PRINCIPLES OF MARKETING / 15

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Based on Ph. Kotler's Principles of marketing / international edition, and miscellaneous designer's lecturing materials

3R Business Development Consultancy

MANAGING MARKETING CHANNELS

The nature of distribution channels

- Importance of managing marketing channels
  - Marketing channel decisions are among the most important decisions that management faces.
    A company's channel decisions are linked with every other marketing decision.
    Pricing depends on whether it makes use of mass merchandising or high-quality specialty stores.
    The company's sales force and advertising decisions depend on how much persuasion, training and motivation the dealers or resellers need.

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MANAGING MARKETING CHANNELS

The nature of distribution channels

- Why are marketing intermediaries used?
  - The use of intermediaries results from their greater efficiency in making goods available to target markets.
    Through their contacts, experiences, specializations and scale of operation, intermediaries usually offer the firm more than it can achieve on its own.
    This not only applies to tangible products.
    Producers of services (such as insurers) and ideas (like many non-profit organizations) also face the problem of making their services available to larger target groups.

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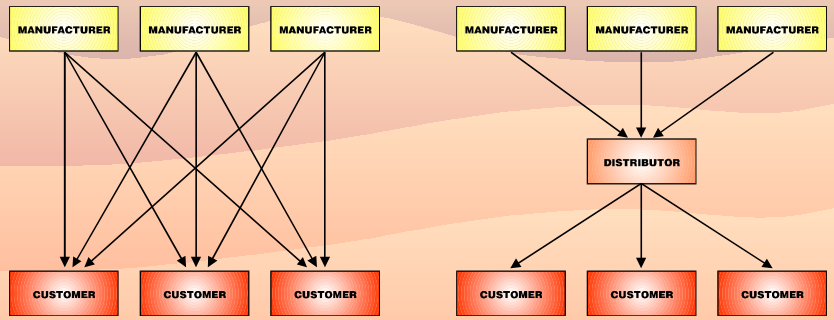
MANAGING MARKETING CHANNELS

The nature of distribution channels

- **Why are marketing intermediaries used?**



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MANAGING MARKETING CHANNELS

The nature of distribution channels

- **Marketing channel functions**
  - **Distribution channels fill the main time, place and possession gaps that separategoods and services from potential users.**
  - **Main functions:**
    - **Information gathering (market research)**
    - **Promotion**
    - **Contact with prospective buyers**
    - **Matching (assembling, packaging, fitting)**
    - **Negotiation with prospective buyers**
    - **Physical distribution (of final products)**
    - **Financing channel work costs**
    - **Risk taking of carrying out channel work.**

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MANAGING MARKETING CHANNELS

The nature of distribution channels

- **Number of channel levels**
  - **The number of intermediary levels indicates the length of a channel.**
    Some distribution situations call for the use of *direct-marketing channels* with no intermediary levels, and others call for *indirect-marketing channels*, involving one or several intermediary levels.
    In any case, distribution channels will involve certain *physical flows of products*, certain *flows of ownership*, certain *information flows*, *payment flows*, *information flows* and *promotion flows*.

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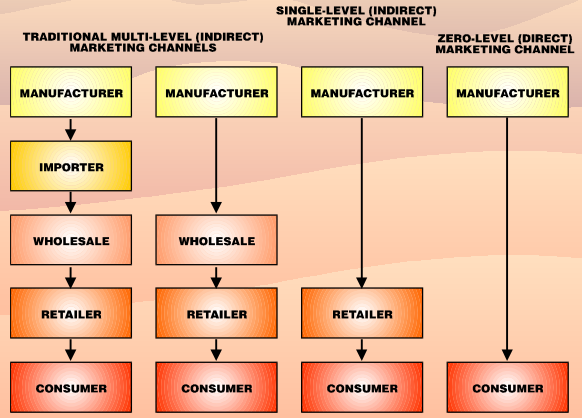
MANAGING MARKETING CHANNELS

The nature of distribution channels

- **Number of channel levels**



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MANAGING MARKETING CHANNELS

Channel behaviour and organization

- **Channel behaviour**
  - **Distribution channels consist of firms that have banded together and that depend on each other to achieve a common goal.**
    The ultimate success of for ex. an individual *Sony* dealer, depends on how well the entire *Sony* distribution channel competes with channels of other electronics maufacturers.
    ***Ideally*, in order to achieve these mutual successes, *all channel firms should work together smoothly* to secure healthy margins or profitable sales, understanding and accepting their particular roles.**

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MANAGING MARKETING CHANNELS

Channel behaviour and organization

- **Channel behaviour**
  - **Unfortunately, individual channel members rarely see business this way. They often disagree on the roles each should play: *who should do what for what rewards*.**
    Such disagreements over goals and roles generate channel conflicts on 2 levels:
    - **horizontal conflict: ex.: *Sony* dealers in a certain region might complain about the aggressive pricing of other Sony dealers in that area.**
    - **vertical conflict: ex.: *Sony*'s dealers might start to complain about Sony's direct sales to consumers through the Internet.**

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MANAGING MARKETING CHANNELS

Channel behaviour and organization

- **Channel organization**
  - Historically, distribution channels have been *loose collections of independent firms*, each showing little concern for overall channel performance. These conventional distribution channels have lacked strong leadership, and have been troubled by conflicts and poor performance.
    Conventional distribution channels consist of 1 or more independent producers, wholesalers and retailers, each a separate business seeking to maximize its own profits, *even at the expense of profits for the system as a whole* (!).

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MANAGING MARKETING CHANNELS

Channel behaviour and organization

- **Channel organization**
  - In contrast, a vertical marketing system (VMS) consists of producers, wholesalers and retailers, acting as a unified system. And furthermore, one channel member owns the others, has contracts with them, or has so much power that they all cooperate.
    Such *VMS's can be dominated by a producer, a wholesaler or even by a retailer*.

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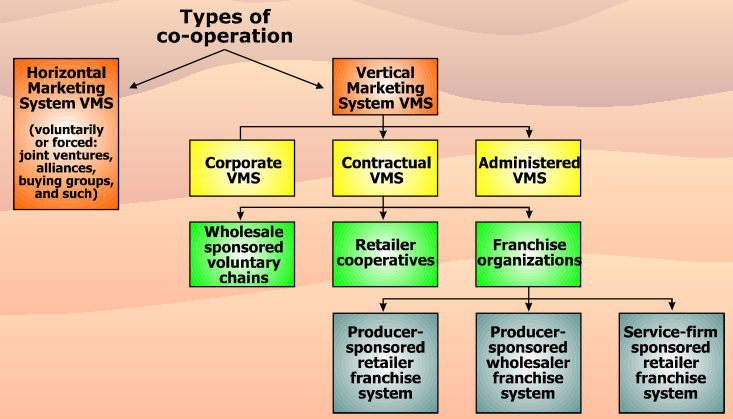
MANAGING MARKETING CHANNELS

Channel behaviour and organization

- **Channel organization**



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MANAGING MARKETING CHANNELS

Channel behaviour and organization

- **Channel organization**
  - **Corporate VMS: a vertical marketing system that combines successive stages of production and distribution under single ownership; channel leadership is established through common ownership.**

    Gasoline (petrol) distribution through chains of gasoline stations owned by the oil company is an example of delivery and control achieved by such a system. Other examples are the car industry & vehicle rental companies, and beer breweries & pubs.

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MANAGING MARKETING CHANNELS

Channel behaviour and organization

- **Channel organization**
  - **Contractual VMS: a vertical marketing system in which independent firms at different levels of production and distribution join together through contracts to obtain more economies or sales impact than they could achieve alone.**

    There are 3 types of contractual VMS's:
    - **wholesale sponsored voluntary chains**
    - **retailer cooperatives**
    - **franchise organizations.**

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MANAGING MARKETING CHANNELS

Channel behaviour and organization

- **Channel organization**
  - **Wholesale sponsored voluntary chains: here wholesalers organize voluntary chains of *independent retailers* to help them compete with large chain organizations. This involves developing programmes in which independent retailers (such as US' IGA / Independent Grocers Alliance) standardize their selling practices and achieve buying economies that let the group compete effectively with chain organizations.**

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MANAGING MARKETING CHANNELS

Channel behaviour and organization

- **Channel organization**
  - **Retailer cooperatives: involves *groups of independent resellers* who band together to *own wholesale operations jointly*, or to conduct joint wholesaling and possible production.**
    Here, small independent retailers, often such as supermarkets and drugstores, form an organization that operates a wholesale facility cooperatively.
    Member retailers then concentrate their buying power through the wholesaler and plan collaborative promotional and pricing activities.

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MANAGING MARKETING CHANNELS

Channel behaviour and organization

- **Channel organization**
  - **Franchise organizations: involve contractual associations between *franchisers* (manufacturers, wholesalers or service organizations) and independent channel members (the *franchisee's*) who buy the right to sell the franchisers's branded product or service.**
    Almost every kind of business is being franchised, from hotels and fast-food restaurants to dental and garden maintenance services, from management training consultants and supermarkets to funeral businesses and fitness centres.

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MANAGING MARKETING CHANNELS

Channel behaviour and organization

- **Channel organization**
  - **Franchise organizations:**
    ***Main advantages for the franchiser*:**
    - **fast distribution for its products and services without the costs of setting up and running own operations**
    - **highly motivated, self-employed franchisee's**
    - **contractual relationship ensuring operation and sustained standards.**

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MANAGING MARKETING CHANNELS

Channel behaviour and organization

- Channel organization
  - Franchise organizations:

    Main advantages for the franchisee:
    - buying into a proven system (when selling an established brand name such as McDonald's, The Body Shop, Starbuck's, etc.)
    - start-up of a business with limited capital plus the benefit from the franchiser's experience
    - benefits of centralized purchasing power as franchisers buy in bulk for their franchisee's
    - instant expertise in operational issues such as advertising, promotions, accounts and legal matters.

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MANAGING MARKETING CHANNELS

Channel behaviour and organization

- Channel organization
  - Franchise organizations:

    Main disadvantages of franchise systems:
    - franchisers invariably have to give up some control when operating through franchisee's
    - some franchisee's might not perform to the franchiser's operating standards, perhaps damaging the brand name by doing so
    - franchisee's may not always have a good deal as they have to work extremely hard in order to make the business pay, and although they have already paid their initial fee, there might be royalty payments to be paid, as well.

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MANAGING MARKETING CHANNELS

Channel behaviour and organization

- Channel organization
  - Franchise organizations:

    There are 3 types of franchise:
    - manufacturer-sponsored retailer franchise system, ex.: car manufacturers such as *BMW*, *Mitsubishi*, and their dealers.
    - manufacturer-sponsored wholesaler franchise system, ex.: *Coca-Cola* and its licenced bottlers (wholesalers).
    - service-firm sponsored retailer franchise system, ex.: car rental business (*Hertz*, *Avis*, *Europcar*) or fast-food (*McDonald's*, *Burger King*), or hotels (*Holiday Inn*, *Ramada Inn*).

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MANAGING MARKETING CHANNELS

Channel behaviour and organization

- **Channel organization**
  - **Administered Vertical Marketing System: a VMS that coordinates successive stages of production and distribution, not through common ownership or contractual ties, but through the size and power of one of the parties.**
    Example: in the *FMCG market*, companies such as *Nestlé*, *Unilever*, *Proctor & Gamble*, *Masterfoods*, etc. can command unusual cooperation from resellers regarding shelf space, displays, promotions and price policies.
    Likewise, *IKEA* exerts strong influence on the manufacturers of their products.

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MANAGING MARKETING CHANNELS

Channel behaviour and organization

- **Channel organization**
  - **Horizontal Marketing System: involves a channel arrangement in which 2 or more companies at one level, join together to follow a new marketing opportunity.**
    Such a joint venture can be done by combining, for instance, capital, production capabilities, or marketing resources.
    Also, these co-operations might involve joining with competitors (*Philips-JVC-Sony*, *HP-IBM*, etc.) or non-competitors, on a temporary or sometimes permanent basis, or even by creating a separate company (joint ventures).

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MANAGING MARKETING CHANNELS

Channel behaviour and organization

- **Channel organization**
  - **Hybrid Marketing System: is often known as multichannel distribution system, and occurs when a single company sets up 2 or more marketing channels to reach one or more customer segments. A variety of direct and indirect approaches are used to deliver the company's goods or services to its customers (example: various banks and insurance companies).**
    Although this allows the company to expand its sales and market coverage, the system is harder to control, and could easily lead to *conflicts* within the channels.

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MANAGING MARKETING CHANNELS

Channel behaviour and organization

- Channel organization
  - Changing channel organization:
    Changes in technology and the explosive growth of direct and online marketing are having an enormous impact on the nature and design of marketing channels, often resulting in disintermediation.
    This involves the by-passing of intermediaries and going directly to final buyers (think of *Dell Computers*), or acquiring radically new types of channel intermediaries (such as e-commerce merchants) to replace the traditional ones.

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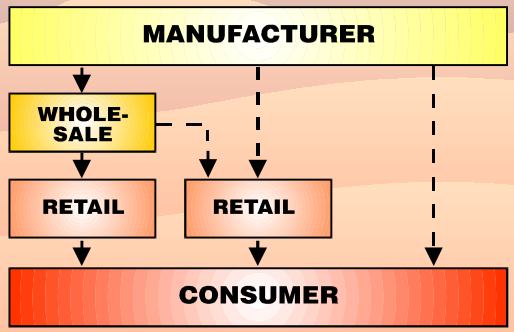
Channel behaviour and organization

- Channel organization
  - Changing channel organization: possible inter-channel & intra-channel conflicts (example):



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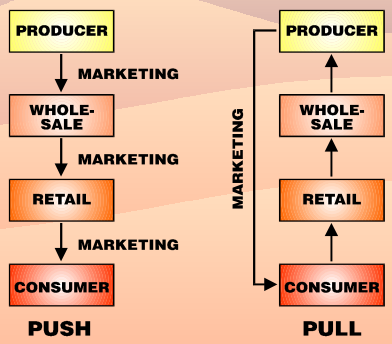
Channel behaviour and organization

- Channel organization
  - Changing channel organization: push- versus pull-strategy:



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MANAGING MARKETING CHANNELS

Channel design decisions

- **Major determining factors of channel length**

Internal factors:

- Company's objectives (market position, market share, cost levels, etc.)
- Company's position (finance, market power, etc.)
- Manufacturing factors (Expiration dates, range of products, etc.)
- Pricing characteristics (value & margins of products)
- Marketing mix (links to other P's such as exclusiveness)

External factors:

- Customer characteristics (amount, locations, buying patterns, sales / customer, etc.)
- Distribution factors (availability and willingness of distributors, power ratio's)
- Competition factors (competitor's strategies, market power, etc.)
- Macro environmental factors (technological, political, etc.)

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Types of channel alternatives**
  - **Direct marketing**: marketing through various advertising media that interact directly with consumers, generally calling for the consumer to make a direct response.
    DM will involve selling via advertisements in print media, on radio or TV, by mail order and catalogues, and selling through telephone and internet.

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Types of channel alternatives**
  - **Sales force**: also, the company can choose to sell directly through its own sales force or even deploy *another firm's* sales force.
    Alternatively, a contract sales force might be used in certain circumstances.
  - **Intermediaries**: the independent organizations that will carry out a number of activities.
    These include *wholesalers* and *retailers* who buy, take title to, and resell the company's goods.

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MANAGING MARKETING CHANNELS

Channel design decisions

- Tasks and types of wholesalers
  - Among the tasks wholesalers perform, are:
    - selecting items, and reduction of quantities
    - conducting and supervising sales and marketing (promotions)
    - building needed assortments
    - holding inventories
    - arranging and conducting transportation
    - financing by providing credit to their customers, and by paying their suppliers promptly
    - absorbing risk by taking responsibility
    - providing management and marketing (information) services.

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MANAGING MARKETING CHANNELS

Channel design decisions

- Tasks and types of wholesalers
  - Merchant wholesalers: independently owned businesses that take title to the merchandise they handle.
    These wholesalers operate as *full-service wholesalers*, or as *limited-service wholesalers*, depending on the number of services they offer (the tasks they are willing to fulfill).

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MANAGING MARKETING CHANNELS

Channel design decisions

- Tasks and types of wholesalers
  - Brokers and agents: differ from merchant wholesalers, as they do not take title to goods, and only perform a few functions.
    Brokers bring buyers and sellers together and assist in negotiations.
    Agents represent buyers or sellers on a permanent basis.
    In most cases brokers and agents get paid through commissions.
  - Another type of wholesaling is that done by manufacturers' sales branches and offices (also known as *service-merchandising*).

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Tasks and types of retailers**
  - **Among the many tasks retailers perform, are:**
    - **selecting items, and reduction of quantities**
    - **dividing products into certain qualities**
    - **holding inventories**
    - **providing pre-sales services, sales-services, and after-sales services**
    - **financing by providing credit to their customers, and collecting money through payments by their customers**
    - **(re-)packaging and internal transportation of products, etc.**

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Tasks and types of retailers**
  - **Different products require different amounts of service, and customer service preferences may differ considerably.**
    Self-service retailers **cater for customers who are willing to perform their own 'search & select' process to save money (supermarkets, discount-stores, etc.).**
    Limited-service retailers **provide more service and sales assistance due to the amount of shopping goods they sell; customers usually need more information regarding these products (as in regular department stores).**

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Tasks and types of retailers**
  - ***Full-service retailers*** **assist customers in every phase of the shopping process. They usually carry more specialty goods and slower moving objects, such as cameras, jewellery and fashions, for which customers like to be 'waited on'.**
    They provide more services, resulting in much higher operating costs, which are obviously passed along to customers as higher prices.
    Examples: up-market department stores, specialty stores, etc.

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Main types of retailers**
  - **Specialty store: a retail store that carries a narrow product line with a deep assortment within that line (ex.: lingerie shops).**
  - **Department store: a retail organization that carries a wide variety of product lines (such as clothing, home furnishing and household goods); each line is operated as a separate department managed by specialist sellers or merchandisers (ex.: *Harrods*, *Bloomingdale*, *Debenhams*, etc.)**

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Channel design decisions

- **Main types of retailers**
  - **Convenience store: a small store located near a residential area that is open long hours, 7 days a week, and carries a limited line of high-turnover convenience goods (ex.: 'evening stores')**
  - **Supermarkets: large, low-cost, low-margin, high-volume, self-service stores that carry a wide variety of food, laundry and household products.** >>

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Main types of retailers**
  - **Superstore: a store about twice the size of a regular supermarket that carries a large assortment of routinely purchased food and non-food items, and offering such services as dry cleaning, post offices, film developing, ATM's, gas-stations, and self-serviced car-washing facilities (ex.: smaller *Sainsbury's*, *Tesco's*, and *Asda's*, etc.).**

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Main types of retailers**
  - **Category killer: a modern 'breed' of exceptionally aggressive 'off-price' retailers that offer branded merchandise in clearly defined product categories at heavily discounted prices (ex.: *Toys 'R' us*).**
  - **Hypermarkets: huge stores that combine supermarket, discount and warehouse retailing. In addition to food, they carry furniture, appliances, clothing, and many other non-food products (ex.: *Tesco's*, *Sainsbury's*, *Carrefour's*, *Asda's*, *Delhaize's*, *Wal-Mart's*, etc.)**

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Main types of retailers**
  - **Discount stores: retail organizations that sell standard merchandise at lower prices by accepting lower margins and selling at higher volumes (ex.: *Aldi*, *Lidl*, *Nettorama*, etc.).**
  - **Off-price retailers / Factory outlets: retailers that buy at less-than-regular wholesale prices and sell at less than retail; perhaps sometimes owned and operated by a manufacturer, carrying the manufacturer's surplus, discontinued or irregular goods.**

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Channel breadth factors**
  - **Intensive distribution: stocking the product in as many outlets / resellers / shops as possible:**
    - **availability as high as possible**
    - **consumers: minimal purchasing effort**
    - **choice of shop above choice of product**
    - **mainly: convenience goods**
    - **for example: grocery goods, such as coffee, tea, milk, sugar, etc.**

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MANAGING MARKETING CHANNELS

Channel design decisions

- Channel breadth factors
  - Selective distribution: using, usually the more qualified, outlets / resellers / shops:
    - more important, qualified distributors
    - consumers: reasonable purchasing effort
    - distributors: more marketing & selling effort
    - mainly: shopping goods
    - examples: A-brand watches such as *Seiko*; ladies shoes & boots; home furniture; etc.

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MANAGING MARKETING CHANNELS

Channel design decisions

- Channel breadth factors
  - Exclusive distribution: giving a limited number of dealers (outlets / resellers / shops) the exclusive right to distribute the company's products in their designated territories:
    - geographical, exclusive selling rights
    - consumers: huge purchasing effort
    - distributors: high marketing & selling effort
    - mainly: specialty goods
    - examples: top exclusive watch brands such as *Rolex* or *Omega*; etc.

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MANAGING MARKETING CHANNELS

Channel design decisions

- Marketing channel (or distribution) ratio's:
  - Distribution intensity (DI), shows the distribution intensity of a product or a branded product:
    the ratio between the number of distributors (or dealers) of the product or brand, and the number of distributors of the product class involved.

$$DI = \frac{\text{number of distributors of brand}}{\text{number of distributors of product class}}$$

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Marketing channel (or distribution) ratio's:**
  - **Market reach (MR), shows the ratio between the total product class turnover (money), achieved by all the appointed distributors, and the total product class turnover, achieved by all the distributors.**

$$MR = \frac{\text{turnover (money) of product class, through all appointed distributors}}{\text{turnover (money) of product class, through all distributors}}$$

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Marketing channel (or distribution) ratio's:**
  - **Market share (MS), shows a firm's relative position in the market: a firm's total amount of product or brand sales (numbers), *or* the total turnover (money) involved, compared to the total market's product class sales *or* turnover.**

$$MS = \frac{\text{turnover resp. sales of branded product through all appointed distributors}}{\text{turnover resp. sales of product class through all distributors}} = TS \times MR$$

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Marketing channel (or distribution) ratio's:**
  - **Turnover share (TS), shows the amount of a product's or a branded product's turnover, achieved by all the appointed distributors, in comparison to the total product class turnover, achieved by these distributors.**
  - **Sales share (SS): same as above, but regarding *sales* instead of turnover.**

$$TS \text{ (resp. } SS) = \frac{\text{turnover resp. sales of branded product through all appointed distributors}}{\text{turnover resp. sales of product class through all appointed distributors}}$$

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Marketing channel (or distribution) ratio's:**
  - **Selection indicator (SI), shows to what extent a product or a branded product is being distributed through distributors who sell their products on a smaller or larger scale than average.**

$$SI = \frac{\text{average product class turnover through all appointed distributors}}{\text{average product class turnover through all distributors}} = \frac{MR}{DI}$$

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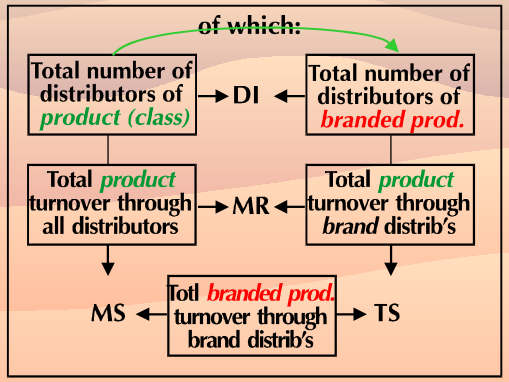
MANAGING MARKETING CHANNELS

Channel design decisions

- **Marketing channel (or distribution) ratio's:**



$$SI = \frac{MR}{DI}$$

$$MS = TS \times MR$$

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Example #1:**

Fony is a Japanese manufacturer of Fony headphones. In Holland, these headphones are sold by 4.000 of the 16.000 electronics shops. The total turnover of all these 16.000 shops, concerning the headphones product group, is $ 200 million. The total turnover regarding Fony head-phones (in Holland) is $ 5 million.
Electronics shops that sell Fony headphones appear to generate an average turnover of $ 9.375 (per shop), regarding their headphones product group.
Based on these figures, calculate:
1/ the market reach of shops that sell Fony headphones;
2/ the turnover share of Fony headphones in Holland;
3/ the selection indicator regarding Fony headphones. And: what conclusion(s) should Fony draw, regarding this SI?

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Solution:** MR = 18,75%; TS = 13,33%; SI = 0,75

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Example #2:**
  The beverage brand Banano is bought by 20% of all the households in a certain area. This brand is available at 70% of all the relevant retail shops, in which the brand represents an average of 30% of the total product group. The retail shops that sell Banano, have an average beverage turnover that is 10% higher than the average beverage turnover of all the retail shops that sell this product group.
  Calculate Banano's market share.

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MANAGING MARKETING CHANNELS

Channel design decisions

- **Solution:** MS = 23,1%

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MANAGING MARKETING CHANNELS

Retailing aspects

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MANAGING MARKETING CHANNELS

Retailing aspects

- **Retail, marketing-P's (retail mix):**
  - **Retail mix:**
    - **product policy**
    - **(place) distribution policy**
    - **pricing policy**
    - **promotions policy, and:**
    - **presentation policy**
    - **personnel policy.**

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MANAGING MARKETING CHANNELS

Retailing aspects

- **Retail, particular aspects**
  - **Store concept / store format:**

    Store concept: the strategic basis of a retail organization, regarding location, shop interior, range of products, pricing levels, product presentation and targeted customers groups, focussing on 3 major issues:

    - ☐ **what customer groups are we looking for?**
    - ☐ **what do we want to offer them?**
    - ☐ **how do we want to reach these customers?**

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MANAGING MARKETING CHANNELS

Retailing aspects

- Retail, particular aspects:
  - Store concept / store format:
    Store format: the actual total offering through which the retail organization tries to attract and bind a certain group of customers.
    This can be identified by evaluating 3 major components:
    - customers (customer groups): who are our customers?
    - type of product range: what we sell to our customers
    - market position: our position in comparison to our competitors.

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MANAGING MARKETING CHANNELS

Retailing aspects

- Retail, particular aspects:
  - Service-retailing / Low margin retailing:
    Service-retailing: strategy of a retail organization, aimed at a narrow target group that prefers (high) quality and service: plus-shoppers.
    - Exclusiveness, narrow range of products, high margins, luxurious ambience, lots of service and advice.

    Low-margin retailing: strategy of a retail organization, aimed at a broad target group that prefers low prices: price-shoppers.
    - Narrow assortment, low margins, low degree of service and advice, 'commom' locations.

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MANAGING MARKETING CHANNELS

Retailing aspects

- Wheel of retailing
  - Wheel of retailing, involves a concept of retailing which shows that new types of retailers usually begin as low-margin, low-price, low-status operations, but later evolve into higher-priced, higher-service operations, eventually becoming like the conventional retailers they once replaced.

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Retailing aspects

- **Wheel of retailing**