don't want. Most e-mail users also get uninvited messages—"spam." Other critics worry about privacy issues related to how a direct-response database might be used, especially if it includes detailed information about a consumer's purchases. Similarly, many consumers don't like getting direct promotion telephone solicitations at any time, but especially in the evening and at meal times when they seem to be particularly frequent. Most states have passed laws prohibiting automatic calling systems that use prerecorded messages rather than a live salesperson. There is also growing concern by computer users about receiving e-mail they don't want. Worse, some firms have been criticized for creating websites that secretly install programs on customers' computers. Then, unknown to the user, the program gathers information about other websites the user visits and sends it back to the firm over the Internet. Most firms that use direct-response promotion are very sensitive to these concerns and take steps to address them.[11]

The Customer May Initiate the Communication Process

Traditional thinking about promotion—and for that matter about the communication process—has usually been based on the idea that it's the seller ("source") who initiates the communication. Of course, for decades consumers have been looking in the Yellow Pages for information or asking retail salespeople for help. Similarly, it's not news that organizational buyers contact potential vendors to ask questions or request bids.

Even so, marketers often think of the buyer as a more or less passive message receiver in the communication process—at least until the marketer has done something to stimulate attention, interest, and desire. That's one reason that targeting is so important—so that the promotion effort and expense isn't wasted on someone who isn't at all interested. Moreover, the need for a blend of promotion methods is built on the idea that at any given moment you can get a customer's attention and interest for only a few seconds—or a few minutes if you're really lucky. Even with highly targeted direct-response promotion, the marketer typically has taken the first step with promotion to get the interaction started.

New electronic media enable interactive communication

However, this is changing. In the information age, it is much easier for customers to search for information on their own. In fact, buyers can access a great deal of information and place an order without the seller having been directly involved at all. The new interactive information technologies enabling this change take many different forms, but some of the most important are websites, e-mail list-servers, caller-controlled fax-on-demand, computerized telephone voice-messaging systems, video kiosks in malls, CD-ROM and DVD disks on personal computers, and WebTV.

New variations on these interactive technologies are being developed all of the time. For example, in England, where interactive cable TV systems have been operating for a decade, consumers have access to a system called Teletext. With Teletext, they can use their standard TV remote control unit to search through thousands of on-screen pages of information—ranging from the schedule for flights from London's airports and the current weather to advertising for automobiles and specials at the local supermarket. The benefits of Teletext are very similar to the benefits of the World Wide Web on the Internet, but it uses a standard TV. Similar systems will become more available in other countries as government regulations change and as cable companies upgrade their equipment.

Internet

Internet Exercise Visit the Campbell's Soup website (www.campbellsoup.com). Does the website make it easy for you to get information? Does it make you want to spend more time and get more information? Explain your answer.

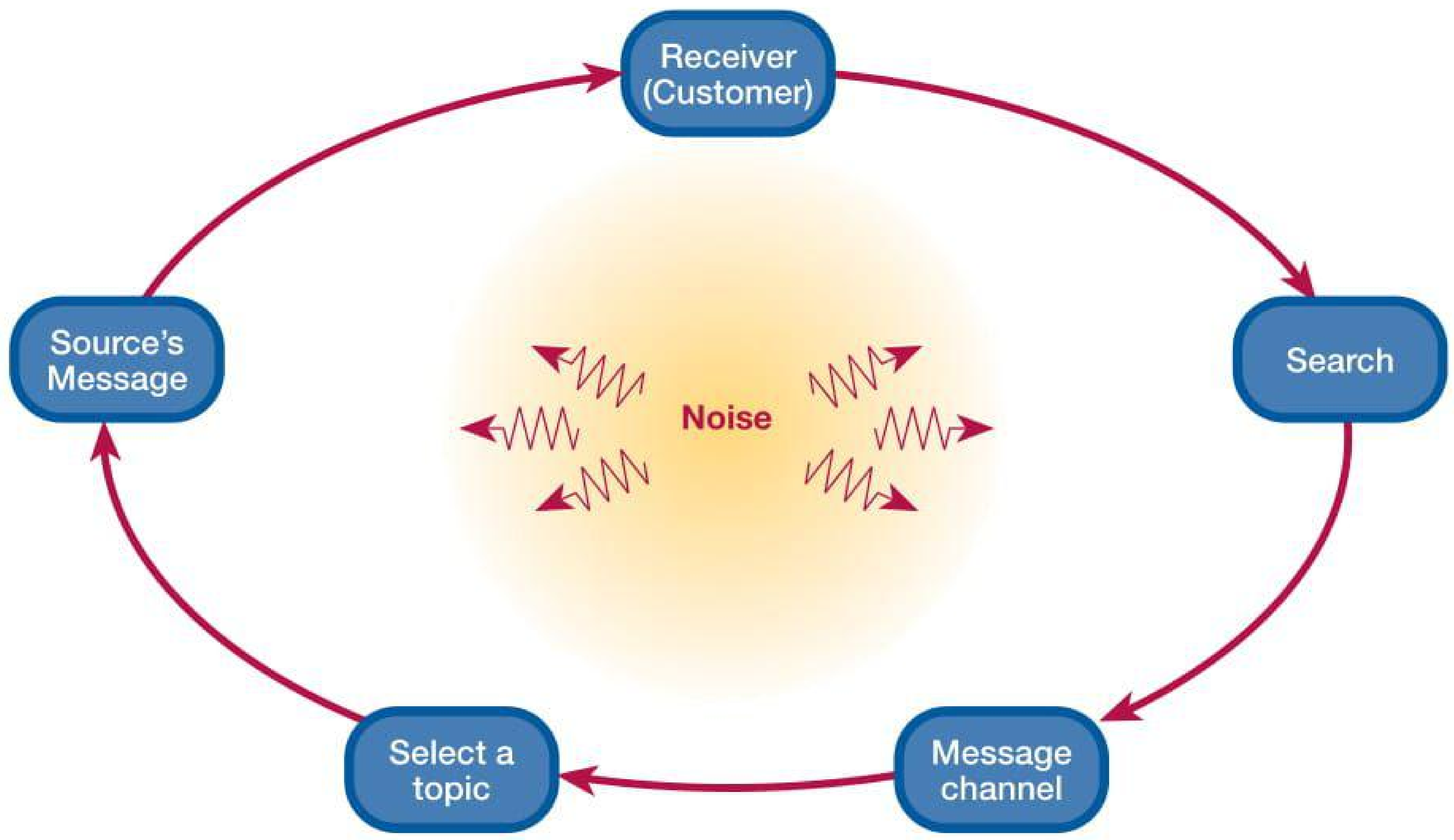
Work is underway to develop broadcast systems in which icons will appear on-screen as consumers watch a program or movie. For example, an icon might appear on a jacket worn by a talk show guest. A consumer who is interested in the product will be able to press a button on a remote control to get more information about the product or where to buy it—or even to place an order. The same concept is already implemented on DVDs for some movies. When this type of system is available via cable (or with streaming video over the Internet), it will provide a powerful new tool for marketers and, over time, reshape the way many marketing communications are handled.

This type of customer-initiated information search and/or communication represents a change that will become prevalent for more types of purchases in the future, so we should think about it in more detail. Let's start by contrasting the simple model of customer ("receiver") initiated interactive communication shown in Exhibit 14-7. At first it doesn't seem very different from the traditional communication model we considered earlier (Exhibit 14-5). However, the differences are significant.

Consumer initiates communication with a search process

In the model in Exhibit 14-7, a customer initiates the communication process with a decision to search for information in a particular message channel. The most far-reaching message channel to search is the Internet. The message channel is still the carrier of the message, as was the case before, but "searchable" message channels

Exhibit 14-7
A Model of Customer-Initiated Interactive Communication



usually feature an archive of existing messages on a number of topics. There may be many available topics—even millions.

In the next step, the consumer selects one specific topic on which to receive a message. Selecting a topic might be done in one of a variety of ways, depending on the message channel. The most typical approaches involve using a mouse, remote control device, or keypad to highlight a selection from an initial list (like a table of contents or index). Of course, other approaches are common. For example, many dial-up telephone systems are using voice-recognition systems. Or, in the case of the Internet, you might enter a word or phrase and have the computer search for a list of topics that include it.

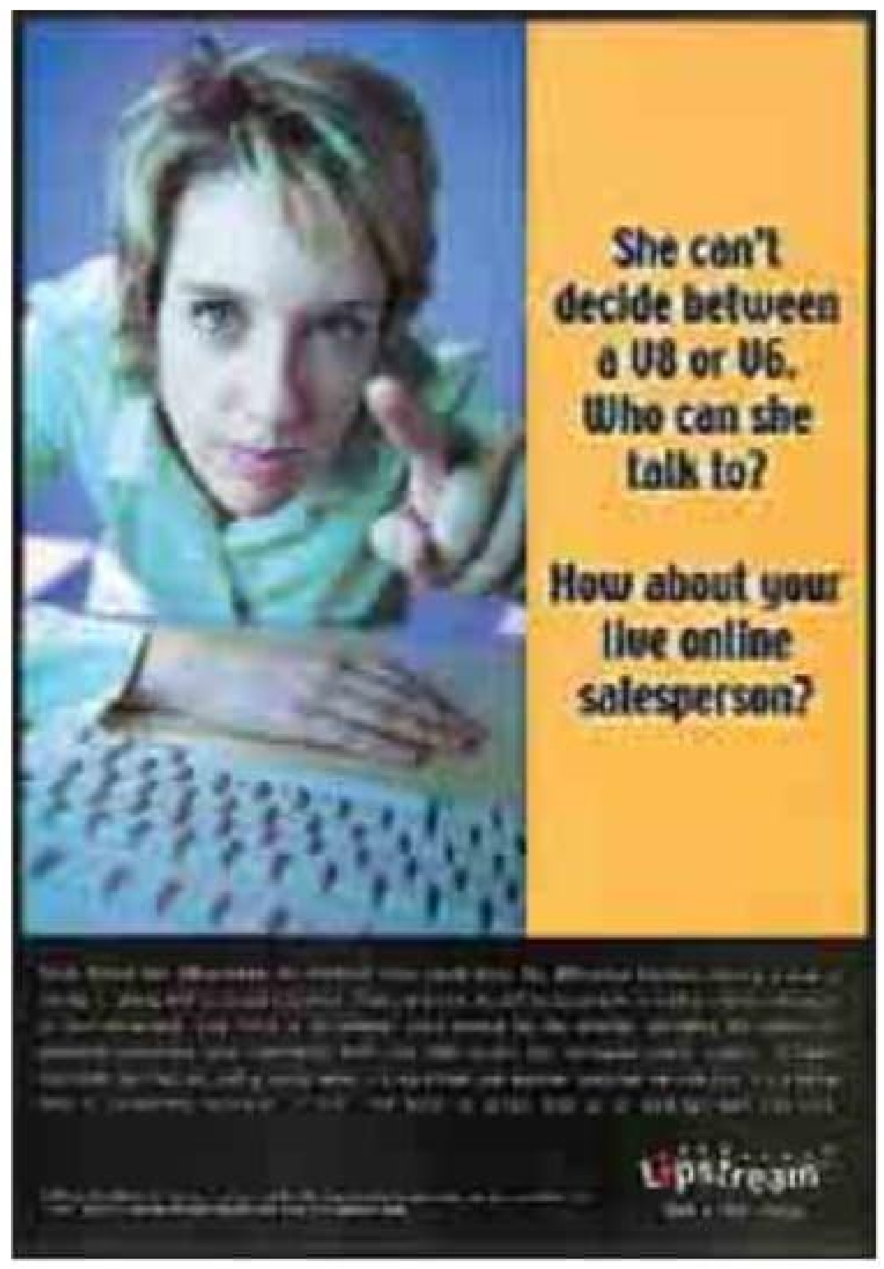
Consumer decides how much information to get

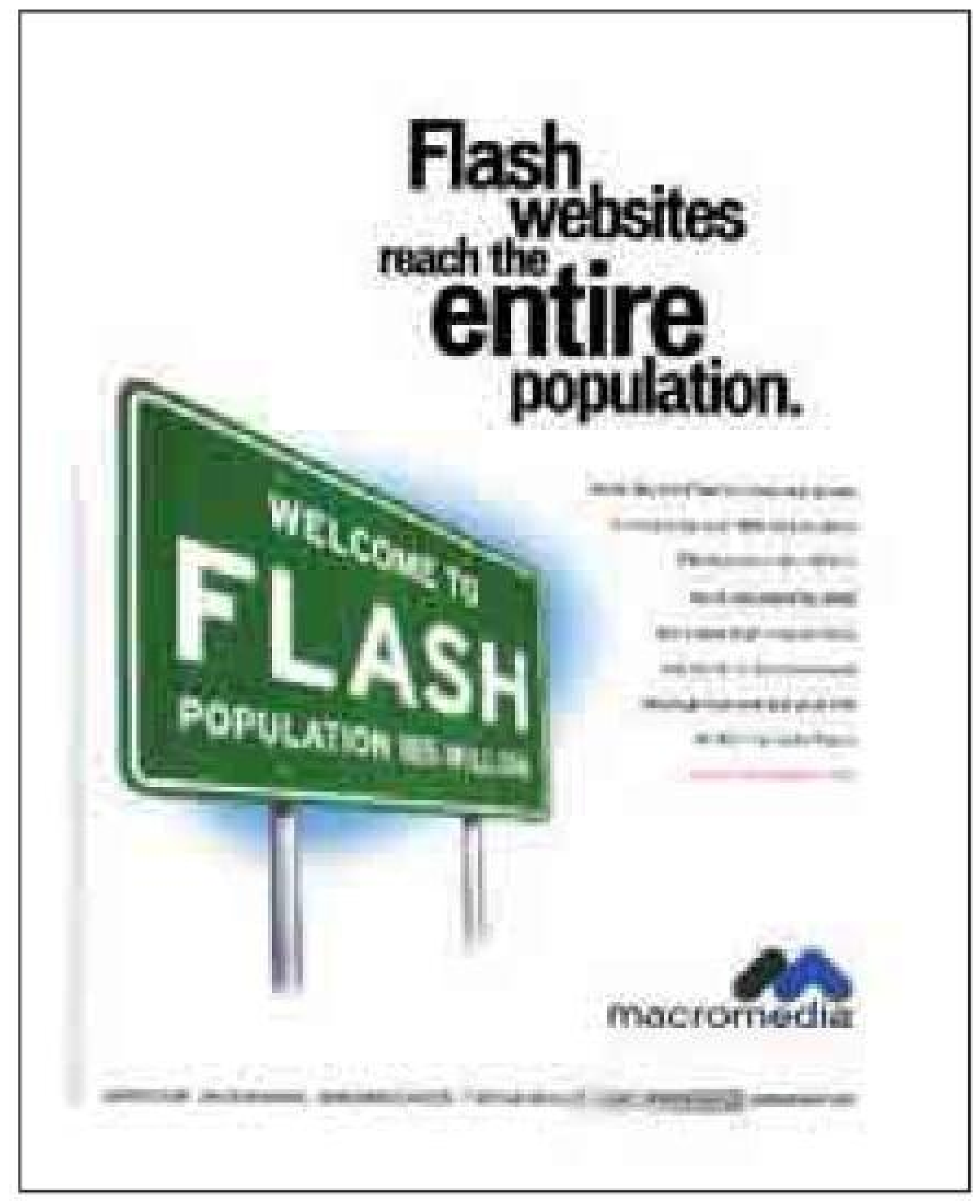
Once a specific topic is selected, the message for that topic is displayed. Typically, the message is brief. But it may include a simple way to get more detailed information, select another related topic, return to the original selection process, or quit the search. Thus, after each message the consumer can decide whether to search further (say, to get more detail on an initial topic or to broaden the search to other topics). This interactive approach makes it easy for the consumer to conveniently get as much or little information as desired and to spend as much time searching as seems worthwhile. However, noise may still be a problem. For example, a consumer who wants information about a specific product may waste a lot of time and still not find what is needed—because it is not available on the message channel or it is too hard to find. So some firms offer consumers a website choice that establishes communication with a real person at a 24-hour-a-day service center. Some of these systems use instant messaging so that the consumer and a customer service person can chat online. With other systems, like AT&T's "Interactive Answers" approach, a person at the calling center telephones the customer and provides the precise product information or help needed. Other firms are using variations of this approach, including live teleconferencing over the Internet. Many personal computers now come equipped with everything needed for this type of Internet teleconferencing.

Action—including purchase—may be immediate

Even without a voice link to a live salesperson, the action required to make a purchase by interactive media is usually very fast and easy—because one of the topics available for the customer to select is "how to buy." At many Internet sites, for example, a consumer can click on a selected item to place it in a virtual shopping cart, charge it to a credit card, and arrange for shipping by a service like UPS.

Lipstream and Macromedia offer products that help marketing managers take advantage of the interactive and multimedia potential of website communications.





Custom communications will be more personalized

As you can see, the traditional principles of communication that we discussed earlier in the chapter are still important in customer-initiated interactive communication. At the same time, the interactive approach allows the marketer to customize communication to the needs and responses of the consumer. As new approaches develop in this arena, we are seeing more promotion targeted at single-person "segments."

Electronic media also allows many types of information—pictures, graphs, words, video, and sounds—to be used. As a result, a key advantage of the new electronic media is that all of the different promotional materials that a firm develops can be available in one place. This allows managers with different specialties to see how their materials work with the rest of the promotion blend—so there is even more incentive to develop integrated communications.[12]

How Typical Promotion Plans Are Blended and Integrated

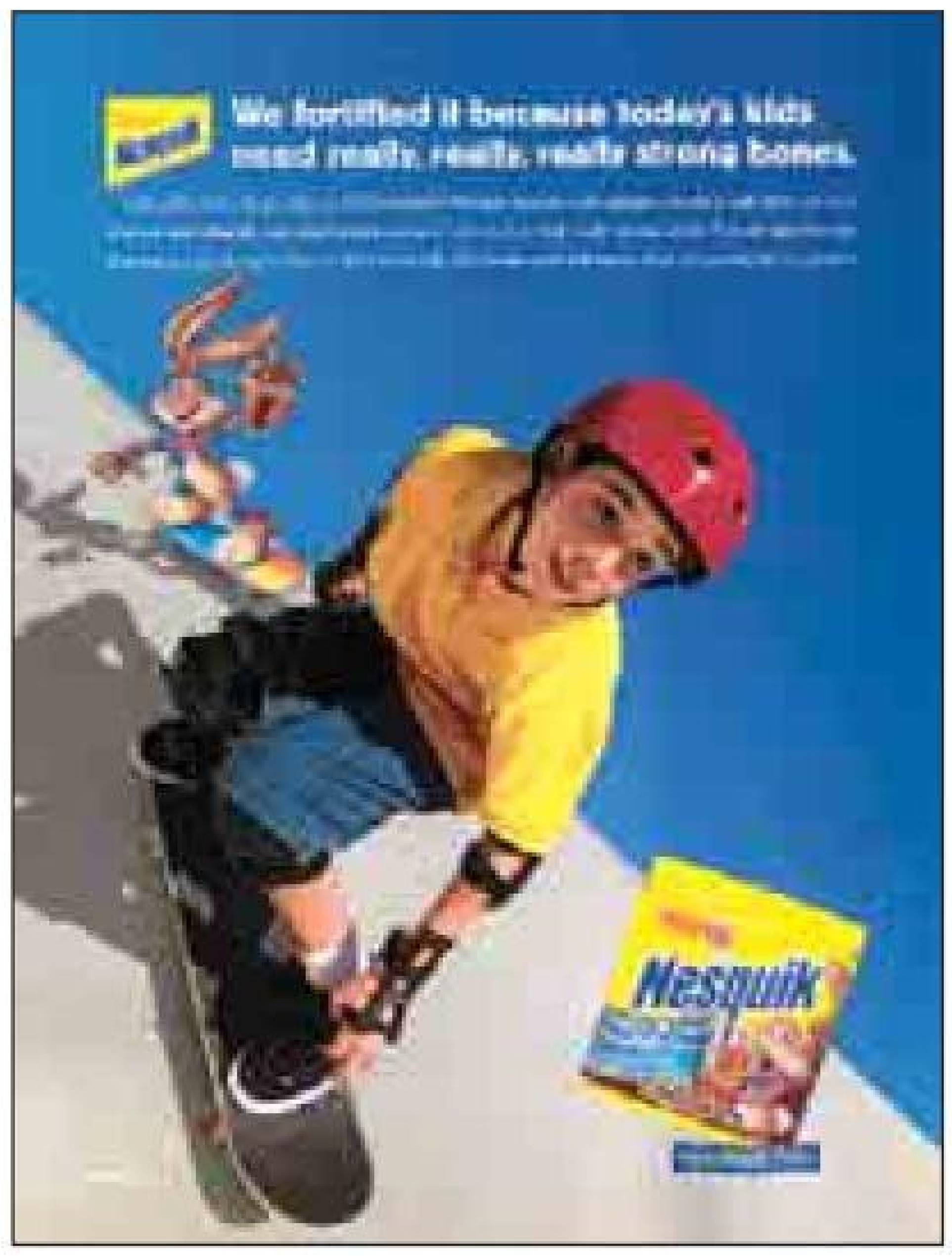
There is no one right blend

There is no one *right* promotion blend for all situations. Each one must be developed as part of a marketing mix and should be designed to achieve the firm's promotion objectives in each marketing strategy. So let's take a closer look at typical promotion blends in different situations.

Get a push in the channel with promotion to middlemen

When a channel of distribution involves middlemen, their cooperation can be crucial to the success of the overall marketing strategy. **Pushing** (a product through a channel) means using normal promotion effort—personal selling, advertising, and sales promotion—to help sell the whole marketing mix to possible channel members. This approach emphasizes the importance of building a channel and securing the wholehearted cooperation of channel members to push the product down the channel to the final user.

Producers usually take on much of the responsibility for the pushing effort in the channel. However, most wholesalers also handle at least some of the promotion to retailers or other wholesalers further down the channel. Similarly, retailers often handle promotion in their local markets. The overall promotion effort is most likely to be effective when all of the individual messages are carefully integrated—that is, coordinated, consistent, and complete.



Nesquik's ad is targeted at parents and kids and designed to stimulate demand and help pull Nesquik's popular chocolate additive for milk through the channel of distribution. Dome's trade ad message is targeted at retailers and designed to persuade them to give the Handeze therapeutic support glove an extra promotional push.

Promotion to middlemen emphasizes personal selling

Salespeople handle most of the important communication with middlemen. Middlemen don't want empty promises. They want to know what they can expect in return for their cooperation and help. A salesperson can answer questions about what promotion will be directed toward the final consumer, each channel member's part in marketing the product, and important details on pricing, markups, promotion assistance, and allowances.

A salesperson can help the firm determine when it should adjust its marketing mix from one middleman to another. In highly competitive urban areas, for example, mixes may emphasize price.

When a number of suppliers offer similar products and compete for attention and shelf space, the wholesaler or retailer usually pays attention to the one with the best profit potential. In these situations, the sales rep must convince the middleman that demand for the product exists and that making a profit will be easy. A firm can make the sales rep's job easier by targeting special sales promotions at middlemen too.

Sales promotions targeted at middlemen usually focus on short-term arrangements that will improve the middleman's profits. For example, a soft-drink bottler might offer a convenience store a free case of drinks with each two cases it buys. The free case improves the store's profit margin on the whole purchase. Other types of sales promotions—such as contests that offer vacation trips for high-volume middlemen—are also common.

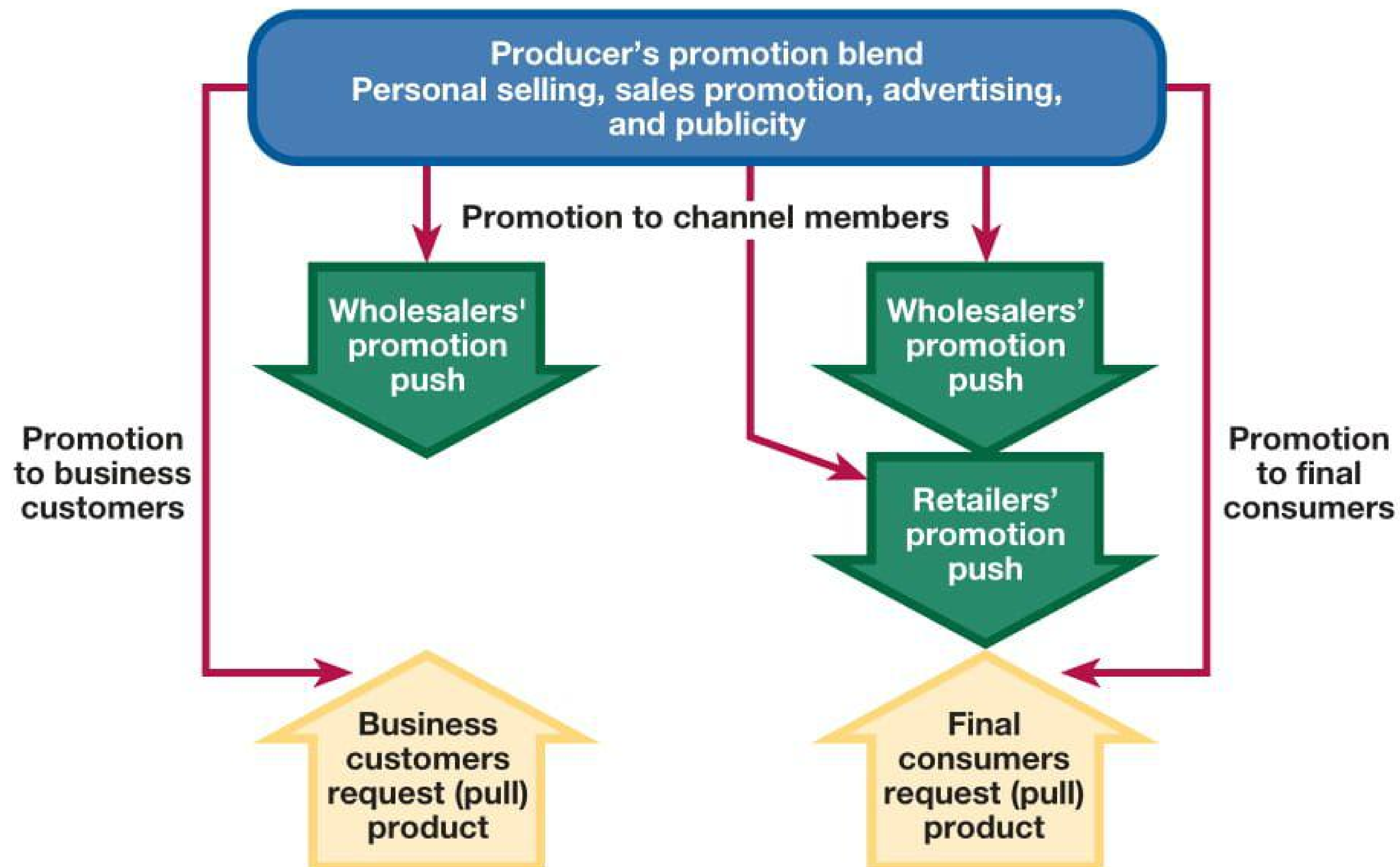
Firms run ads in trade magazines to recruit new middlemen or to inform channel members about a new offering. Trade ads usually encourage middlemen to contact the supplier for more information, and then a salesperson takes over.

Push within a firm—with promotion to employees

Some firms emphasize promotion to their own employees—especially salespeople or others in contact with customers. This type of *internal marketing* effort is basically a variation on the pushing approach. One objective of an annual sales meeting is to inform reps about important elements of the marketing strategy—so they'll work together as a team to implement it. Some firms use promotion to motivate employees to work harder at specific jobs—such as providing customer service or achieving higher sales. For example, many firms use sales contests and award free trips to big sellers.

Some companies design ads to communicate to employees and boost the employees' image. This is typical in services where the quality of the employees' efforts is a big part of the product. Some ads, for example, use the theme "we like to see you

Exhibit 14-8
Promotion May Encourage Pushing in the Channel, Pulling by Customers, or Both



smile." The ads communicate to customers, but also remind employees that the service they provide is crucial to customer satisfaction.

Pulling policy—customer demand pulls the product through the channel

Regardless of what promotion a firm uses to get help from channel members or employees in pushing a product, most producers focus a significant amount of promotion on customers at the end of the channel. This helps to stimulate demand and pull the product through the channel of distribution. **Pulling** means getting customers to ask middlemen for the product.

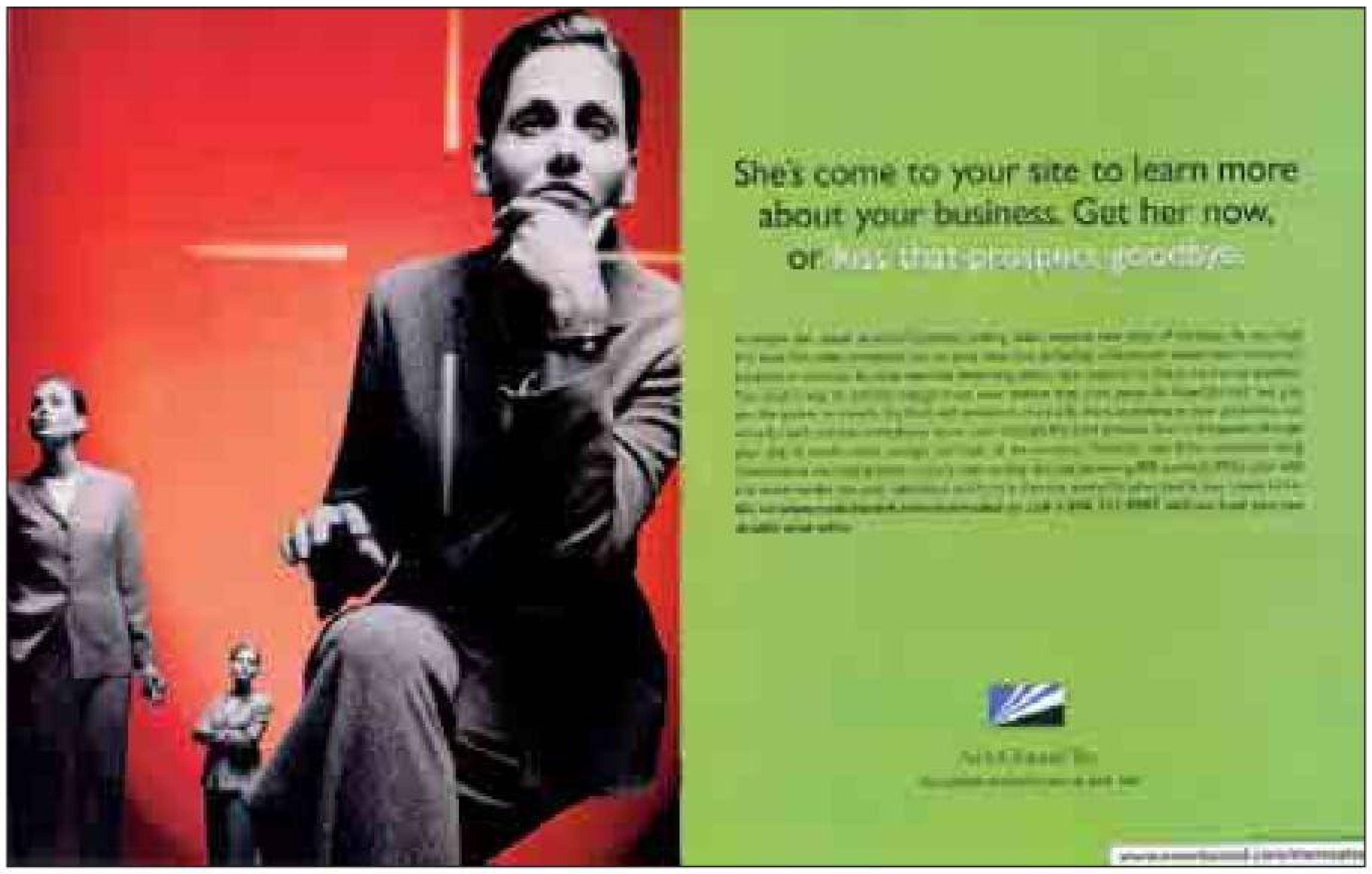
Pulling and pushing are usually used in combination. See Exhibit 14-8. However, if middlemen won't work with a producer—perhaps because they're already carrying a competing brand—a producer may try to use a pulling approach by itself. This involves highly aggressive and expensive promotion to final consumers or users—perhaps using coupons or samples—temporarily bypassing middlemen. If the promotion works, the middlemen are forced to carry the product to satisfy customer requests. However, this approach is risky. An expensive promotion effort is wasted if customers lose interest before reluctant middlemen make the product available. At minimum, middlemen should be told about the planned pulling effort—so they can be ready if the promotion succeeds.

Who handles promotion to final customers at the end of the channel varies in different channel systems—depending on the mix of pushing and pulling. Further, the promotion blend typically varies depending on whether customers are final consumers or business users.[13]

Promotion to final consumers

The large number of consumers almost forces producers of consumer products and retailers to emphasize advertising and sales promotion. Sales promotion—such as coupons, contests, or free samples—builds consumer interest and short-term sales of a product. Effective mass selling may build enough brand familiarity so that little personal selling is needed—as in self-service and discount operations.[14]

Some retailers—specialty shops in particular—rely heavily on well-informed salespeople. Technical products (like camcorders or computers) and personal services (like health care and estate planning) may also require personal selling. Direct selling firms like Amway also rely on personal selling. But aggressive personal selling to final consumers usually is found in expensive channel systems, such as those for fashionable clothing, furniture, consumer electronics, and automobiles.



NewChannel wants to help firms identify the best prospects who visit the firm's website so that a salesperson can then immediately reach out and move them through the sales process.

Promotion to business customers

Producers and wholesalers who target business customers often emphasize personal selling. This is practical because these customers are much less numerous than final consumers and their purchases are typically larger.

Moreover, business customers may have technical questions or need adjustments in the marketing mix. An extremely technical business product may require a heavy emphasis on personal selling—using technically trained salespeople. This is the only sure way to make the product understood and get feedback on how customers use it. The technical sales rep meets with engineers, production managers, purchasing agents, and top managers and can adjust the sales message to the needs of these various influences.

Sales reps can be more flexible in adjusting their companies' appeals to suit each customer—and personal contact is usually required to close a sale. A salesperson is also able to call back later to follow up with additional information, resolve any problems, and nurture the relationship with the customer.

While personal selling dominates in business markets, mass selling is necessary too. A typical sales call on a business customer costs about $200.[15] That's because salespeople spend less than half their time actually selling. The rest is consumed by such tasks as traveling, paperwork, sales meetings, and strictly service calls. So it's seldom practical for salespeople to carry the whole promotion load.

Ads in trade magazines or at a B2B e-commerce website, for instance, can inform potential customers that a product is available. Most trade ads give a toll-free telephone number, fax number, or website address to stimulate direct inquiries. Domestic and international trade shows also help identify prospects. Even so, most sellers who target business customers spend only a small percentage of their promotion budget on mass selling and sales promotion.

Each market segment may need a unique blend

Knowing what type of promotion is typically emphasized with different targets is useful in planning the promotion blend. But each unique market segment may need a separate marketing mix and a different promotion blend. Some mass-selling specialists miss this point. They think mainly in terms of mass marketing rather than target marketing. Aiming at large markets is desirable in some situations, but promotion aimed at everyone can end up hitting no one. In developing the promotion blend, you should be careful not to slip into a shotgun approach when what you really need is a rifle approach—with a more careful aim.

Adoption Processes Can Guide Promotion Planning

The AIDA and adoption processes look at individuals. This emphasis on individuals helps us understand how promotion affects the way that people behave. But it's also useful to look at markets as a whole. Different segments of customers within a market may behave differently—with some taking the lead in trying new products and, in turn, influencing others.

Promotion must vary for different adopter groups

Research on how markets accept new ideas has led to the adoption curve model. The **adoption curve** shows when different groups accept ideas. It shows the need to change the promotion effort as time passes. It also emphasizes the relations among groups and shows that individuals in some groups act as leaders in accepting a new idea.

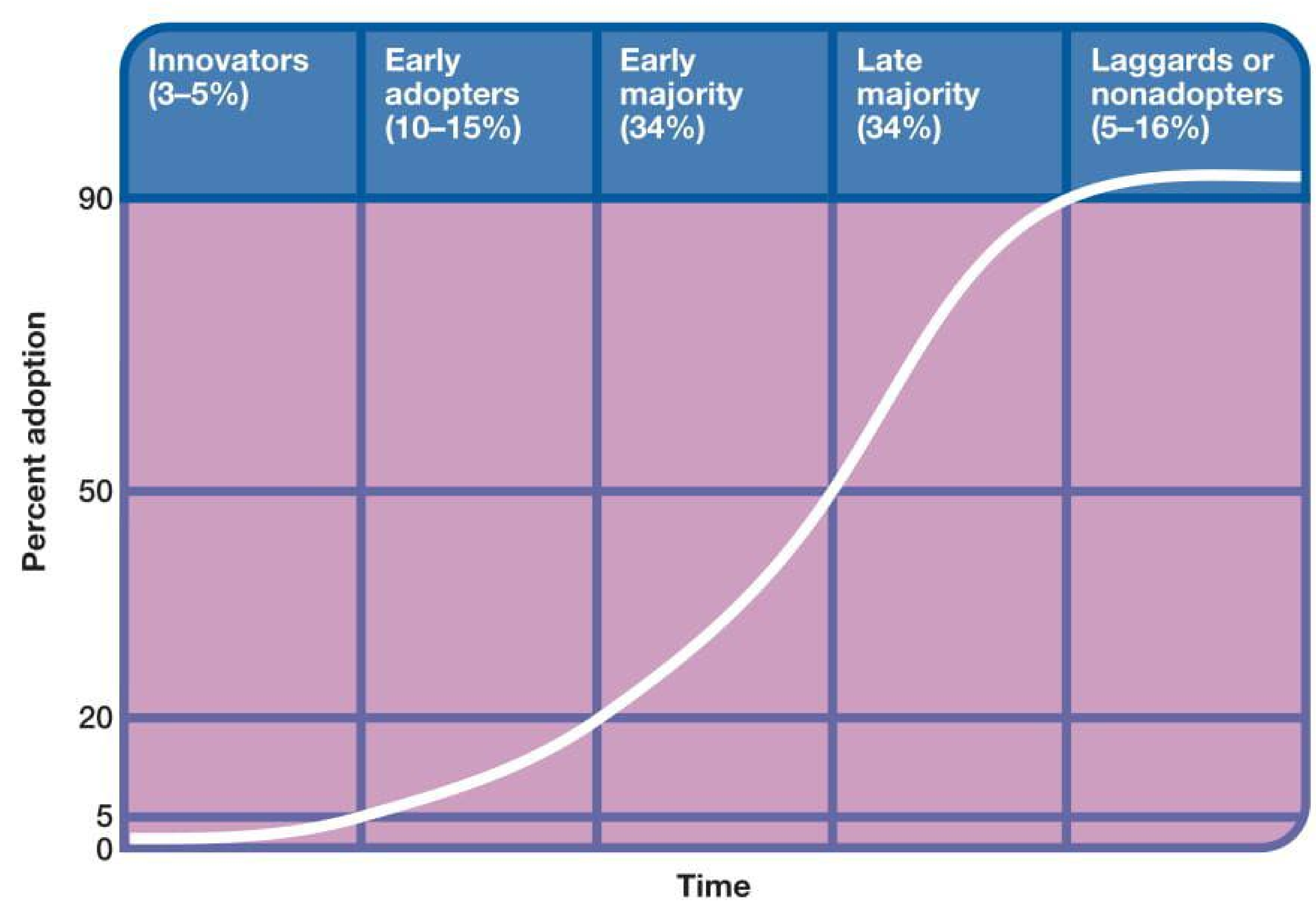
Exhibit 14-9 shows the adoption curve for a typical successful product. Some of the important characteristics of each of these customer groups are discussed below. Which one are you?

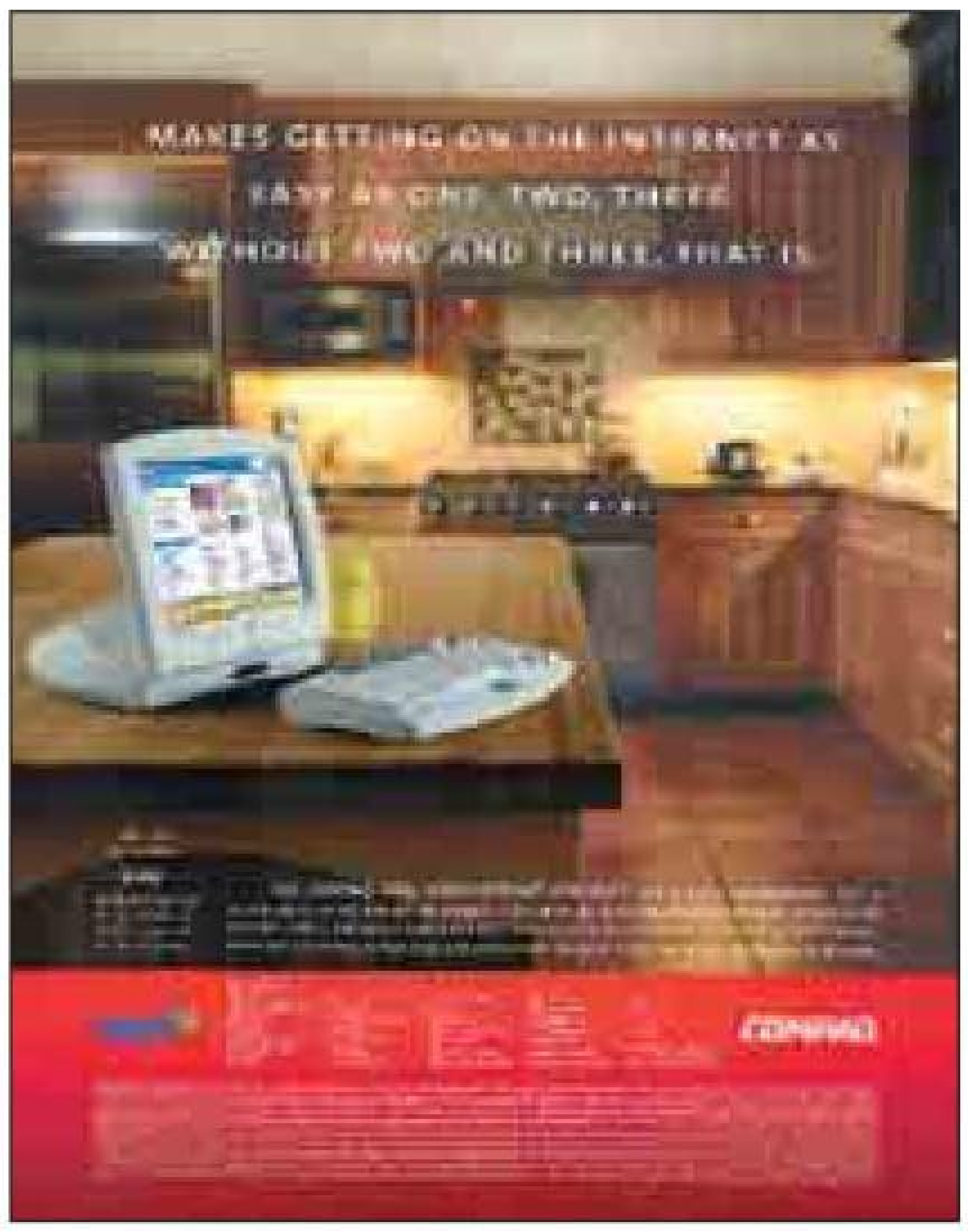
Innovators don't mind taking some risks

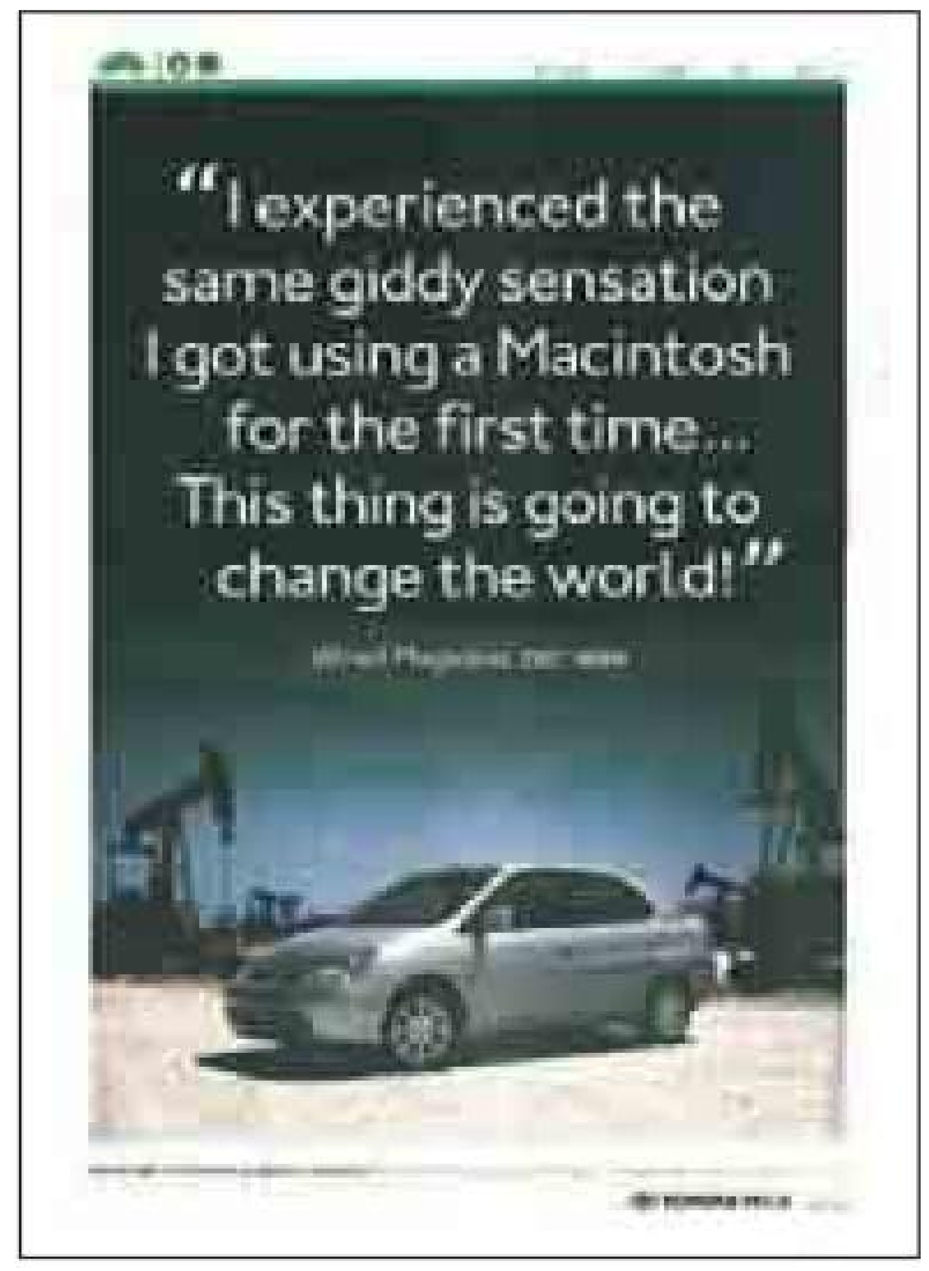
The **innovators** are the first to adopt. They are eager to try a new idea and willing to take risks. Innovators tend to be young and well educated. They are likely to be mobile and have many contacts outside their local social group and community. Business firms in the innovator group are often aggressive small companies with an entrepreneurial view and willingness to take the risk of doing something new and different. However, large firms, especially specialized ones, may be in the innovator group.

An important characteristic of innovators is that they rely on impersonal and scientific information sources, or other innovators, rather than salespeople. They often search for information. For example, they might do a search on the Internet, read articles in technical publications, or look for informative ads in special-interest magazines.

Exhibit 14-9
The Adoption Curve







Compaq is not targeting people who are Internet innovators but rather members of the late majority group who just want a hassle-free way to use e-mail as part of their everyday life. On the other hand, Toyota's Prius ad targets innovators and early adopters.

Early adopters are often opinion leaders

Early adopters are well respected by their peers and often are opinion leaders. They tend to be younger, more mobile, and more creative than later adopters. But unlike innovators, they have fewer contacts outside their own social group or community. Business firms in this category also tend to be specialized.

Of all the groups, this one tends to have the greatest contact with salespeople. Mass media are important information sources too. Marketers should be very concerned with attracting and selling the early adopter group. Their acceptance is really important in reaching the next group because the early majority look to the early adopters for guidance. The early adopters can help the promotion effort by spreading *word-of-mouth* information and advice among other consumers.

Opinion leaders help spread the word

Marketers know the importance of personal conversations and recommendations by opinion leaders. If early groups reject the product, it may never get off the ground. For example, some moviegoers are the first to see new movies. If they think a movie is dull, they quickly tell their friends not to waste their time and money. Consumers are even more likely to talk about a negative experience than a positive experience.

But if opinion leaders accept a product, what they say about it can be very important. Such word-of-mouth publicity may do the real selling job—long before the customer ever walks into the retail store. That's why some companies try to target promotion to encourage opinion leadership and word-of-mouth publicity.

The Internet is also providing companies, even small ones, with a low-cost way to encourage word of mouth. An interesting web page can attract attention—and customers can easily e-mail a copy to a friend. For example, a retail shop called Hot Hot Hot, which carries a very wide variety of hot sauces for food, established a website. Very quickly, largely because of word of mouth, 1,500 people were visiting the website each day.[16]

Early majority group is deliberate

The **early majority** avoid risk and wait to consider a new idea after many early adopters have tried it—and liked it. Average-sized business firms that are less specialized often fit in this category. If successful companies in their industry adopt the new idea, they will too.

Do You Hear That Buzz, and Where Is It Coming From?

Computer viruses can spread like wildfire. Some marketers are trying to get attention for their products by promoting the same kind of "viral" spread of word-of-mouth promotion from a small set of opinion leaders to other consumers. For example, BMW commissioned famous movie directors to create a series of short (about 5 minutes each) action films that show BMWs in high-performance chase action. The films are available for online viewing at www.bmwfilms.com. It would be impossible to show all of the dangerous stunts in TV ads. But car enthusiasts who hear about the site love the action and tell their friends to go check it out. It's all a well-planned effort to create more buzz about BMW as the ultimate driving machine.

Lee Dungarees used a complicated viral marketing campaign to try to build a cooler image among youthful males. Lee's agency e-mailed 200,000 computer game fans a trio of grainy video clips. The videos were supposedly intended to draw people to websites about three quirky characters. But the clips were so bad that they were funny. That was intentional. Many guys who received them forwarded them to friends. Little did they know that the odd characters in the videos would later be featured in an online computer game created by Lee. Gamers who figured out the connection with the videos passed the word and the popularity of the game spread across the Web. But to win at the game guys had to enter a secret code, which could only be found on Lee's jeans labels and required a visit to a store.

It's clear why a marketer might want target consumers to hear the buzz about a product from their coolest friends—and not just dismiss it as some commercial pitch. But often the intent is to mislead consumers about where the buzz starts. Some say that makes it unethical; others say that the marketer is only planting a few seeds and that it really is consumers who spread the word. Of course, this can backfire. Sony, for instance, got bad publicity for fabricating favorable movie reviews and portraying them as coming from movie critics.[17]

The early majority have a great deal of contact with mass media, salespeople, and early adopter opinion leaders. Members usually aren't opinion leaders themselves.

Late majority is cautious

The **late majority** are cautious about new ideas. Often they are older than the early majority group and more set in their ways. So they are less likely to follow opinion leaders and early adopters. In fact, strong social pressure from their own peer group may be needed before they adopt a new product. Business firms in this group tend to be conservative, smaller-sized firms with little specialization.

The late majority make little use of marketing sources of information—mass media and salespeople. They tend to be oriented more toward other late adopters rather than outside sources they don't trust.

Laggards or nonadopters hang on to tradition

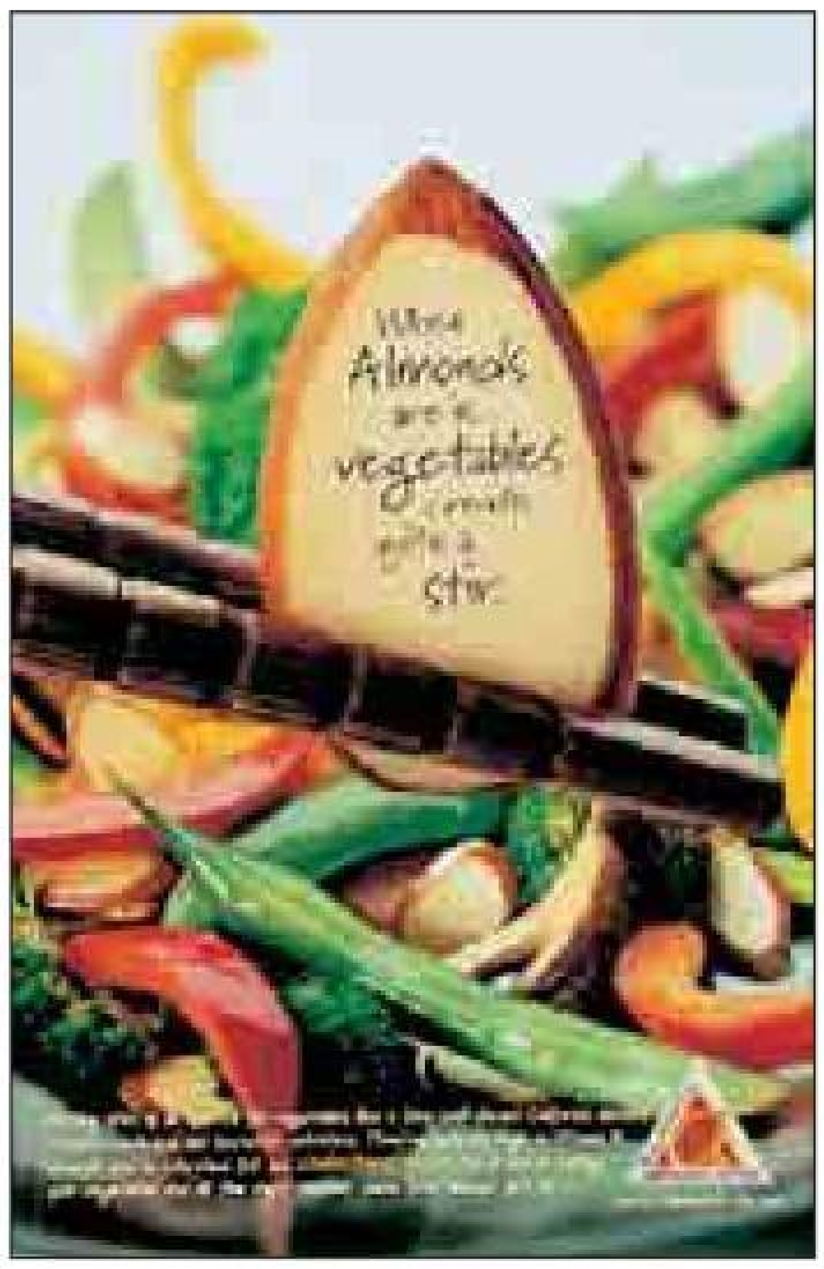
Laggards or **nonadopters** prefer to do things the way they've been done in the past and are very suspicious of new ideas. They tend to be older and less well educated. The smallest businesses with the least specialization often fit this category. They cling to the status quo and think it's the safe way.

The main source of information for laggards is other laggards. This certainly is bad news for marketers who are trying to reach a whole market quickly or who want to use only one promotion method. In fact, it may not pay to bother with this group.[18]

Promotion Blends Vary over the Life Cycle

Stage of product in its life cycle

A new product concept seldom becomes a spectacular success overnight. The adoption curve helps explain why. Further, the adoption curve helps explain why a new product goes through the product life-cycle stages described in Chapter 10—market introduction, market growth, market maturity, and sales decline. During these stages, promotion blends may have to change to achieve different promotion objectives.



These ads are not for individual brands but rather were placed as a cooperative effort by almond growers in California and apple producers in France to help build primary demand for their respective products.

Market introduction stage—"this new idea is good"

During market introduction, the basic promotion objective is informing. If the product is a really new idea, the promotion must build **primary demand**—demand for the general product idea—not just for the company's own brand. Video phone service and electric cars are good examples of product concepts where primary demand is just beginning to grow. There may be few potential innovators during the introduction stage, and personal selling can help find them. Firms also need salespeople to find good channel members and persuade them to carry the new product. Sales promotion may be targeted at salespeople or channel members to get them interested in selling the new product. And sales promotion may also encourage customers to try it.

Market growth stage—"our brand is best"

In the market growth stage, more competitors enter the market, and promotion emphasis shifts from building primary demand to stimulating **selective demand**—demand for a company's own brand. The main job is to persuade customers to buy, and keep buying, the company's product.

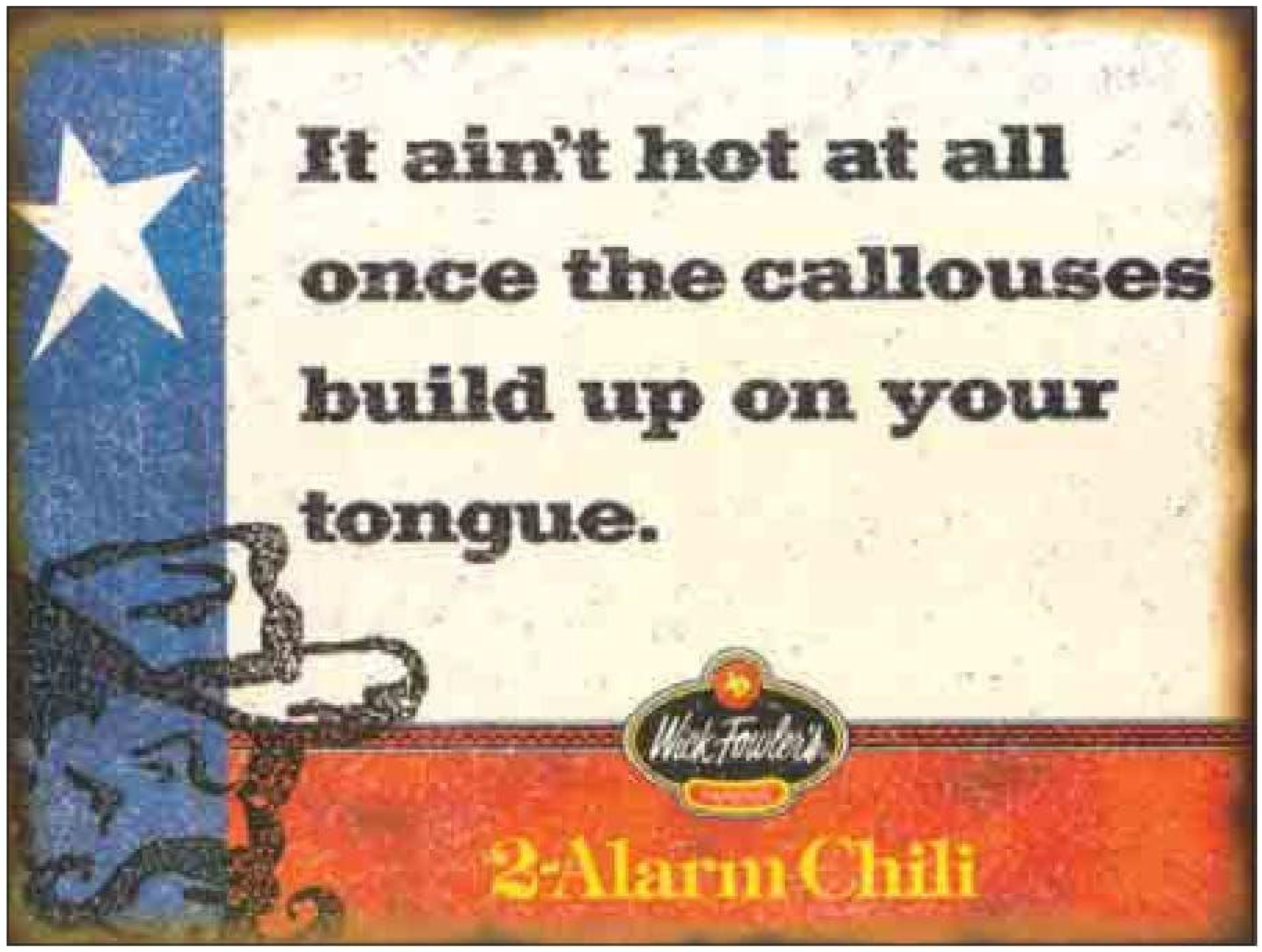
Now that more potential customers are trying and adopting the product, mass selling may become more economical. But salespeople and personal selling must still work in the channels—expanding the number of outlets and cementing relationships with current channel members.

Market maturity stage—"our brand is better, really"

In the market maturity stage, even more competitors have entered the market. Promotion becomes more persuasive. At this stage, mass selling and sales promotion may dominate the promotion blends of consumer products firms. Business products may require more aggressive personal selling—perhaps supplemented by more advertising. The total dollars allocated to promotion may rise as competition increases.

If a firm already has high sales—relative to competitors—it may have a real advantage in promotion at this stage. If, for example, Nabisco has twice the sales for a certain type of cookie as Keebler, its smaller competitor, and they both spend the same *percentage* of total sales on promotion, Nabisco will be spending twice as much and will probably communicate to more people. Nabisco may get even more than twice as much promotion because of economies of scale.

Firms that have strong brands can use reminder-type advertising at this stage. Similarly, many firms turn to various types of frequent-buyer promotions or newsletters targeted at current customers to strengthen the relationship and keep customers loyal. This may be less costly and more effective than efforts to win customers away from competitors.



This ad uses humor to highlight what's distinctive about 2-Alarm Chili—to stimulate selective demand in a very competitive market.

Sales decline stage—"let's tell those who still want our product"

During the sales decline stage, the total amount spent on promotion usually decreases as firms try to cut costs to remain profitable. Since some people may still want the product, firms need more targeted promotion to reach these customers.

On the other hand, some firms may increase promotion to try to slow the cycle—at least temporarily. Crayola had almost all of the market for children's crayons, but sales were slowly declining as new kinds of markers came along. Crayola increased ad spending to urge parents to buy their kids a "fresh box."

Nature of competition requires different promotion

Firms in monopolistic competition may favor mass selling because they have differentiated their marketing mixes and have something to talk about. As a market tends toward pure competition, or oligopoly, it is difficult to predict what will happen. Competitors in some markets try to outpromote each other. The only way for a competitor to stay in this kind of market is to match rivals' promotion efforts—unless the whole marketing mix can be improved in some other way. We see a lot of such competitive advertising in our daily newspapers and in cents-off coupons at grocery store checkout counters.

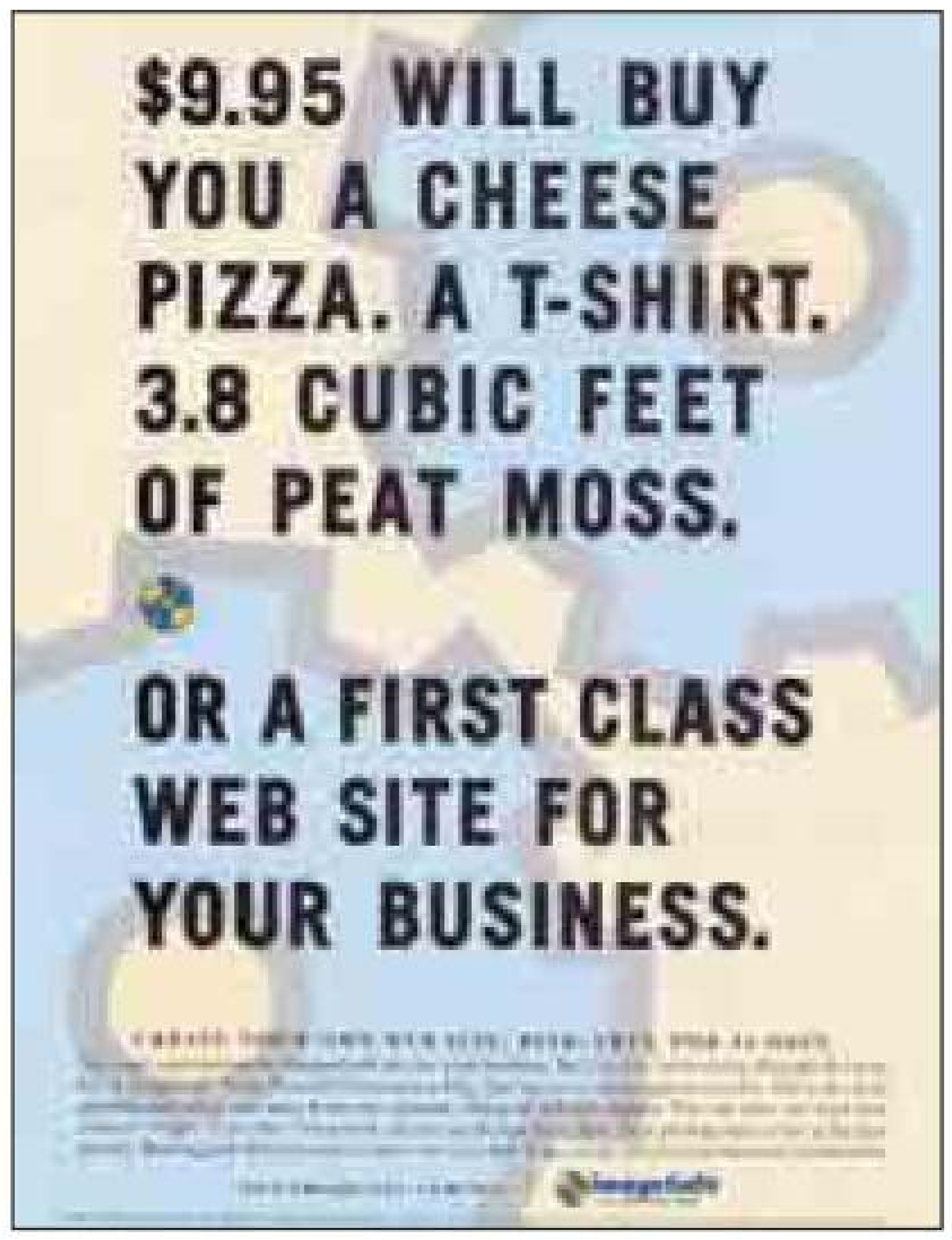
In markets that are drifting toward pure competition, some companies resort to price-cutting. This *may* temporarily increase the number of units sold, but it may also reduce total revenue and the amount available for promotion *per unit.* And competitive retaliation, perhaps in the form of short-term sales promotions, may reduce the temporary sales gains and drag price levels down faster. As cash flowing into the business declines, spending may have to be cut back.[19]

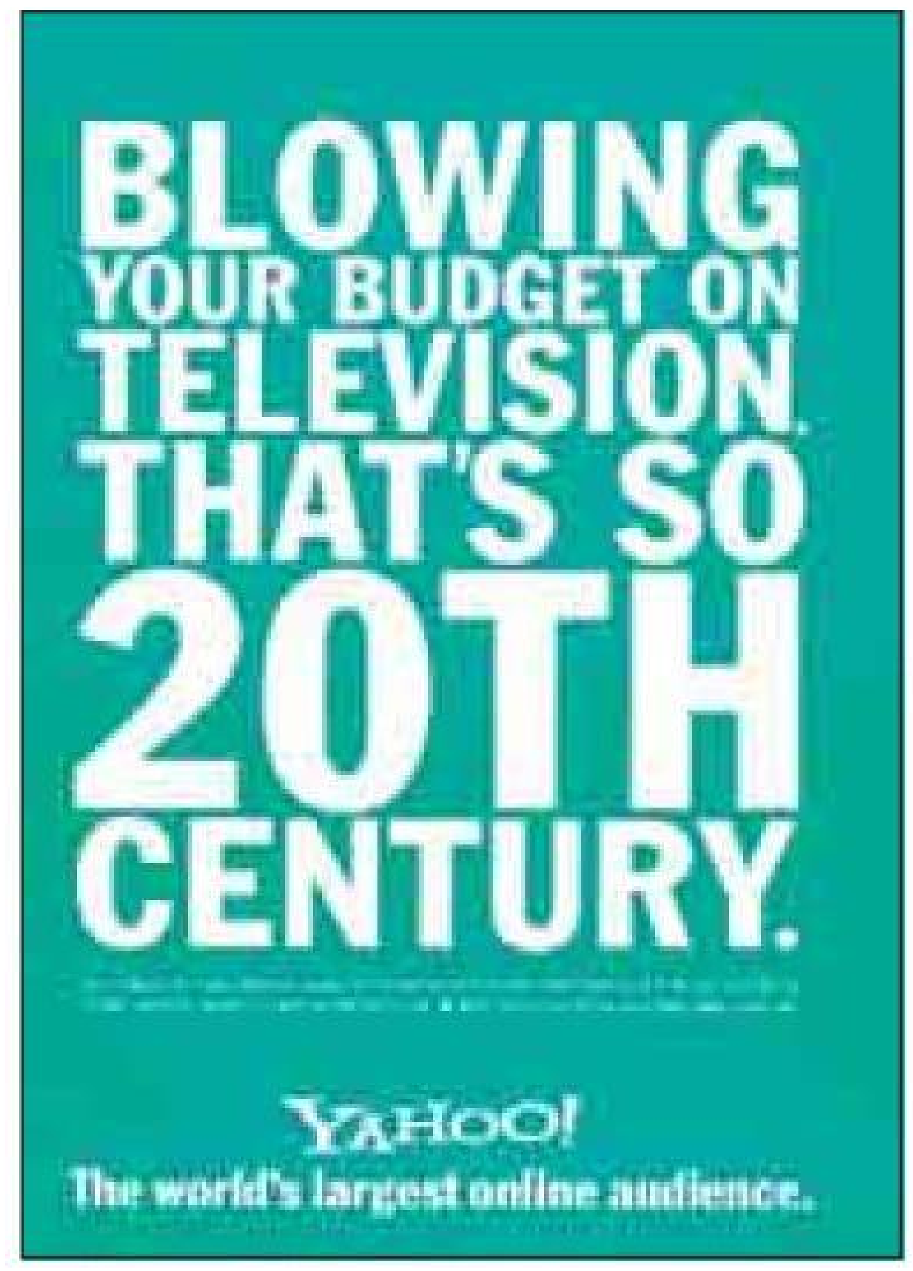
Setting the Promotion Budget

Size of budget affects promotion efficiency and blend

There are some economies of scale in promotion. An ad on national TV might cost less *per person* reached than an ad on local TV. Similarly, citywide radio, TV, and newspapers may be cheaper than neighborhood newspapers or direct personal

Many marketing managers now view promotion on the Internet as a "must buy" in a promotion budget.





contact. But the *total cost* for some mass media may force small firms, or those with small promotion budgets, to use promotion alternatives that are more expensive per contact. For example, a small retailer might want to use local television but find that there is only enough money for a web page, an ad in the Yellow Pages, and an occasional newspaper ad.

Smaller producers and firms that offer relatively undifferentiated consumer products emphasize personal selling first and rely mainly on sales promotion for the balance. The objective is to build good channel relations and encourage channel members to recommend and push the product. Note that here we are referring to percentages in the promotion blend, not the level of expenditures. Setting the overall level of promotion spending and how much to spend on each type of promotion is an important but difficult decision.

Budgeting for promotion—50 percent, 30 percent, or 10 percent is better than nothing

The most common method of budgeting for promotion expenditures is to compute a percentage of either past sales or sales expected in the future. The virtue of this method is its simplicity. A similar percentage can be used automatically each year—eliminating the need to keep evaluating the kind and amount of promotion effort needed and its probable cost. However, when a company's top managers have this attitude, they often get what they deserve—something less than the best results.

Find the task, budget for it

Just because budgeting a certain percentage of past or forecast sales is common doesn't mean that it's smart. This mechanical approach leads to expanding marketing expenditures when business is good and cutting back when business is poor. It may be desirable to increase marketing expenditures when business is good. But when business is poor, this approach may just make the problem worse—if weak promotion is the reason for declining sales. The most sensible approach may be to be *more*, not less, aggressive!

Other methods of budgeting for marketing expenditures are:

1. Match expenditures with competitors.
2. Set the budget as a certain number of cents or dollars per sales unit (by case, by thousand, or by ton) using the past year or estimated year ahead as a base.
3. Base the budget on any uncommitted revenue, perhaps including budgeted profits. Companies with limited resources may use this approach. Or a firm may be willing to sacrifice some or all of its current profits for future sales—that is, it looks at promotion spending as an *investment* in future growth.

4. Base the budget on the job to be done. For example, the spending level might be based on the number of new customers desired and the percentage of current customers that the firm must retain to leverage investments in already established relationships. This is called the **task method**—basing the budget on the job to be done.

Task method can lead to budgeting without agony

In the light of our continuing focus on planning marketing strategies to reach objectives, the most sensible approach to budgeting promotion expenditures is the task method. In fact, this approach makes sense for *any* marketing expenditure, but here we'll focus on promotion.

A practical approach is to determine which promotion objectives are most important and which promotion methods are most economical and effective for the communication tasks relevant to each objective. There's never enough money to do all of the promotion that you might want to do. However, this approach helps you to set priorities so that the money you spend produces specific results.

The amount budgeted using the task method can be stated as a percentage of sales. But you should see that calculating the right amount is more involved than picking up a past percentage. It requires careful review of the specific promotion (and marketing) tasks to be accomplished and how each task fits with others to achieve the overall objectives. The costs of these tasks are then totaled—to determine how much should be budgeted for promotion (just as money is allocated for other marketing activities required by the strategy). In other words, the firm can assemble its total promotion budget directly from detailed plans rather than by simply relying on historical patterns or ratios.

This method also helps to eliminate budget fights between different promotion areas. Such conflicts may occur if managers and specialists responsible for different promotion methods see themselves as pitted against each other for limited budget dollars. Instead, the task method of budgeting encourages everyone to focus on the overall strategy and what promotion objectives need to be achieved. The specialists may still make their own suggestions about how to perform tasks. But then the budget allocations are based on the most effective ways of getting things done, not on what the firm did last year, what some competitor does, or even on internal politics. With this approach, different promotion specialists are also more likely to recognize that they must all work together to achieve truly integrated marketing communications.[20]

Conclusion

Promotion is an important part of any marketing mix. Most consumers and intermediate customers can choose from among many products. To be successful, a producer must not only offer a good product at a reasonable price but also inform potential customers about the product and where they can buy it. Further, producers must tell wholesalers and retailers in the channel about their product and their marketing mix. These middlemen, in turn, must use promotion to reach their customers.

The promotion blend should fit logically into the strategy being developed to satisfy a particular target market. Strategy planning needs to state *what* should be communicated to them and *how*. The overall promotion objective is to affect buying behavior, but the basic promotion objectives are informing, persuading, and reminding.

Three basic promotion methods can be used to reach these objectives. Behavioral science findings can help firms combine various promotion methods for effective communication. In particular, what we know about the communication process and how individuals and groups adopt new products is important in planning promotion blends.

An action-oriented framework called AIDA can help marketing managers plan promotion blends. But the marketing manager has the final responsibility for combining the promotion methods into one integrated promotion blend for each marketing mix.

In this chapter, we considered some basic concepts that apply to all areas of promotion. In the next two chapters, we'll discuss personal selling, advertising, and sales promotion in more detail.

Questions and Problems

1. Briefly explain the nature of the three basic promotion methods available to a marketing manager. What are the main strengths and limitations of each?
2. In your own words, discuss the integrated marketing communications concept. Explain what its emphasis on "consistent" and "complete" messages implies with respect to promotion blends.
3. Relate the three basic promotion objectives to the four jobs (AIDA) of promotion using a specific example.
4. Discuss the communication process in relation to a producer's promotion of an accessory product—say, a new electronic security system businesses use to limit access to areas where they store confidential records.
5. If a company wants its promotion to appeal to a new group of target customers in a foreign country, how can it protect against its communications being misinterpreted?
6. Promotion has been the target of considerable criticism. What specific types of promotion are probably the object of this criticism? Give a specific example that illustrates your thinking.
7. With direct-response promotion, customers provide feedback to marketing communications. How can a marketing manager use this feedback to improve the effectiveness of the overall promotion blend?
8. How can a promotion manager target a message to a certain target market with electronic media (like the Internet) when the customer initiates the communication? Give an example.
9. What promotion blend would be most appropriate for producers of the following established products? Assume average- to large-sized firms in each case and support your answer.
   a. Chocolate candy bar.
   b. Car batteries.
   c. Panty hose.
   d. Castings for truck engines.
   e. A special computer used by manufacturers for control of production equipment.
   f. Inexpensive plastic rainhats.
   g. A digital tape recorder that has achieved specialty-product status.
10. A small company has developed an innovative new spray-on glass cleaner that prevents the buildup of electrostatic dust on computer screens and TVs. Give examples of some low-cost ways the firm might effectively promote its product. Be certain to consider both push and pull approaches.
11. Would promotion be successful in expanding the general demand for: *(a)* almonds, *(b)* air travel, *(c)* golf clubs, *(d)* walking shoes, *(e)* high-octane unleaded gasoline, *(f)* single-serving, frozen gourmet dinners, and *(g)* bricks? Explain why or why not in each case.
12. Explain how an understanding of the adoption process would help you develop a promotion blend for digital tape recorders, a new consumer electronics product that produces high-quality recordings. Explain why you might change the promotion blend during the course of the adoption process.
13. Explain how opinion leaders affect a firm's promotion planning.
14. Discuss how the adoption curve should be used to plan the promotion blend(s) for a new automobile accessory—an electronic radar system that alerts a driver if he or she is about to change lanes into the path of a car that is passing through a blind spot in the driver's mirrors.
15. If a marketing manager uses the task method to budget for marketing promotions, are competitors' promotion spending levels ignored? Explain your thinking and give an example that supports your point of view.
16. Discuss the potential conflict among the various promotion managers. How could this be reduced?

Suggested Cases

18. State Bank
19. myWedding.com

Computer-Aided Problem

14. Selecting a Communications Channel

Helen Troy, owner of three Sound Haus stereo equipment stores, is deciding what message channel (advertising medium) to use to promote her newest store. Her current promotion blend includes direct-mail ads that are effective for reaching her current customers. She also has knowledgeable salespeople who work well with consumers once they're in the store. However, a key objective in opening a new store is to attract new customers. Her best prospects are professionals in the 25–44 age range with incomes over $38,000 a year. But only some of the people in this group are audiophiles who want the top-of-the-line brands she carries. Troy has decided to use local advertising to reach new customers.

Troy narrowed her choice to two advertising media: an FM radio station and a biweekly magazine that focuses on entertainment in her city. Many of the magazine's readers are out-of-town visitors interested in concerts, plays, and restaurants. They usually buy stereo equipment at home. But the magazine's audience research shows that many local professionals do subscribe to the magazine. Troy doesn't think that the objective can be achieved with a single ad. However, she believes that ads in six issues will generate good local awareness with her target market. In addition, the magazine's color format will let her present the prestige image she wants to convey in an ad. She thinks that will help convert aware prospects to buyers. Specialists at a local advertising agency will prepare a high-impact ad for $2,000, and then Troy will pay for the magazine space.

The FM radio station targets an audience similar to Troy's own target market. She knows repeated ads will be needed to be sure that most of her target audience is exposed to her ads. Troy thinks it will take daily ads for several months to create adequate awareness among her target market. The FM station will provide an announcer and prepare a tape of Troy's ad for a one-time fee of $200. All she has to do is tell the station what the message content for the ad should say.

Both the radio station and the magazine gave Troy reports summarizing recent audience research. She decides that comparing the two media in a spreadsheet will help her make a better decision.

a. *Based on the data displayed on the initial spreadsheet, which message channel (advertising medium) would you recommend to Troy? Why?*

b. *The agency that offered to prepare Troy's magazine ad will prepare a fully produced radio ad—including a musical jingle—for $2,500. The agency claims that its musical ad will have much more impact than the ad the radio station will create. The agency says its ad should produce the same results as the station ad with 20 percent fewer insertions. If the agency claim is correct, would it be wise for Troy to pay the agency to produce the ad?*

c. *The agency will not guarantee that its custom-produced radio ad will reach Troy's objective—making 80 percent of the prospects aware of the new store. Troy wants to see how lower levels of awareness—between 50 percent and 70 percent—would affect the advertising cost per buyer and the cost per aware prospect. Use the feature analysis to vary the percent of prospects who become aware. Prepare a table showing the effect on the two kinds of costs. What are the implications of your analysis?*

For additional questions related to this problem, see Exercise 14-3 in the *Learning Aid for Use with Basic Marketing*, 14th edition.