Chapter 12 zara

Business, Company

CHAPTER Marketing Channels Delivering 12 Customer Value PRE VIEWING We now arrive at the third marketing mix tool—distribution. Firms rarely work alone in creating value for customers and building profitable customer relationships. Instead, most THE CONCEPTS are only a single link in a larger supply chain and marketing channel. As such, an individual firm's success depends not only on how well it performs but also on how well its entire marketing channel competes with competitors' channels. To be good at customer relationship management, a company must also be good at partner relationship management.

The first part of this chapter explores the nature of marketing channels and the marketer's channel design and management decisions. We then examine physical distribution—or logistics—an area that is growing dramatically in importance and sophistication. In the next chapter, we'll look more closely at two major channel intermediaries—retailers and wholesalers. We'll start with a look at a company whose groundbreaking, customer-centred distribution strategy took it to the top of its industry. Q uick, which rental-car company is number one? Chances are good that you said Hertz. Okay, who's number two?

That must be Avis, you say. After all, for years Avis advertising has said, " We're #2, so we try harder! " But if you said Hertz or Avis, you're about to be surprised. By any measure—most locations, revenues, profits, or number of cars—the number-one North American rental-car company is Enterprise Rent-A-Car. What's more, this is no recent development. Enterprise left number-two Hertz in its rear-view mirror in the late 1990s and has never looked back. What may have fooled you is that for a long time, Hertz was number one in airport car rentals. However, with estimated revenues of US$9. billion and growing, Enterprise now has 30 percent more overall car rental sales than Hertz. What's more, analysts estimate that the privately owned Enterprise is twice as profitable as Hertz. How did Enterprise become such a dominating industry leader? The company might argue that it was through better prices or better marketing. But what contributed most to Enterprise taking the lead was an industry-changing, customer-driven distribution strategy. While competitors such as Hertz and Avis focused on serving travellers at airports, Enterprise developed a new distribution doorway to a large and untapped segment.

It opened off-airport, neighbourhood locations that provided short-term carreplacement rentals for people whose cars were wrecked, stolen, or being serviced, or for people who simply wanted a different car for a short trip or special occasion. It all started more than half a century ago when Enterprise founder Jack Taylor discovered an unmet customer need. He was working at a St. Louis auto dealership, and customers often asked him where they could get a replacement The tagline " Pick Enterprise. We'll Pick You car when theirs was in the shop for repairs or body work.

To meet this need, Up" remains the company's main value Taylor opened a car-leasing business. But rather than competing head-on with proposition. the likes of Hertz and Avis serving travellers at airports, Taylor located his rental offices in centre-city and neighbourhood areas, closer to his replacement-car target customers. These locations also gave Taylor a cost advantage—property rents were lower and he didn't have to pay airport taxes and fees. Taylor’s groundbreaking distribution strategy worked and the business grew quickly. As he opened multiple locations in St.

Louis and other cities, he renamed his business Enterprise Rent-A-Car after the U. S. Navy aircraft carrier on which he had served as a naval aviator. Enterprise continued to focus steadfastly on what it called the “ home-city” market, primarily serving customers who’d been in wrecks or whose cars were being serviced. Enterprise branch managers developed strong relationships with local auto insurance adjusters, dealership sales and service personnel, and body shops and service garages, making Enterprise their preferred neighbourhood rental-car provider.

Customers in the home-city market had special needs. Often, they were at the scene of a wreck or at a repair shop and had no way to get to an Enterprise office to pick up a rental car. So the company came up with another gamechanging idea—picking customers up wherever they happen to be and bringing them back to the rental office. Hence the tagline: “ Pick Enterprise. We’ll Pick You Up,” which remains the company’s main value proposition to this day. By the late 1980s, Enterprise had a large nationwide network of company-owned off-airport locations and a virtual lock on the home-city market.

From this strong base, in the mid-1990s Enterprise began expanding its distribution system by directly challenging Hertz and Avis in the onairport market. A decade later, it had operations in 230 airports in North America and Europe. Enterprise opened its first Canadian branch in 1993 in Windsor, Ontario, and since then has experienced double-digit growth in Canada. It now employs 2800 Canadians, and has over 35 000 vehicles and 400 locations, including 23 offices serving Canadian airports. In late 2007, Enterprise purchased the Vanguard Car Rental Group, which owned the National and Alamo brands.

National focused on the corporate negotiated rental market while Alamo served primarily the leisure traveller airport market. With the Vanguard acquisition, Enterprise now captures a 27. 4 percent share of the airport market, putting it While competitors Hertz and Avis focused on serving travellers at airports, Enterprise opened off-airport, neighbourhood locations that provided short-term car-replacement rentals for people whose cars were wrecked, stolen, or being serviced. neck-and-neck with Hertz at 28. 5 percent and jointly owned Avis/Budget at 30. percent. That, combined with its more than 55 percent share of the off-airport market, makes Enterprise the runaway leader in overall car rental sales. Enterprise owns a stunning one-half of all North American rental cars and is the world’s largest automobile buyer. Last year, it purchased 800 000 cars to support its 7900 locations in the United States and four other countries. However, rather than resting on its laurels, Enterprise continues to seek better ways to get its cars where customers want them.

The enterprising company is now motoring into yet another innovative distribution venue—“ car sharing” and hourly rentals. Car sharing was pioneered in the late 1990s by Zipcar, which operates on parking-starved university campuses and in congested urban areas, where it rents cars on an hourly or daily basis to people who want to run errands or make short trips. Zipcar does not currently serve the Canadian university market but does have branches serving the general public in Vancouver and Toronto. Enterprise has now revved up its own car-sharing program, WeCar.

This new operation will park automobiles at convenient locations in densely populated urban areas, where residents often don't own cars and where business OBJECTIVES 1 2 3 4 5 Explain why companies use marketing channels and discuss the functions these channels perform. Discuss how channel members interact and how they organize to perform the work of the channel. Identify the major channel alternatives open to a company. Explain how companies select, motivate, and evaluate channel members. Discuss the nature and importance of marketing logistics and integrated supply chain management. 90 Part 3 Designing a Customer-Driven Strategy and Mix commuters would like to have occasional car access. Enterprise will also target businesses that want to have WeCar vehicles available in their parking lots for commuting employees to use. WeCar members pay a US$35 annual membership fee. They can then rent conveniently located, fuel-efficient cars (mostly Toyota Prius hybrids) for US$10 per hour or US$30 overnight—the rate includes gas and a 200-mile allotment. Renting a WeCar vehicle is a simple get-in-and-go operation.

Just pass your member key fob over a sensor to unlock the car, then open the glove box and enter a PIN to release the car key. Although the carsharing market now belongs to tiny Zipcar, a US$100 million company that has cars on more than 70 university campuses in several large metropolitan areas, look for giant Enterprise to perfect and expand the new distribution concept. Thus, Enterprise continues to move ahead aggressively with its winning distribution strategy. Says Andy Taylor, founder Jack's son and now longtime

Enterprise CEO, “ We own the high ground in this business and we aren’t going to give it up.

As the dynamics of our industry continue to evolve, it’s clear to us that the future belongs to the service providers who offer the broadest array of services for anyone who needs or wants to rent a car. ” The company intends to make cars available wherever, whenever, and however customers want them. 1 As the Enterprise story shows, good distribution strategies can contribute strongly to customer value and create competitive advantage for both a firm and its channel partners. It demonstrates that firms cannot bring value to customers by themselves.

Instead, they must work closely with other firms in a larger value delivery network. 1 Value delivery network The network made up of the company, suppliers, distributors, and ultimately customers who “ partner” with each other to improve the performance of the entire system in delivering customer value. Supply Chains and the Value Delivery Network Producing a product or service and making it available to buyers requires building relationships not just with customers, but also with key suppliers and resellers in the company’s supply chain. This supply chain consists of “ upstream” and “ downstream” partners.

Upstream from the company is the set of firms that supply the raw materials, components, parts, information, finances, and expertise needed to create a product or service. Marketers, however, have traditionally focused on the “ downstream” side of the supply chain—on the marketing channels (or distribution channels) that look toward the customer. Downstream marketing channel partners, such as wholesalers and retailers, form a vital connection between the firm and its customers. The term supply chain may be too limited—it takes a make-and-sell view of the business.

It suggests that raw materials, productive inputs, and factory capacity should serve as the starting point for market planning. A better term would be demand chain because it suggests a sense-and-respond view of the market. Under this view, planning starts with the needs of target customers, to which the company responds by organizing a chain of resources and activities with the goal of creating customer value. Even a demand chain view of a business may be too limited, because it takes a step-by-step, linear view of purchase–production–consumption activities.

With the advent of the Internet and other technologies, however, companies are forming more numerous and complex relationships with other firms. For example, Ford manages numerous supply chains. It also sponsors or transacts on many B2B websites and online purchasing exchanges as needs arise. Like Ford, most large companies today are engaged in building and managing a continuously evolving value delivery network. As defined in Chapter 2, a value delivery network is made up of the company, suppliers, distributors, and ultimately customers who “ partner” with each other to improve the performance of the entire system.

For example, in making and marketing its iPod touch products, Apple manages an entire network of peoValue delivery network: In making and market- ple within Apple plus suppliers and resellers outside the company who work ing iPod touch products, Apple manages an together effectively to give final customers “ so much to touch. ” This chapter focuses on marketing channels—on the downstream side of the entire network of people within

Apple plus suppliers and resellers outside the company who value delivery network.

We examine four major questions concerning marketing work effectively together to give final cus- channels: What is the nature of marketing channels and why are they important? tomers “ so much to touch. ” How do channel firms interact and organize to do the work of the channel? What Chapter 12 Marketing Channels Delivering Customer Value 391 problems do companies face in designing and managing their channels? What role do physical distribution and supply chain management play in attracting and satisfying customers? In Chapter 13, we will look at marketing channel issues from the viewpoint of retailers and wholesalers.

The Nature and Importance of Marketing Channels Marketing channel (distribution channel) A set of interdependent organizations that help make a product or service available for use or consumption by the consumer or business user. Few producers sell their goods directly to the final users. Instead, most use intermediaries to bring their products to market. They try to forge a marketing channel (or distribution channel)—a set of interdependent organizations that help make a product or service available for use or consumption by the consumer or business user.

A company’s channel decisions directly affect every other marketing decision. Pricing depends on whether the company works with national discount chains, uses high-quality specialty stores, or sells directly to consumers via the Web. The firm’s sales force and communications decisions depend on how much persuasion, training, motivation, and support its channel partners need. Whether a company develops or acquires certain new products may depend on how well those products fit the capabilities of its channel members.

For example, Kodak initially sold its EasyShare printers only in Best Buy stores to take advantage of the retailer's on-the-floor sales staff and their ability to educate buyers on the economics of paying higher initial prices but lower long-term ink costs. Companies often pay too little attention to their distribution channels, sometimes with damaging results. In contrast, many companies have used imaginative distribution systems to gain a competitive advantage. FedEx's creative and imposing distribution system made it a leader in express delivery. Enterprise revolutionized the car-rental business by setting up off-airport rental offices.

And Amazon. com pioneered the sales of books and a wide range of other goods via the Internet. Distribution channel decisions often involve long-term commitments to other firms. For example, companies such as Ford, HP, or McDonald's can easily change their advertising, pricing, or promotion programs. They can scrap old products and introduce new ones as market tastes demand. But when they set up distribution channels through contracts with franchisees, independent dealers, or large retailers, they cannot readily replace these channels with company-owned stores or websites if conditions change.

Therefore, management must design its channels carefully, with an eye on tomorrow's likely sellingenvironmentas well as today's. How Channel Members Add Value Why do producers give some of the selling job to channel partners? After all, doing so means giving up some control over how and to whom they sell their products. Producers use intermediaries because they create greater efficiency in making goods available to target markets. Through their contacts, experience, specialization, and scale of operation, intermediaries usually offer the firm more than it can achieve on its own. Figure 12. shows how using intermediaries can provide economies. Figure 12. 1A shows three manufacturers, each using direct marketing to reach three customers. This system requires nine different contacts. Figure 12. 1B shows the three manufacturers working through one distributor, which contacts the three customers. This system requires only six contacts. In this way, intermediaries reduce the amount of work that must be done by both producers and consumers. From the economic system's point of view, the role of marketing intermediaries is to transform the assortment of products made by producers into the assortment wanted by consumers.

Producers make narrow assortments of products in large quantities, but consumers want broad assortments of products in small quantities. Marketing channel members buy large quantities from many producers and break them down into the smaller quantities and broader assortments wanted by consumers. 392 Part 3 Designing a Customer-Driven Strategy and Mix 1 Manufacturer 3 4 Manufacturer 6 7 Manufacturer 8 9 Customer Manufacturer 6 3 Customer 5 2 Customer Manufacturer Distributor 5 Customer 2 Customer Manufacturer 1 4 Customer A. Number of contacts without a distributor M? C= 3? 3= 9 B.

Number of contacts with a distributor M+C= 3+3= 6 Figure 12. 1 How adding a distributor reduces the number of channel transactions For example, Unilever makes millions of bars of Lever 2000 hand soap each day, but you want to buy only a few bars at a time. So bigfood, drug, and discount retailers, such as Superstore, Shoppers Drug Mart, and Walmart, buy Lever 2000 by the truckload and stock it on their store shelves. In turn, you can buy a single bar of Lever 2000, along with a shopping cart full of small quantities of toothpaste, shampoo, and other related products as you need them.

Thus, intermediaries play an important role in matching supply and demand. In making products and services available to consumers, channel members add value by bridging the major time, place, and possession gaps that separate goods and services from those who would use them. Members of the marketing channel perform many key functions. Some help to complete transactions: • Information: Gathering and distributing marketing research and intelligence information about actors and forces in the marketing environment needed for planning and aiding exchange. Promotion: Developing and spreading persuasive communications about an offer. • Contact: Finding and communicating with prospective buyers. • Matching: Shaping and fitting the offer to the buyer’s needs, including activities such as manufacturing, grading, assembling, and packaging. • Negotiation: Reaching an agreement on price and other terms of the offer so that ownership or possession can be transferred. Others help to fulfill the completed transactions: • Physical distribution: Transporting and storing goods. • Financing: Acquiring and using funds to cover the costs of the channel work. Risk taking: Assuming the risks of carrying out the channel work. And a new item that has been added to the list of functions to be performed within the supply chain is environmental sustainability. Take the case of Toronto-based Grand & Toy: In 2007, Grand & Toy, Canada’s leading provider of business solutions, announced a new corporate strategy aimed at becoming a leader in environmental sustainability. Among its initiatives was a plan to significantly reduce its environmental footprint in supply chain carbon intensity, packaging, recycling of waste, and distribution centre management.

In just a few short years, Grand & Toy has established itself as a leader in sustainable procurement practices, In 2009, for example, the company sponsored two free sustainable procurement showcases to help supply chain management professionals understand how sustainability is becoming a key driver for innovative procurement solutions, and how to adopt sustainable supply chain practices when working with suppliers and partners that maximize both profitability and corporate socialresponsibility. 2 Chapter 12 Marketing Channels Delivering Customer Value 393 FPO

The question is not whether these functions need to be performed—they must be—but rather who will perform them. To the extent that the manufacturer performs these functions, its costs go up and its prices must be higher. When some of these functions are shifted to intermediaries, the producer’s costs and prices may be lower, but the intermediaries must charge more to cover the costs of their work. In dividing the work of the channel, the various functions should be assigned to the channel members who can add the most value for the cost. Number of Channel Levels

Companies can design their distribution channels to make products and services available to customers in different ways. Each layer of marketing intermediaries that perform some work in bringing the product and its ownership closer to the final buyer is a channel level. Because the producer and the final consumer both perform some work, they are part of every channel. The number of intermediary levels indicates the length of a channel. Figure 12. 2A shows several consumer distribution chanGrand & Toy’s sustainability vision involves “ powering the potential of Canadian businesses to lead the journey towards sustainability. nels of different lengths. Channel 1, called a direct marketing channel, has no intermediary levels; the company sells directly to consumers. For example, Mary Kay and Amway sell their products door-to-door, Channel level through home and office sales parties, and on the Web; Veseys, located in York, Prince EdA layer of intermediaries that ward Island, sells its plants and bulbs to gardeners across the country through mail cataperform some work in bringing the logues, by telephone, and online. The remaining channels in Figure 12. 2A re indirect product and its ownership closer marketing channels, containing one or more intermediaries. to the final buyer. Figure 12. 2B shows some common business distribution channels. The business marDirect marketing channel keter can use its own sales force to sell directly to business customers. Or it can sell to various A marketing channel that has no types of intermediaries, who in turn sell to these customers. Consumer and business marketintermediary levels. ing channels with even more levels can sometimes be found, but less often.

From the proIndirect marketing channel ducer’s point of view, a greater number of levels means less control and greater channel A marketing channel containing complexity. Moreover, all of the institutions in the channel are connected by several types of one or more intermediary levels. flows. These include the physical flow of products, the flow of ownership, the payment flow, the information flow, and the promotion flow. These flows can make even channels with only one or a few levels very complex. Producer Producer Producer Producer Producer Producer Wholesaler Manufacturer? s representatives or sales branch Retailer

Retailer Business distributor Business distributor Consumer Channel 1 Consumer Channel 2 Consumer Channel 3 Business customer Channel 1 Business customer Channel 2 Business customer Channel 3 A. Consumer marketing channels B. Business marketing channels Figure 12. 2 Consumer and business marketing channels 394 Part 3 Designing a Customer-Driven Strategy and Mix 2 Channel Behaviour and Organization Distribution channels are more than simple collections of firms tied together by various flows. They are complex behavioural systems in which people and companies interact to accomplish individual, company, and channelgoals.

Some channel systems consist only of informal interactions among loosely organized firms. Others consist of formal interactions guided by strong organizational structures. Moreover, channel systems do not stand still—new types of intermediaries emerge and whole new channel systems evolve. Here we look at channel behaviour and at how members organize to do the work of the channel. Channel Behaviour A marketing channel consists of firms that have partnered for their common good. Each channel member depends on the others. For example, a Ford dealer depends on Ford to design cars that meet consumer needs.

In turn, Ford depends on the dealer to attract consumers, persuade them to buy Ford cars, and service cars after the sale. Each Ford dealer also depends on other dealers to provide good sales and service that will uphold the brand’s reputation. In fact, the success of individual Ford dealers depends on how well the entire Ford marketing channel competes with the channels of other auto manufacturers. Each channel member plays a specialized role in the channel. For example, consumer electronics maker Samsung’s role is to produce electronics products that consumers will like and to create demand through national advertising.

Future Shop’s role is to display these Samsung products in convenient locations, to answer buyers’ questions, and to complete sales. The channel will be most effective when each member assumes the tasks it can do best. Ideally, because the success of individual channel members depends on overall channel success, all channel firms should work together smoothly. They should understand and accept their roles, coordinate their activities, and cooperate to attain overall channel goals. However, individual channel members rarely take such a broad view.

Cooperating to achieve overall channel goals sometimes means giving up individual company goals. Although channel members depend on one another, they often act alone in their own short-run best interests. They often disagree about who should do what and for what rewards. Such disagreements over goals, roles, and rewards generate channel conflict. Horizontal conflict occurs among firms at the same level of the channel. For instance, some Ford dealers in Vancouver might complain that the other dealers in the city steal sales from them by pricing too low or by advertising outside their assigned territories.

Or Holiday Inn franchisees might complain about other Holiday Inn operators overcharging guests or giving poor service, hurting the overall Holiday Inn image. Vertical conflict, conflicts between different levels of the same channel, is even more common. For example, Goodyear created hard feelings and conflict with its premier independent-dealer channel when it began selling through mass-merchant retailers: For more than 60 years Goodyear sold replacement tires exclusively through its premier network of independent Goodyear dealers.

Then, in the 1990s, Goodyear shattered tradition and jolted its dealers by agreeing to sell its tires through mass merchants such as Sears and Walmart, placing dealers in direct competition with the nation’s Channel conflict Disagreements among marketing channel members on goals and roles—who should do what and for what rewards. Channel conflict: Goodyear created conflict with its premier independent-dealer channel when it began selling through mass-merchant retailers. Fractured dealer relations weakened the Goodyear name and dropped the company into a more than decade-long profit funk.

Chapter 12 Marketing Channels Delivering Customer Value 395 most potent retailers. Goodyear claimed that value-minded tire buyers were increasingly buying from cheaper, multibrand discount outlets and department stores, and that it simply had to put its tires where many consumers were going to buy them. Not surprisingly, Goodyear’s aggressive moves into new channels set off a surge of channel conflict, and dealer relations deteriorated rapidly. Some of Goodyear’s best dealers defected to competitors. Other angry dealers struck back by taking on competing brands of cheaper private-label tires.

Such dealer actions weakened the Goodyear name, and the company’s replacement tire sales—which make up 71 percent of its revenues—went flat, dropping the company into a more than decade-long profit funk. Although Goodyear has since actively set about repairing fractured dealer relations, it still has not fully recovered. “ We lost sight of the fact that it’s in our interest that our dealers succeed,” admits a Goodyear executive. 3 Some conflict in the channel takes the form of healthy competition. Such competition can be good for the channel—without it, the channel could become passive and noninnovative.

But severe or prolonged conflict, as in the case of Goodyear, can disrupt channel effectiveness and cause lasting harm to channel relationships. Companies should manage channel conflict to keep it from getting out of hand. Vertical Marketing Systems Conventional distribution channel A channel consisting of one or more independent producers, wholesalers, and retailers, each a separate business seeking to maximize its own profits, even at the expense of profits for the system as a whole. Vertical marketing system (VMS) A distribution channel structure in which producers, wholesalers, and retailers act as a unified system.

One channel member owns the others, has contracts with them, or has so much power that they must all cooperate. For the channel as a whole to perform well, each channel member’s role must be specified and channel conflict must be managed. The channel will perform better if it includes a firm, agency, or mechanism that providesleadershipand has the power to assign roles and manage conflict. Historically, conventional distribution channels have lacked such leadership and power, often resulting in damaging conflict and poor performance.

One of the biggest channel developments over the years has been the emergence of vertical marketing systems that provide channel leadership. Figure 12. 3 contrasts the two types of channel arrangements. A conventional distribution channel consists of one or more independent producers, wholesalers, and retailers. Each is a separate business seeking to maximize its own profits, perhaps even at the expense of the system as a whole. No channel member has much control over the other members, and no formal means exists for assigning roles and resolving channel conflict.

In contrast, a vertical marketing system (VMS) consists of producers, wholesalers, and retailers acting as a unified system. One channel member owns the others, has contracts with them, or wields so much power that they must all cooperate. The VMS can be dominated by the producer, wholesaler, or retailer. The Forzani Group, headquartered in Calgary, is an example of a retail-dominated VMS. It owns and operates a range of sporting Consumer Figure 12. 3 Comparison of a conventional distribution channel with vertical marketing system Conventional marketing channel

Vertical marketing channel 396 Part 3 Designing a Customer-Driven Strategy and Mix goods stores including Sport Chek, Coast Mountain Sports, Sport Mart, Athletes World, Hockey Experts, and National Sports. We look now at three major types of VMSs: corporate, contractual, and administered. Each uses a different means for setting up leadership and power in the channel. Corporate VMS Corporate VMS A vertical marketing system that combines successive stages of production and distribution under single ownership—channel leadership is established through common ownership.

A corporate VMS integrates successive stages of production and distribution under single ownership. Coordination and conflict management are attained through regular organizational channels. For example, U. S. grocery giant Kroger owns and operates 42 factories that crank out more than 8000 private-label items found on its store shelves. Similarly, to help supply products for its 1760 grocery stores, Safeway owns and operates nine milk plants, eight bakery plants, four ice cream plants, four soft drink bottling plants, and four fruit and vegetable processing plants.

And little-known Italian eyewear maker Luxottica produces many famous eyewear brands—including its own Ray-Ban brand and licensed brands such as Polo Ralph Lauren, Dolce & Gabbana, Prada, Versace, and Bvlgari. It then sells these brands through two of the world's largest optical chains, LensCrafters and Sunglass Hut, which it also owns. 4 Controlling the entire distribution chain has turned Spanish clothing chain Zara into the world's fastest-growing fashion retailer: The secret to Zara's success is its control over almost every aspect of the supply chain, from design and production to its own worldwide distribution network.

Zara makes 40 percent of its own fabrics and produces more than half of its own clothes, rather than relying on a hodgepodge of slow-moving suppliers. New designs feed into Zara manufacturing centres, which ship finished products directly to 1161 Zara stores in 68 countries, saving time, eliminating the need for warehouses, and keeping inventories low. Effective vertical integration makes Zara faster, more flexible, and more efficient than international competitors such as the Gap, Benetton, and H&M. And Zara's low costs let it offer midmarket chic at downmarket prices.

A couple of summers ago, Zara managed to latch onto one of the season's hottest trends in just four weeks (versus an industry average of nine months). The process started when trendspotters spread the word back to headquarters: White eyelet—cotton with tiny holes in it—was set to become white-hot. A quick telephone survey of Zara store managers confirmed that the fabric could be a winner, so in-house designers got down to work. They zapped patterns electronically to Zara's factory across the street, and the fabric was cut.

Local subcontractors stitched white-eyelet V-neck belted dresses—think Jackie Kennedy, circa 1960—and finished them in less than a week. The US$129 dresses were inspected, tagged, and transported through a tunnel under the street to a distribution centre. From there, they were quickly dispatched to Zara stores from New York to Tokyo—where they were flying off the racks just two days later. In all, the company's stylish but affordable offerings have attracted a cult following. Zara store sales grew almost 40 percent last year to nearly US$9. 8 billion. 5 Contractual VMS

A contractual VMS consists of independent firms at different levels of production and distribution who join together through contracts to obtain more economies or sales impact than each could achieve alone. Channel members coordinate their activities and manage conflict through contractual agreements. Corporate VMS: Effective vertical integration makes Zara more flexible and more efficient—a virtual blur compared with competitors. It can take a new line from design to production to worldwide distribution in its own stores in less than a month (versus an industry average of nine months).

Chapter 12 Marketing Channels Delivering Customer Value 397 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. Franchise organization A contractual vertical marketing system in which a channel member, called a franchisor, links several stages in the production–distribution process. The franchise organization is the most common type of contractual relationship—a channel member called a franchisor links several stages in the production–distribution process.

Franchising has been the fastest-growing retailing form in Canada, growing more than 20 percent since 1993. It is estimated that Canada has four times more franchises per capita than the United States, with over 78 000 franchises across the country. Canadian franchising employs over 1 million people and represents over $100 billion in annual sales. 6 Almost every kind of business has been franchised—from motels and fast-food restaurants to dental centres and dating services, from wedding consultants and maid services to fitness centres and funeral homes. There are three types of franchises.

The first type is the manufacturer-sponsored retailer franchise system—for example, Ford and its network of independent franchised dealers. The second type is the manufacturer-sponsored wholesaler franchise system—Coca-Cola licenses bottlers (wholesalers) in various markets who buy Coca-Cola syrup concentrate and then bottle and sell the finished product to retailers in local markets. The third type is the service-firmsponsored retailer franchise system—examples are found in the auto-rental business (Hertz, Avis), the fast-food service business (McDonald’s, Burger King), the motel usiness (Holiday Inn, Ramada), and more recently inhealthcare (Vancouver-based Nurse Next Door). Let’s face it: Canadians are getting older. And with the aging population comes a greater need for quality senior home health care. Enter Ken Sim and John DeHart, founders of Nurse Next Door Home Healthcare Services, who sought to “ provide high quality services that could help improve the lives of those struggling with sick or agingfamilymembers. ” Established in 2001, the company began franchising in 2007.

By 2009, Nurse Next Door had 30 franchises across Canada and continues to expand at a rate of two franchises per month across North America—a staggering 3400 percent growth rate since 2001! The company’s success has largely been attributed to the way it supports its franchise operators. For example, client calls are handled through a centralized call centre in Vancouver, freeing franchisees from the time-consuming task of fielding urgent calls around the clock. Nurse Next Door is highly selective about which franchisee applicants it takes on, and those that are successful receive the highest level of support and training possible.

The company has earned a number of awards, including being named the sixth best midsize franchise system in North America by Franchise Business Review in 2009. As it looks toward the future, Nurse Next Door’s goal is to generate $1 billion in sales and have 500 franchisees worldwide by 2021. Given its explosive growth and the aging world population, this goal seems very achievable. 7 Nurse Next Door’s strategy of “ treating franchisees like customers it aims to retain for decades” has led to rapid growth for this Canadian company. 398

Part 3 Designing a Customer-Driven Strategy and Mix The fact that most consumers cannot tell the difference between contractual and corporate VMSs shows how successfully the contractual organizations compete with corporate chains. Chapter 13 presents a fuller discussion of the various contractual VMSs. Administered VMS Administered VMS A vertical marketing system 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.

In an administered VMS, leadership is assumed not through common ownership or contractual ties but through the size and power of one or a few dominant channel members. Manufacturers of a top brand can obtain strong trade cooperation and support from resellers. For example, General Electric, Procter & Gamble, and Kraft can command unusual cooperation from resellers regarding displays, shelf space, promotions, and price policies. Large retailers such as Walmart, Home Depot, and Chapters Indigo can exert strong influence on the manufacturers that supply the products they sell.

Horizontal Marketing Systems Horizontal marketing system A channel arrangement in which two or more companies at one level join together to follow a new marketing opportunity. Another channel development is the horizontal marketing system, in which two or more companies at one level join together to follow a new marketing opportunity. By working together, companies can combine their financial, production, or marketing resources to accomplish more than any one company could alone. Companies might join forces with competitors or noncompetitors.

They might work with each other on a temporary or permanent basis, or they may create a separate company. For example, McDonald's now places " express" versions of its restaurants in Walmart stores. McDonald's benefits from Walmart's heavy store traffic, and Walmart keeps hungry shoppers from needing to go elsewhere to eat. In another example, once major competitors, Canada's two largest wineries, T. G. Bright & Co. and Cartier Inniskillin Vintners Inc. , formed an alliance so that they could increase their economies of scale and resources. This was necessary because they wanted to export to the U.

S. market, which is dominated by huge American vintners, such as E. &J. Gallo. Such channel arrangements also work well globally. For example, McDonald's recently joined forces with Sinopec, China's largest gasoline retailer, to place drive-through restaurants at Sinopec's more than 31 000 gas stations. The move greatly speeds McDonald's expansion into China while at the same time pulling hungry motorists into Sinopec gas stations. 8 Multichannel distribution system A distribution system in which a single firm sets up two or more marketing channels to reach one or more customer segments.

Multichannel Distribution Systems In the past, many companies used a single channel to sell to a single market or market segment. Today, with the proliferation of customer segments and channel possibilities, more and more companies have adopted multichannel distribution systems— often called hybrid marketing channels. Such multichannel marketing occurs when a single firm sets up two or more marketing channels to reach one or more customer segments. The use of multichannel systems has increased greatly in recent years. Figure 12. 4 shows a multichannel marketing system.

In the figure, the producer sells directly to consumer segment 1 using direct-mail catalogues, telemarketing, and the Internet and reaches consumer segment 2 through retailers. It sells indirectly to business Horizontal marketing systems: McDonald's recently joined forces with Sinopec, China's largest gasoline retailer, to place restaurants at its more than 31 000 gas stations. Here, the presidents of the two companies shake hands while announcing the partnership. Chapter 12 Marketing Channels Delivering Customer Value 399 Figure 12. 4 Multichannel distribution system Producer

Distributors Catalogues, telephone, Internet Retailers Dealers Sales force Consumer segment 1 Consumer segment 2 Business segment 1 Business segment 2 segment 1 through distributors and dealers and to business segment 2 through its own sales force. These days, almost every large company and many small ones distribute through multiple channels. For example, John Deere sells its familiar green and yellow lawn and garden tractors, mowers, and outdoor power products to consumers and commercial users through several channels, including John Deere retailers, Home Depot stores, and online.

It sells and services its tractors, combines, planters, and other agricultural equipment through its premium John Deere dealer network. And it sells large construction and forestry equipment through selected large, full-service dealers and their sales forces. Multichannel distribution systems offer many advantages to companies facing large and complex markets. With each new channel, the company expands its sales and market coverage and gains opportunities to tailor its products and services to the specific needs of diverse customer segments.

But such multichannel systems are harder to control, and they generate conflict as more channels compete for customers and sales. For example, when John Deere began selling selected consumer products through Home Depot, many of its dealers complained loudly. To avoid such conflicts in its Internet marketing channels, the company routes all of its website sales to John Deere dealers. Changing Channel Organization Disintermediation The cutting out of marketing channel intermediaries by product or service producers, or the displacement of traditional resellers by radical new types of intermediaries.

Changes intechnologyand the explosive growth of direct and online marketing are having a profound impact on the nature and design of marketing channels. One major trend is toward disintermediation—a big term with a clear message and important consequences. Disintermediation occurs when product or service producers cut out intermediaries and go directly to final buyers, or when radically new types of channel intermediaries displace traditional ones. Thus, in many industries traditional intermediaries are dropping by the wayside.

For example, Air Canada is selling directly to final buyers, cutting travel agents from its marketing channels altogether. In other cases, new forms of resellers are displacing traditional intermediaries. For example, online marketing is growing rapidly, taking business from traditional brick-and-mortar retailers to the Internet. Consumers can buy airline tickets and hotel rooms from Expedia. ca and Travelzoo. com; electronics from SonyStyle. com; clothes and accessories from Bluefly. com; and books, videos, toys, jewellery, sports, consumer electronics, home and garden items, and almost anything else from Amazon. a—all without ever stepping into a traditional retail store. Onlinemusicdownload services such as iTunes and Yahoo! Music are threatening the very existence of traditional music-store retailers. 400 Part 3 Designing a Customer-Driven Strategy and Mix Avoiding disintermediation problems: Black & Decker's website provides detailed information, but you can't buy any of the company's products there. Instead, Black & Decker refers you to resellers' websites and stores. In fact, once-dominant music retailer Tower Records declared bankruptcy and closed its doors for good.

Disintermediation presents both opportunities and problems for producers and resellers. Channel innovators who find new ways to add value in the channel can sweep aside traditional resellers and reap the rewards. In turn, traditional intermediaries must continue to innovate to avoid being swept aside. For example, when Netflix pioneered online video rentals, it sent traditional brick-and-mortar video-rental stores such as Blockbuster reeling. To meet the threat, Blockbuster developed its own online DVD-rental service.

Now, both Netflix and Blockbuster face disintermediation threats from an even hotter channel—digital video distribution (see Real Marketing 12. 1). Similarly, to remain competitive, product and service producers must develop new channel opportunities such as the Internet and other direct channels. However, developing these new channels often brings them into direct competition with their established channels, resulting in conflict. To ease this problem, companies often look for ways to make going direct a plus for the entire channel.

For example, Black & Decker knows that many customers would prefer to buy its power tools and outdoor power equipment online. But selling directly through its website would create conflicts with important and powerful retail partners such as Home Depot, Lowe’s, Walmart, and Amazon. ca. So, although Black & Decker’s website provides detailed information about the company’s products, you can’t buy a new Black & Decker cordless drill, laser level, or leaf blower there. Instead, the Black & Decker website refers you to resellers’ websites and stores.

Thus, Black & Decker’s direct marketing helps both the company and its channel partners. 3 Channel Design Decisions We now look at several channel decisions manufacturers face. In designing marketing channels, manufacturers struggle between what is ideal and what is practical. A new firm with limited capital usually starts by selling in a limited market area. Deciding on the best channels might not be a problem: The problem might simply be how to convince one or a few good intermediaries to handle the line. If successful, the new firm can branch out to new markets through the existing intermediaries.

In smaller markets, the firm might sell directly to retailers; in larger markets, it might sell through distributors. In one part of the country, it might grant exclusive franchises; in another, it might sell through all available outlets. Then, it might add a web store that sells directly to hard-to-reach customers. In this way, channel systems often evolve to meet market opportunities and conditions. Real Marketing Netflix: Disintermediator or Disintermediated? 12.

1 Baseball great Yogi Berra, known more for his mangled phrasing than for his baseball prowess, once said, “ The future ain’t what it used to be. For Netflix, the world’s largest online movie-rental service, no matter how you say it, figuring out the future is challenging and a bit scary. Netflix faces dramatic changes in how movies and other entertainment content will be distributed. The question is, will Netflix be among the disintermediators or among the disintermediated? Less than a decade ago, if you wanted to watch a movie in the comfort of your own home, your only choice was to roust yourself out of that easy chair and trot down to the local Blockbuster or another neighbourhood movie-rental store.

In fact, that’s how most people still Netflix faces dramatic changes in how movies and other entertainment content will be distributed. Instead of simply do it. Blockbuster has grown to become watching the developments, Netflix intends to lead them. the world’s largest store-rental chain, Since first opening its virtual doors, Netflix has continwith more than 7800 outlets worldwide ued to add innovative features. Its “ dynamic queue” lets and more than US$5. 5 billion in annual sales. customers select as many movie titles as they wish and rank But now, thanks to Netflix, that distribution model is them by preference.

Netflix has also developed an online changing quickly. In the late 1990s, Netflix pioneered a new recommendation system, called Cinematch, to help customers way to rent movies—via the Web and direct mail. With Netflix, find movies they’ll love based on their own past ratings, you pay a monthly subscription fee and create a movie wish member and critic reviews, and top-rented lists. list online. Netflix mails you a set number of DVDs from your

As a result, more and more customers are signing up list at a given time, which you can keep for as long as you like. ith Netflix. Membership has grown to more than 7. 5 million As you return the DVDs in prepaid return envelopes, Netflix subscribers, and in just the past two years, sales and profits automatically sends you new ones from your list. While Netflix have surged 77 percent and 60 percent, respectively. Meanis not available in Canada, Zip. ca offers a very similar service, while, Netflix’s success has sent Blockbuster and other videooffering Canadians over 72 000 titles to choose from. rental stores reeling.

As Netflix sales and profits have soared, Netflix offers lots of advantages over the traditional Blockbuster’s sales have lagged and losses have mounted. Blockbuster brick-and-mortar system. With store video The video rental giant has lostmoneyin 10 of the last rentals, you have to make a special trip whenever you want a 11 years. Although the traditional brick-and-mortar videomovie, and if you don’t plan ahead, you’ll probably find the rental market is still alive and kicking, it’s stagnating as the latest hot releases out of stock.

As for finding copies of oldies red-hot online channel gains momentum. but goodies, or an old documentary or independent film, To meet the disintermediation threat, Blockbuster introforget it—stores can hold only a limited selection of DVDs. duced its own online video-rental service. In fact, Blockbuster Finally, many consumers are frustrated by short due dates Total Access takes the new distribution model one step furand those dreaded late return fees. In contrast, Netflix isn’t ther. Total Access customers can order videos online and bound by store-space limitations.

It offers a huge selection of then return or exchange them either through the mail or at more than 90 000 titles and 40 million DVDs. The Netflix systheir local Blockbuster store. Blockbuster's online business tem eliminates store trips—you always have a stack of DVDs quickly grew to over 2 million subscribers before levelling off. on hand. And there are no per-movie charges, no due dates, and no late fees. 402 Part 3 Designing a Customer-Driven Strategy and Mix However, for the most part, Blockbuster is still struggling to find the right formula.

And so the video-rental channels battle continues. Blockbuster claims the advantages of a click-and-mortar model that offers both online and store services. In contrast, Netflix sees physical stores as an unnecessary and costly limitation. Says Netflix founder and CEO Reed Hastings, " For people who'd love never to go into a Blockbuster store ever again, we offer better selection, better tools for choosing movies, and more consistent overnight delivery. " Either way, there's no going back to the past—the two competitors are rapidly disintermediating store-only video-rental outfits.

But just as the present isn't what it used to be, neither is the future. At the same time that Netflix is displacing traditional store channels, it faces its own disintermediation threat from a potentially even hotter channel—digital video distribution in the form of digital downloads and video on demand (VOD). Digital distribution is a fact of life in the music industry, where music download services are quickly making traditional CD retailers obsolete. Most experts agree that it's only a matter of time before digital video distribution displaces DVD video sales and rentals.

In fact, it's already begun. These days, you can download all kinds of video entertainment—from movies and TV shows to ads and amateur videos—to your computer, iPod, or even your cellphone. Satellite and cable TV companies are promising VOD services that will let you view movies and other video entertainment on television whenever and wherever you wish. And video-rental download services such as CinemaNow are already offering a growing list of downloadable titles via the Web.

Digital video downloads and video on demand create obvious cost, distribution, and customer convenience advantages over physically producing and distributing DVDs. For sure, the digital video distribution industry still faces problems. Downloading videos can take a lot of time and yields less-than-DVD quality. Perhaps the biggest barrier so far— Hollywood has been cautious about granting video distribution rights, severely limiting the number of available titles. In time, however, all these limitations will likely dissipate. When that happens, it could be lights out for the DVD sales and rental industry.

Netflix CEO Hastings understands the future challenges. " We're sure that we're going to be buying cars in 25 years, whereas renting DVDs through the mail in 25 years—for sure that's not going to exist," he says. The solution? Keep innovating. Instead of simply watching digital video distribution developments, Netflix intends to lead them. Netflix has already added a " watch instantly" feature to its website that allows subscribers to instantly stream near-DVD-quality video for a limited but growing list of movie titles and TV programs. Our intention," says Hastings, " is to get [our watch instantly] service to every Internet-connected screen, from cellphones to laptops to WiFi-enabled plasma screens. ” In this way, Netflix plans to disintermediate its own distribution model before others can do it. Compared to the United States, the online DVD market in Canada is still in its infancy. Thus, it is anticipated that Canadian firms like Zip. ca will experience more modest growth, primarily because of the lack of content rights in this country as compared to those in the Unites States. To Hastings, the key to the future is all in how Netflix defines itself. If [you] think of Netflix as a DVD rental business, [you’re] right to be scared,” he says. But “ if [you] think of Netflix as an online movie service with multiple different delivery models, then [you’re] a lot less scared. We’re only now starting to deliver [on] that second vision. ” When asked what Netflix will be like in five years, Hasting responds, “ We hope to be much larger, have more subscribers, and be successfully expanding into online video. ” Sources: Quotes and other information from Matthew Boyle, “ Reed Hastings,” Fortune, May 28, 2007, p. 30; Nick Wingfield, “ Netflix vs.

Naysayers,” Wall Street Journal, March 27, 2007, p. B1; Yuval Rosenberg, “ What’s Next for Netflix? ” Fortune, November 29, 2006, p. 172; Paul R. La Monica, “ DVD or Download? ” CNNMoney. com, June 26, 2006; Nancy Macdonald, “ Blockbuster Proves It’s Not Dead Yet,” Maclean’s, March 17, 2008, p. 36; Michael V. Copeland, “ Netflix Lives! ” Fortune, April 28, 2008, p. 40; “ Netflix, Inc. ,” Hoover’s Company Records, April 15, 2008, p. 100752; “ Online DVD Rental Firms Find Big Profits in Tough Times,” CBC News, January 27, 2009; and information from www. netflix. com and www. blockbuster. om, accessed November 2008. Marketing channel design Designing effective marketing channels by analyzing consumer needs, setting channel objectives, identifying major channel alternatives, and evaluating them. For maximum effectiveness, however, channel analysis and decision making should be more purposeful. Marketing channel design calls for analyzing consumer needs, setting channel objectives, identifying major channel alternatives, and evaluating them. Analyzing Consumer Needs As noted previously, marketing channels are part of the overall customer-value delivery network.

Each channel member and level adds value for the customer. Thus, designing the marketing channel starts with finding out what target consumers want from the channel. Do consumers want to buy from nearby locations or are they willing to travel to more distant centralized locations? Would they rather buy in person, by phone, or online? Do they value breadth of assortment or do they prefer specialization? Do consumers want many add-on services (delivery, repairs, installation), or will they obtain these elsewhere? The Chapter 12 Marketing Channels Delivering Customer Value 403 aster the delivery, the greater the assortment provided, and the more add-on services supplied, the greater the channel's service level. Providing the fastest delivery, greatest assortment, and most services may not be possible or practical. The company and its channel members may not have the resources or skills needed to provide all the desired services. Also, providing higher levels of service results in higher costs for the channel and higher prices for consumers. The company must balance consumer needs not only against the feasibility and costs of meeting these needs but also against customer price preferences.

The success of discount retailing shows that consumers will often accept lower service levels in exchange for lower prices. Setting Channel Objectives Companies should state their marketing channel objectives in terms of targeted levels of customer service. Usually, a company can identify several segments wanting different levels of service. The company should decide which segments to serve and the best channels to use in each case. In each segment, the company wants to minimize the total channel cost of meeting customer service requirements.

The company’s channel objectives are also influenced by the nature of the company, its products, its marketing intermediaries, its competitors, and the environment. For example, the company’s size and financial situation determine which marketing functions it can handle itself and which it must give to intermediaries. Companies selling perishable products may require more direct marketing to avoid delays and too much handling. In some cases, a company may want to compete in or near the same outlets that carry competitors’ products.

In other cases, companies may avoid the channels used by competitors. Mary Kay, for example, sells direct to consumers through its network of more than 1 million independent beauty consultants in 34 markets worldwide rather than going headto-head with other cosmetics makers for scarce positions in retail stores. And GEICO primarily markets automobile and homeowner’s insurance directly to consumers via the telephone and Internet rather than through agents. Finally, environmental factors such as economic conditions and legal constraints may affect channel objectives and design.

For example, in a depressed economy producers want to distribute their goods in the most economical way, using shorter channels and dropping unneeded services that add to the final price of the goods. Identifying Major Alternatives When the company has defined its channel objectives, it should next identify its major channel alternatives in terms of types of intermediaries, the number of intermediaries, and the responsibilities of each channel member. Types of Intermediaries A firm should identify the types of channel members available to carry out its channel work. Most companies face many channel member choices.

For example, until recently, Dell sold directly to final consumers and business buyers only through its sophisticated phone and Internet marketing channel. It also sold directly to large corporate, institutional, and government buyers using its direct sales force. However, to reach more consumers and to match competitors such as HP, Dell now sells indirectly through retailers such as Best Buy and Walmart. It also sells indirectly through “ value-added resellers,” independent distributors and dealers who develop computer systems and applications tailored to the special needs of small and medium-sized business customers.

Using many types of resellers i