

Chapter 8

Business, Marketing



Chapter 8 TARGET MARKETS AND CHANNEL DESIGN STRATEGY Chapter Outline A Framework for Market Analysis Markets, whether consumer or industrial, are complex. Frameworks consisting of four basic dimensions for discussing markets are: 1. Market geography 2. Market size 3. Market density 4. Market behavior Figure 8. 1 illustrates this market framework. The emphasis will be on showing how these market dimensions influence channel design strategy. Market Geography and Channel Design Strategy Key Term and Definition ^a Market geography: Refers to the geographical extent of markets and where they are located. The channel manager is charged with the task of evaluating market geography relative to channel structure to make sure that the structure is able to serve the markets effectively and efficiently. Changing market locations resulting from expanding geographical boundaries or the opening up of new, more distant markets should signal the channel manager that modifications in channel structure may be needed. 1) Locating Markets The channel manager may be called upon to delineate the geographical locations of target markets. Table 8. 1 provides definitions of these geographical entities and Table 8. 2 lists some useful sources for obtaining additional geographical market data. As an in-class exercise, you may want to have the students explore the amount of information obtainable from these sources for a particular area code or ZIP code (such as the school's or student's residence) to see how pertinent the information is that is obtained. What is required of the channel manager is an awareness of and sensitivity to changes in market geography reflected in the data and a willingness to examine their possible implications for channel design decisions. Market Size and Channel Design Strategy Key Term and Definition

Market size: Refers to the number of buyers or potential buyers (consumer or industrial) in a given market. Bucklin developed a model relating market size to channel structure, which provides some insight for using market size data. Figure 8. 2 shows the effect of the number of buyers on the relative cost of direct channel versus middleman channels. The key teaching lesson here is that when the market size reaches point U_e , the cost of the intermediary structure is equal to the direct structure. Market Density and Channel Design Strategy Key Terms and Definitions

Market density: Refers to the number of buyers or potential buyers per unit of geographical area. A useful concept that helps to illustrate the relationship is that of efficient congestion.

Efficient congestion: According to this concept, congested (high-density) markets can promote efficiency in the performance of several basic distribution tasks, particularly those of transportation, storage, communication, and negotiation. The major strategic implication of this discussion is that the opportunity to achieve a relatively high level of customer access at low cost is higher in dense markets than in more dispersed ones. Even though dense markets are most often located in major metropolitan areas and are the most competitive, the large number of customers in close proximity to huge assortments of products provides the greatest opportunity and highest level of efficiency. Figure 8. 3 shows a typical Japanese channel of distribution for a consumer product and points out that due to Japanese sociocultural patterns, Japanese channels are longer than would be indicated otherwise. Market Behavior and Channel Design Strategy

The fourth dimension, market behavior, consists of four subdimensions: (1) when the market buys, (2) where the market buys, (3)

how the market buys, and (4) who buys. 1) When the Market Buys Neither consumer nor industrial markets buy products on a precisely predictable time schedule that remains constant per time period. Weekly and daily variations in buyer behavior are common at the retail level and vary across different trade areas throughout the country. Two important implications for the channel manager are related to this subdimension: a. First, seasonal variations tend to create peaks and valleys in the manufacturer's production scheduling. Manufacturers who experience wide seasonal variations in the purchase of their products should attempt to select channel members who are amenable to buying in the off-season to help offset carrying costs. b. The channel manager should attempt to select channel members who are in tune with the changing patterns of when people buy. In other words, the channel manager should try to avoid selecting channel members who are out of touch with the time demands of the markets they serve. 2) Where the Market Buys The types of outlets from which final buyers choose to make their purchases and the location of those outlets determine where the market buys. Research on where consumers buy is often based on the assumption that they will behave so as to maximize their convenience in the selection of retail outlets. An increasing amount of research seeks to explain consumer store choice behavior based on factors other than a desire for locational convenience. The self-image of the consumer, his or her social status, attitudes, values, and beliefs, and the overall image of the retail store have been postulated as factors affecting consumer store choice. The major strategic implication for the channel manager is to develop an effective channel design strategy by knowing where customers generally buy

particular types of products, and, more importantly, whether these patterns may be changing. 3) How the Market Buys Customer preferences reflected in purchase behavior indicate how the market buys. Table 8. 3 shows contrasting behaviors related to how customers buy at the consumer level. Each of the eight behaviors in the table can vary across different market segments and over time for any given product category. At this point in the lecture, you may want to give an example of a product and ask the students to list their own behaviors when purchasing this product, where they purchase the product, when they purchase the product and whether or not store image affects their decision process. One of the most profound changes in how the market buys may occur in the realm of Internet shopping. A key determinant in the potential growth of electronic shopping is whether consumers and industrial buyers find this mode of shopping and purchasing to be superior to traditional modes. The changing nature of how customers buy means that the channel manager must be closely tuned in to what changes are likely to occur and determining whether such changes are temporary or long term. 4) Who Buys The subdimension of who does the buying has two aspects: (a) who makes the physical purchase, and (b) who takes part in the buying decisions. A) Who Makes the Purchases From a channel design standpoint, who actually buys the product can affect the type of retailers to choose in the consumer market, and may also influence the kinds of channel members to use to serve the industrial market. Product purchases should not be confused with product usage. Care should therefore be taken to distinguish between who uses the product and who makes the actual purchase. Here the text compares and contrasts the purchasing of

men's products by women. A discussion among class members at this point may elicit some interesting opinions and comments and can drive the point home between product usage and product purchase.

B) Who Takes Part in the Buying Decision

The more difficult aspect to analyze than who actually makes the physical purchase is who decides to make the purchase in the first place. At the consumer level, the question is usually answered by the family unit. Influence on buying decisions revolves around the roles played by the husband, wife, and children. In the industrial market, a concept called "buying centers" exists, and it is not unusual to have several people involved in the purchase decision. These "buying centers" have six distinct roles that various individuals in the organization fill:

1. Users—those who will use the product and service.
2. Influencers—those who influence the buying decision often by design specifications. Technical people are especially important as influencers.
3. Deciders—people who have the power to make a decision on the product.
4. Approvers—people who must authorize the proposed actions of the deciders or buyers.
5. Buyers—people with formal authority for selecting.
6. Gatekeepers—people who have the power to prevent sellers or information from reaching members of the buying center.

Two heuristics exist to provide the channel manager some insight for analyzing the relationship of channel structure to the ability to reach the influential parties of buying decisions:

- a. As the channel becomes longer, the degree of control exercised by the manufacturer is lessened.
- b. As the intensity of distribution at each level of the channel becomes greater, the manufacturer's capacity to supervise the selling efforts of channel members becomes lower.

Other than heeding these two general heuristics, the

channel manager can help to assure the appropriateness of a channel structure for reaching the influential buying parties through explicit consideration of this issue when selecting channel members. Answers to Review Questions 1. The market variables are the most basic and important variables in channel design because, quite simply, the needs and wants of the target market should drive channel design. The target market is the final adjudicator of the channel design. 2. In general, yes, market variables should be considered before the other variables because market variables are so basic to channel design. This emphasis is sometimes referred to as the “bottom to top” approach, meaning that in attempting to develop channel structures to serve markets, the channel manager should look first at the last level of the channel (the market) and then work backwards in developing the channel structure based on the needs of the target markets. 3. The market variables are a four-dimensional construct for analyzing markets. The four basic dimensions are: ^a Market Geography: defines the market in terms of its geographic boundaries, its location and its distance. ^a Market Size: defines the market in terms of the number of buyers or potential buyers. ^a Market Density: defines the market in terms of the number of buyers or potential buyers per unit of geography. ^a Market Behavior: consists of four sub-dimensions: a. When the market buys: seasonal, weekly and daily variations in the time of purchase. b. Where the market buys: the types of outlets from which the buyers choose to make their purchases and the location of those outlets. c. How the market buys: the buyer’s purchase behavior including quantity purchased per transaction, purchase assistance, stops per shopping trip, purchase decision process, credit utilization, in-home

versus out-of-home purchasing, effort expended and service demanded. d. Who buys: includes both the actual buyer and those partaking in the purchase decision. 6. Highly dense markets are said to be in efficient congestion because the large number of buyers per unit of geography facilitates the performance of such distribution tasks as transportation, storage, communication and negotiations. The large number of buyers may allow the manufacturer to emphasize economies of scale rather than economies of scope in channel design and thus structure a shorter channel. However, while such market density usually supports shorter channels, there can be additional variables at work that would offset this heuristic. This is especially true in some foreign markets. 7. Market Behavior consists of four sub-dimensions: ^a When the Market Buys: seasonal, weekly and daily variations in the time of purchase. In some cases, particularly prepared food retailing, variations are tracked hourly. ^a Where the Market Buys: the types of outlets from which the buyers choose to make their purchases and the location of those outlets. ^a How the Market Buys: the buyer's purchase behavior including quantity purchased per transaction, purchase assistance, stops per shopping trip, purchase decision process, credit utilization, in-home versus out-of-home purchasing, effort expended and service demanded. ^a Who Buys: includes both the actual buyer and those partaking in the purchase decision. For consumer purchases, family unit members may be the buyer, user, influencer and/or decider. One person may assume any number of those roles or each may be played by a different member of the household. In the industrial market, two additional roles are found in the buying center: approvers are people who authorize the actions of the

deciders and buyers, and gatekeepers are people who can block sellers and their information from reaching members of the buying center.