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DISTRIBUTION

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Theo M.M. Verhallen[1]

I. INTRODUCTION

The delivery of goods from manufacturer to user often involves other parties as well. In buying a textbook, we typically get it from an independent bookstore, not from the publisher. Different manufacturers have made fundamentally different decisions on channels of distribution. For example:

- Avon sells through its own sales force directly to individual consumers in their homes.
- Tupperware sells directly to end consumers with a "party-plan" approach.
- Seat sells cars to franchised dealers, who in turn sell to consumers.
- Philips sells its small appliances, such as mixers and hair dryers, to wholesalers, who then sell to retail outlets.

Thus some manufacturers sell directly to consumers (Avon, Tupperware), others involve one intermediary (Seat), and still others (Philips), make use of two or more intermediairs. While these examples all concern consumer goods, this also holds for industrial goods.
Why do these "middlemen" exist? How many intermediaries should there be at each level - for example, how many franchised dealers should Seat have? How can the manufacturer make other members of the distribution channel do what they want them to do? These issues will be adressed in this chapter.
For most organizations, the objective is to enable the target market to gain access to the product or service in a way that is convenient for the customer and that is cost-effective for the supplier. However, the difficulty that companies are facing nowadays is to achieve competitive advantage relative to the competition by the way in which the product is presented. Aspects such as quality and service have become the key components of added value in the channel of distribution. Companies are no longer in the business of simply minimizing the costs of distribution. They are perpetually assessing the trade-off between level of customer service and the cost of delivering it. When a company has made a commitment to hold sufficient stock of their key assortment, this is a benefit that can be advertized. However it is an expensive promise, as an overview of the various channel functions will illustrate.

II. THE CHANNEL OF DISTRIBUTION DEFINED

The term *channel of distribution* has its origins in the French word for canal. This suggests a path that goods take as they flow from producers to consumers. In this

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sense, the channel of distribution is defined by the organizations or individuals along the route from producer to consumer. Because the beginning and ending points of the route must be included, both producer and consumer are always members of the channel of distribution. In addition, there may be intermediate stops along the way. Several marketing intermediairs have developed to facilitate the flow of the physical product. These marketing intermediaries specialize in distribution rather than production. They include wholesalers, who sell to retailers or other organizations that resell the product, and retailers, who sell to ultimate consumers. When intermediaries join with a manufacturer in a loose coalition to engage in exploiting joint opportunities, a channel of distribution is formed[2].

A **marketing** or **distribution channel** is composed of a network of interdependent companies or agencies involved in the movement or transmission of an item of value from the point of production to the point of consumption. The end-user will be concerned with *what* is delivered, *how* it is delivered, *where* and *when*. Assuming that the end-user receives the correct product to match the need, then each of the other three components has a value in its own right which contributes to the final purchase price[3].

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[2] See William G. Zikmund and Michael d'Amico, (1995), *Effective Marketing, Creating and Keeping Customers,* West Publishing Company, New York

[3] see Susan Norgan (1994), *Marketing Management, A European Perpective*, Adison-Wesley, page 265

Figure 1: major participants in the distribution channel

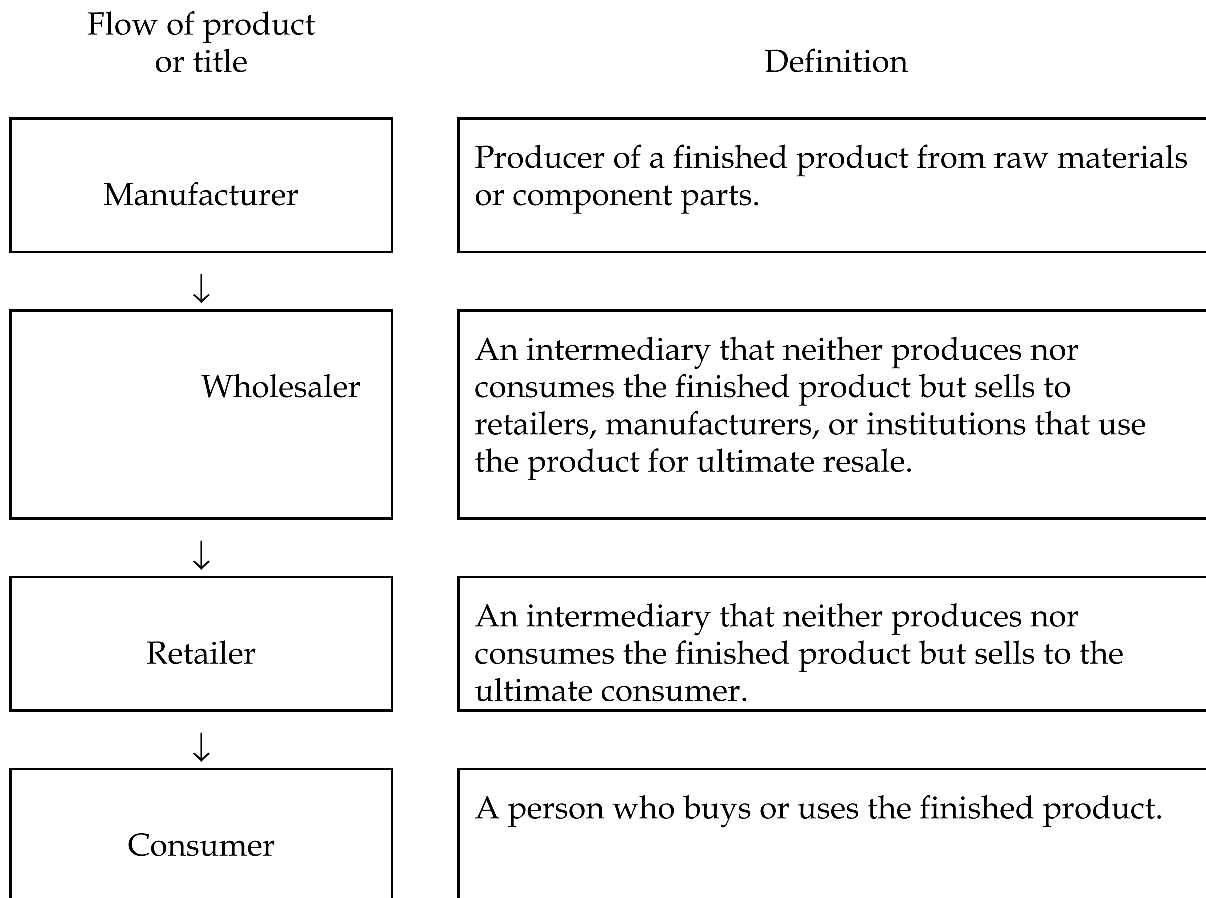


Figure 1 illustrates a basic channel of distribution consisting of a manufacturer, a wholesaler, a retailer, and the ultimate consumer. Each of these parties engages in a transaction that involves movement of a physical good and/or a transfer of title (ownership) to that product. The actual path that a product or title takes may be simpler or much more complex than the one illustrated in figure 1.

We should note that each distribution channel relates to a product that has taken on its final form. The channel of distribution for an automobile begins after the product has become a finished automobile. It does not include the paths of raw materials (such as steel) or component parts (such as tires) to the automobile manufacturer. These products have their own channels, which end with the industrial user, the auto manufacturer.

The channel's purpose in moving products to people is more than a simple matter of transportation. The channel of distribution must accomplish the task of transferring the title to the product (the ownership) as well as facilitating the physical movement of the goods to their ultimate destination. Although title transfer and the exchange of physical possession (transportation) generally follow the same channel of distribution, they do not necessarily need to follow the same path.

A distinction may be made between **merchant intermediaries**, which take title to the product, and **agent intermediaries**, which do not take title to the product. Although agent intermediaries never own the goods, they perform a number of

marketing functions, such as selling, that facilitates further transactions in the exchange process.

Most intermediaries are independent organizations tied to the producers they deal with only by mutual agreement. Some intermediaries are owned by producers, such as most of the retail outlets of Benetton.

In service marketing, it sometimes appears that there is no channel of distribution. When a hairdresser delivers a product, such as a haircut, he or she deals directly with the customer. But even in these shortest of distribution channels, where no intermediaries are involved, marketing functions are being performed. The required activities to *what* is delivered *how*, *where* and *when* are simply performed by the provider of the service (or, in a self-service environment, by the ultimate consumer).

When identifiable intermediaries are present, the channel members form a coalition intended to act on joint opportunities in the marketplace. Each channel member, from producer to retailer, must be rewarded or see some opportunity for continued participation in the channel.

The coalition between channel members may be a loose one resulting from negotiation or a formal set of contractual arrangements identifying each party's role in the distribution process. The **conventional channel** is characterized by loosely aligned, relatively autonomous marketing organizations that have developed a system to carry out a trade relationship. In contrast, formal **vertical marketing systems** are more tightly organized systems in which the channel members are either owned by a manufacturer or a distributor, linked by contracts or other legal agreements such as franchises, or informally managed and coordinated as an integrated system. Vertical marketing systems are discussed in greater detail later in this chapter.

III. WHY USING INTERMEDIARIES?

Why not delivering the goods directly to the final consumer? Why placing the firm's destiny in the hands of intermediaries?
There can be several reasons for producers to use intermediaries:

- Direct marketing requires to many financial resources for most producers.
- Direct marketing would require many producers to become middlemen for the complementary products of other producers in order to achieve mass-distribution economies. Most producers lack skills in performing the middlemens job.
- Producers who can afford to establish their own channels can often earn a greater return by increasing their investments in their main business.

The use of middlemen largely boils down to their superior efficiency in making goods widely available and accessible to target markets. Marketing intermediaries, through their contacts, experience, specialization, and scale of operation, offer the firm more than it can usually achieve on its own.

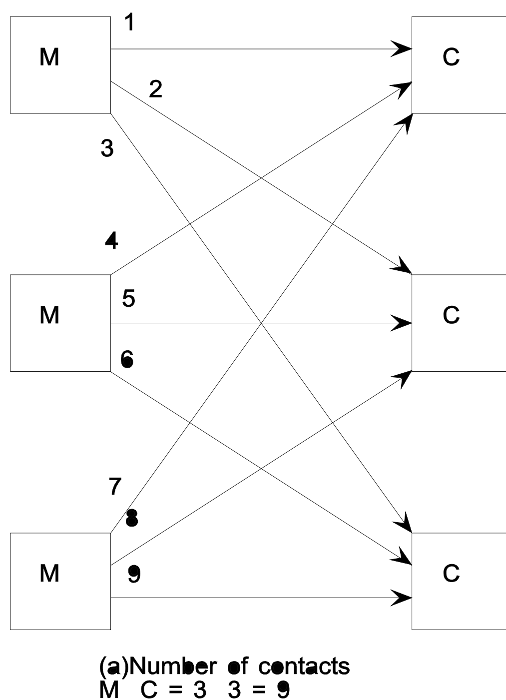
The basic role of marketing intermediaries is to transform the heterogeneous supplies into assortments of goods that people want to buy. According to Stern and

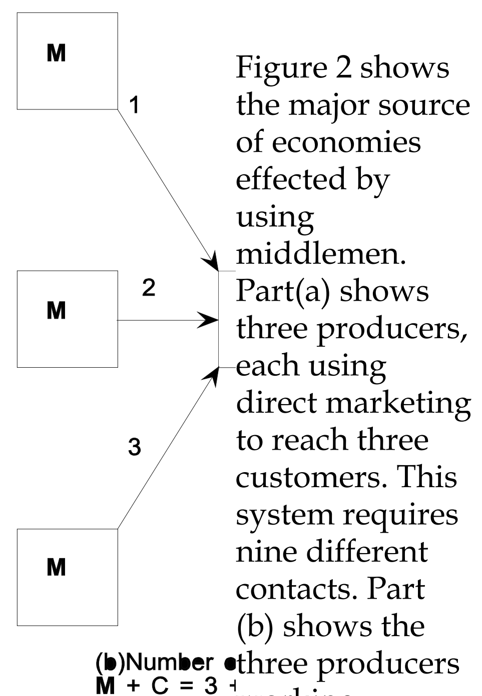
El-Ansary[4]:

> Intermediaries smooth the flow of goods and services...This procedure is necessary in order to bridge the discrepancy between the assortment of goods and services generated by the producer and the assortment demanded by the consumer. The discrepancy results from the fact that manufacturers typically produce a large quantity of a limited variety of goods, whereas consumers usually desire only a limited quantity of a wide variety of goods.

Wroe Alderson[5] stated the same point: "The goal of marketing is the matching of segments of supply and demand."

Figure 2: Efficiency in exchanges provided by an intermediary





M = Manufacturer C = Customer D = Distributor

Figure 2 shows the major source of economies effected by using middlemen. Part(a) shows three producers, each using direct marketing to reach three customers. This system requires nine different contacts. Part (b) shows the three producers working through one distributor, who contacts the three customers. This system requires only six contacts. In this way, middlemen reduce the amount of work that must be done. This affects the costs of transportation.

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4 Stern and El-Ansary, *Marketing Channels*, 4th edition, Englewood Cliffs, NJ.: Prentice Hall, 1992, page 1

5 Alderson Wroe, *The Analytical Framework for Marketing*", in "Proceedings - Conference of Marketing Teachers from Far Western States, Berkeley: University of California Press, 1958, In Philip Kotler, *Marketing Management*, 1994 page 526

III.1 Functions of Intermediaries[6]

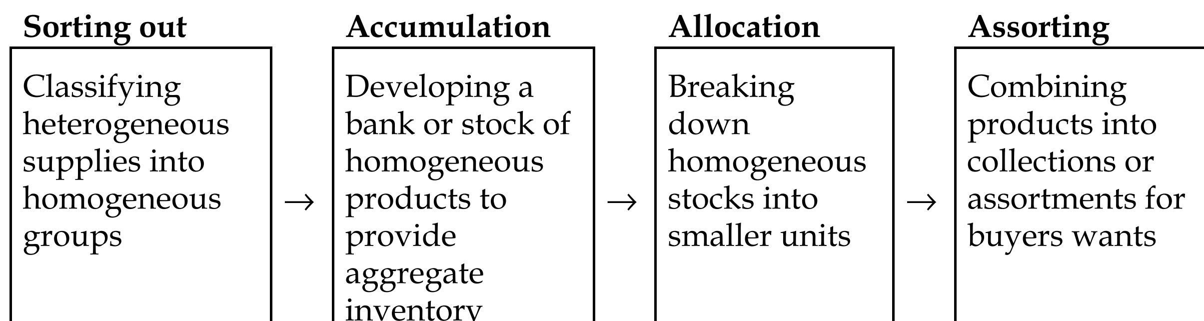
Before we examine the functions of intermediaries in some detail, it should be noted that a distribution network helps overcome two major distribution problems. Consider a firm which manufactures bulbs. To make bulbs the most economical way possible, the producer turns out a hundred thousand products each day. Few persons, however, want to buy a hundred thousand bulbs. Thus the quantity of bulbs that the company can produce efficiently is more than the average customer wants. The result is called a *discrepancy in quantity*.

An **assortment** is a combination of products put together to satisfy the customer in his demands . In order to satisfy his demands a consumer holds and creates an assortment. In general, the customers assortment consists of a large number of products and services, ranging from a stereo to foods and cars. The set of products made available to customers is an organisation's assortment. Yet a manufacturer normally has a narrow assortment because it makes only one or a limited range of products. There is a *discrepancy in assortment* because a consumer wants a broad assortment but an individual manufacturer produces a narrow assortment.

Quantity and assortment discrepancies are resolved through the sorting activities of intermediaries in a marketing channel. **Sorting activities** are functions that allow channel members to divide roles and separate tasks. Sorting activities, as Figure 3 shows, may be grouped into four main tasks: sorting out, accumulation, allocation, and assorting of products.

Sorting out, the first step in developing an assortment, is the separating of conglomerates of heterogeneous products into relatively uniform, homogeneous groups based on product characteristics such as size, shape, weight or colour. Sorting out is especially common in the marketing of agricultural products and other raw materials, which vary widely in size, grade and quality and would be largely unusable in an undifferentiated mass.

Figure 3: Sorting activities conducted by intermediaries



[6] Based on Dibb, Sally, Lyndon Simkin, William M. Pride and O.C. Ferrel, *Marketing: Concepts and Strategies*, second European edition, Houghton Mifflin Company, London, 1994

Sorting out thus helps alleviate discrepancies in assortment by making relatively homogeneous products available for the next step, accumulation.

Accumulation is the development of a bank or inventory of homogeneous products which have similar production or demand requirements.

Combining many small groups of similar products into larger groups serves several purposes. Products move through subsequent marketing channels more economically in large quantities because transport rates are lower for bulk loads. In addition, accumulation gives buyers a steady supply of products in large volumes. Accumulation lets producers continuously use up stocks and replenish them, thus minimising losses from interruptions in the supply of materials.

For both buyer and seller, accumulation also alleviates some of the problems associated with price fluctuations and highly seasonal materials. Buyers may obtain large volume purchases at lower prices because sellers are anxious to dispose of perishable goods; purchasing agents may accumulate stocks of materials in anticipation of price rises. In other cases, sellers may receive higher prices because they enter into longterm supply contracts with producers or they agree to store accumulated materials until the producer is ready for them. Accumulation thus relieves discrepancies in quantity. It enables intermediaries to build up specialised inventories and allocate products according to customers' needs.

Allocation is the breaking down of large homogeneous inventories into smaller lots. This process, which addresses discrepancies in quantity, enables wholesalers to buy efficiently in lorry or container loads and then apportion products by cases to other channel members.

Because supply and demand are seldom in perfect balance, allocation is influenced by several factors. At times price is the overriding consideration. The highest bidder, or perhaps the buyer placing the largest order, is allocated most of the stock. At other times an intermediary gives preference to customers whose loyalty has been established or to those whose businesses show the most growth potential. In still other cases, products are allocated through compromise and negotiation.

Depending on the product, allocation may begin with the manufacturer and continue through several levels of intermediaries, including retailers. Allocation ends when the ultimate user selects the desired quantity of a particular products from the assortment of products available.

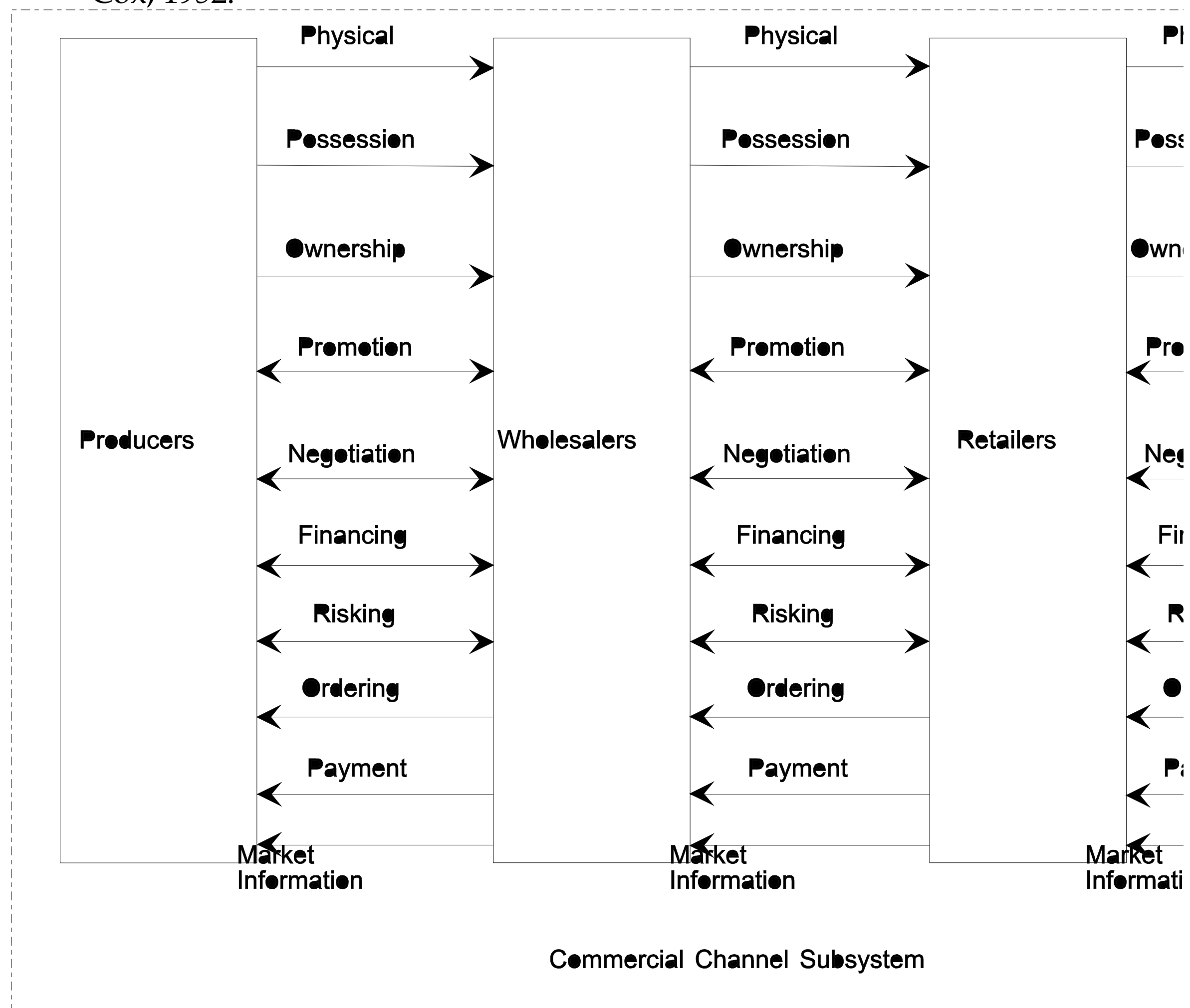
Assorting is the process of combining products into collections or assortment which buyers want to have available in one place. Assorting eliminates discrepancies in assortment by grouping products to satisfy buyers.

Buyers want an assortment of products at one location because of some task they want to perform or some problem they want solved. A buyer looking for a variety of products, all serving different purposes, requires a broad assortment from which to choose: a buyer with more precise needs or interests will seek out a narrower, and deeper, product assortment.

Assorting is especially important to retailers, and they strive to create assortments that match the demands of consumers who patronise their stores. When retailers fail to keep pace with shifts in consumer attitudes new specialists - such as

retail outlets for computer products or video games - may enter the market to provide assortments existing retailers do not offer.

Figure 4: Marketing flows in channels. Adapted from R.S. Vaile, E.T. Grether and R. Cox, 1952.



III.2. Flows in marketing channels

The four basic functions as discussed stress the main tasks of the distribution system. In addition to this one should look to the final service output a channel has to realize. In short one could say that the distribution channel should provide goods or services to the end users at the right *quantity, quality, time*, and *place.* This means that other functions have to be performed too. According to Vaille (1952), one can make a distinction between nine basic functions or flows within a marketing channel:

- *Information*: The collection and dissemination of marketing research information about potential and current customers, competitors, and other actors and forces in the marketing environment.

- *Promotion*: The development and dissemination of persuasive communications about the offer designed to attract customers.
- *Negotiation*: The attempt to reach final agreement on price and other terms so that transfer of ownership or possession can be effected.
- *Ordening*: The backward communication of intentions to buy by the marketing-channel members to the manufacturer.
- *Financing*: The acquisition and allocation of funds required to finance inventories at different levels of the marketing channel.
- *Risk Taking*: The assumption of risks connected with carrying out the channel work.
- *Physical Possession*: The successive storage and movement of physical products from raw materials to the final customers.
- *Payment*: Buyers paying their bills through banks and other financial institutions to the sellers.
- *Title*: The actual transfer of ownership from one organization or person to another.

These functions are listed in the normal order in which they arise between any two channel members. Physical possession, ownership and promotion are typically forward flows from producer to consumer. The negotiation, financing, and risking flows move in both directions, whereas ordering and payment are backward flows. In figure 4 the directions of the flows are illustrated.

III.3 Number of Channel levels

The classical way of distributing goods is by using intermediaries like wholesalers and retailers, who sell the goods to the final consumer. This so called conventional distribution channel is illustrated in figure 5.

Figure 5: Distribution Channels for Consumer Goods

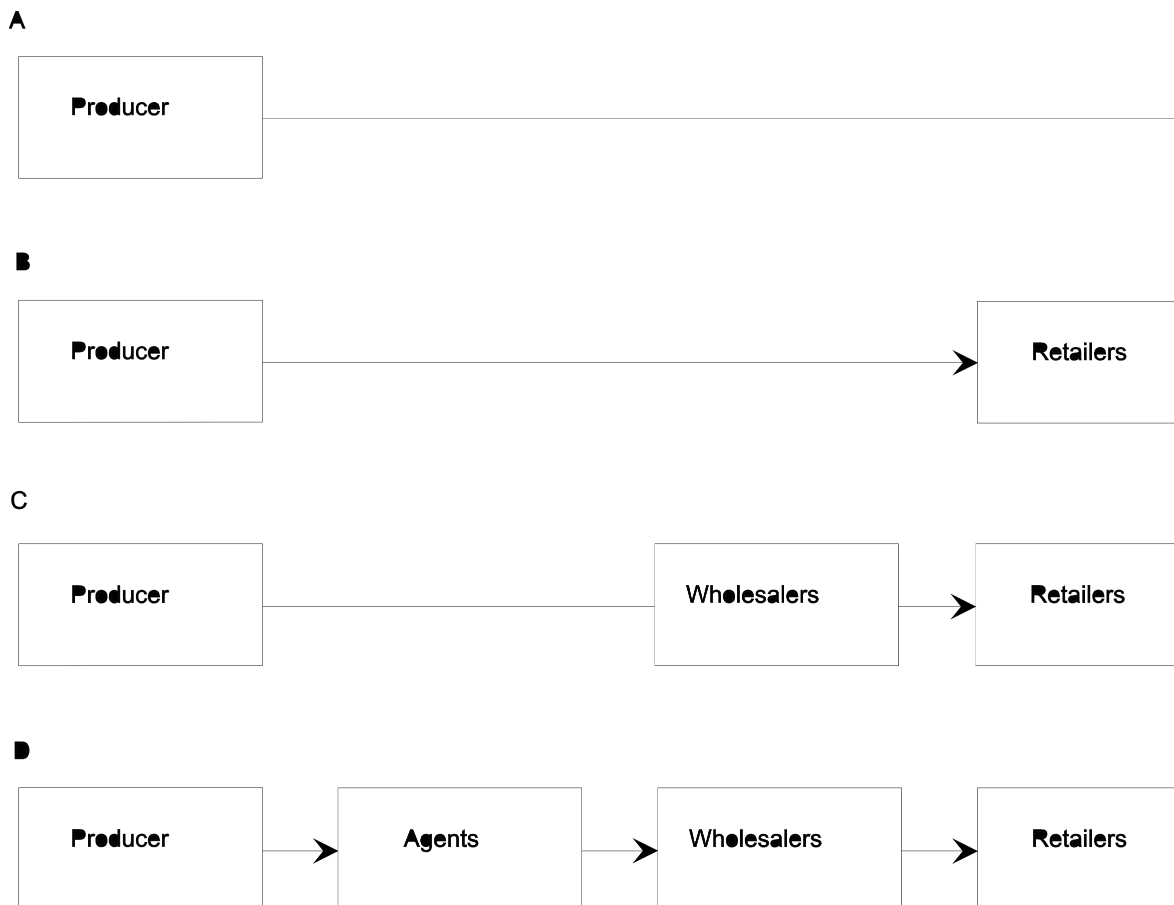


Figure 5 shows the four most common marketing channels for consumer goods. It also shows the number of levels in each marketing channel by the number of intermediaries between the producer and the consumer. A distinction can be made between the direct and indirect marketing channel.

In the *direct marketing* channel the producer and the end user deal directly with each other. The consequence is that the producer must perform all distribution functions. Tupperware, who sells kitchen goods through home parties, and Avon who sells cosmetics to women on a door to door bases, can be considered as examples of direct marketing. Other forms of direct marketing are mail order selling, teleshopping, advertising selling, direct mail, and television in home shopping. The strategies of these direct marketers depend largely on their data-base management.

The manufacturer-retailer-consumer channel is called the *one-level-channel*. The one-level channel is mostly dominated by a large scale retailer, like for example Carrefour. The consequence is that the retailer has to perform most of the distribution functions. He is willing to do so because of the economies of scale, discounts, and the possibility to have special, exclusive products produced for his retail operation by dealing directly with the manufacturers. Sometimes, the manu-facturer takes over some of the distribution tasks like keeping inventory. This is mostly done under pressure of the large scale retailer or because the producer can

save costs by performing the wholesalers tasks.

The manufacturer-wholesaler-retailer-consumer-channel is called the *two-level-channel.* The two-level-channel is mostly used when a product is sold by a high number of different retailers. For example beer is sold in almost every food-retail outlet as well as in many other places like petrol stations, bars, restaurants, vending machines, etcetera. For this reason it is impossible for the manufacturers to deal directly with all the retailers who sell their products. By using a number of wholesalers the manufacturer can reach his final targetgroup much easier and more cost effective.

The *three-level-channel* consists of the traditional two level channel extended with an agent. The agent supports the manufacturer by selling the goods to the wholesaler and sometimes retailer. Especially importing and exporting manufacturers make use of an agent. The reason for this is that they lack experience in marketing in foreign countries.

Channels of industrial goods are somewhat different from channels of customer goods. These differences can be explained by the characteristics of the industrial market. The total number of organizational buyers is much smaller compared to the customer market. In addition, organizational buyers are more concentrated geographically, and they often buy in relatively large quantities. On top of this, many industrial goods, like for instance machinery, need a great deal of pre and after sales service. Because of these reasons, distribution channels for industrial good are usually shorter. In the industrial market a manufacturer uses its salesforce to sell directly to his industrial customers. In general this is called *business to business marketing* (B-to-B marketing). The direct channel, in B-to-B marketing, is most efficient when buyers are large and well defined, when selling requires extensive negotiations, when the price per unit is high, and when the product requires extensive service and support. In other cases industrial distributors are used to get the product available for the industrial user.

Channels normally describe a forward movement of products. One can also talk about *backward channels*. According to Zikmund and Stanton[7]:

> *The recycling of solid wastes is a major ecological goal. Although recycling is technologically feasible, reversing the flow of materials in the channel of distribution - marketing trash through a "backward" channel - presents a challenge. Existing backward channels are primitive, and financial incentives are inadequate. The consumer must be motivated to undergo a role change and become a producer - the initiating force in the reverse distribution process.*

Reversed channels have gained attention with the growth of *recycling* efforts and consumer interest in the environment. The recycling industry is becoming an

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[7] William C. Zikmund and William J. Stanton, *Recycling Solid Wastes: AChannels of Distribution Problem*, Journal of Marketing, July 1971, p. 34

important player in modern society. There are already recycling channels for refrigerators, cars, computers, glass, batteries, chemicals etcetera. Another type of reverse channel is the system set up for product recalls.

Channels of services are mostly characterized by the short channel, i.e. direct marketing. The reason for this is that in general services are produced and consumed at the same time. For a hair cut you have to go to the hairdressers and for a financial advice you have to go to a bank or an accountant. When service firms use intermediaries, these are usually agents or brokers. An example is a temporary employment agency, who acts on behalf of their customers to select and appoint temporary staff.

IV. THE STRUCTURE OF THE CHANNEL

Designing the perfect channel to accomplish the firm's objectives in its target product-market is one thing. But actually getting the desired number of appropriate middlemen to carry the product and perform their functions consistent with the manufacturer's marketing strategy presents an entirely new set of challenges. The structure of a marketing channel depends mainly on two factors namely the members of that channel and the extend of their relationship. Interdependence, mutual interest, and power are important variables in structuring the marketing channel.

A **traditional marketing channel** consists of an independent producer, agents, wholesalers, and/or retailers, each operating as a separate business entity primarily concerned with maximizing its own profits. One authority characterizes such conventional channels as "highly fragmented networks in which loosely aligned manufacturers, wholesalers, and retailers have bargained with each other at arm's length, negotiated aggressively over terms of sale, and otherwise behaved autonomously."[8] In such systems no one member has substantial control over the actions of the others. It can be difficult for a manufacturer to gain the cooperation of these middlemen or to coordinate their efforts in distributing its product.

In recent years, manufacturers and large wholesalers and retailers like Sears have sought ways to improve their control and coordination of the activities of their distribution channel members. As a result, several forms of vertical marketing systems have emerged. These **vertical marketing systems** (VMSs) are:

> *professionally managed and centrally programmed networks pre-engineered to achieve operating economies and maximum market input... These vertical marketing systems are... designed to achieve technological, managerial and promotial economies through the integration, coordination and synchronization of marketing flows from points of production to points of ultimate use.*[9]

Firms have attempted to develop and manage such integrated VMSs in one of three

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8 Bert C. McCammon, Jr., "Perspectives for Distribution Programming," in Vertical Marketing Systems, ed. Louis P. Bucklin (Glenview, Ill.: Scott, Foresman, 1970), p.43.

9 see footnote 8

ways: A **corporate VMS** uses the formal authority acquired by vertically integrating the system. A **contractual VMS** formulates agreements spelling out a coordinated set of rights and obligations for members of the system. An **administered VMS** uses the firm's economic position or expertise to provide inducements for cooperation from other members. Figure 6 diagrams the three VMSs - corporate VMSs, contractual VMSs, and administered VMSs.

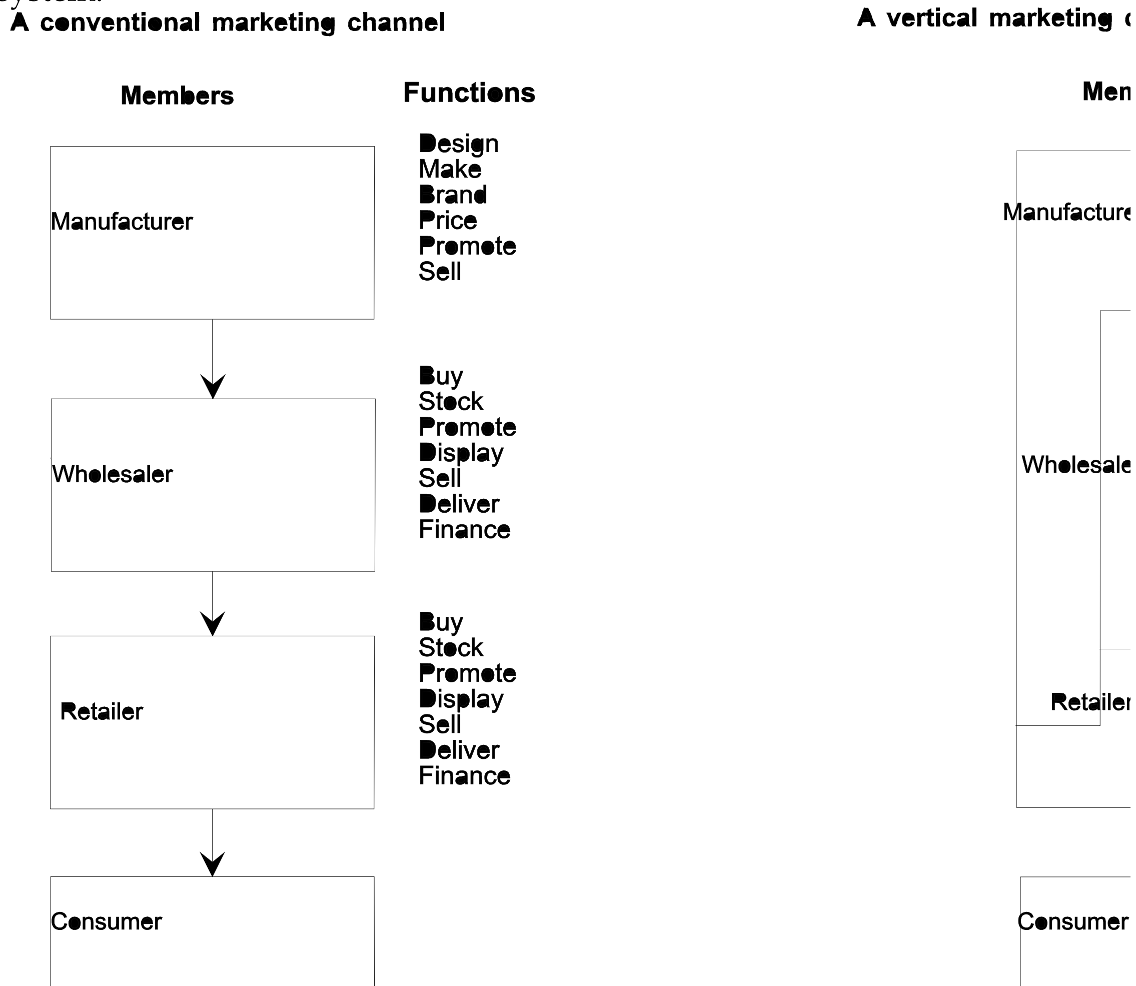
Greater coordination and cooperation in all these VMSs lead to greater marketing effectiveness and distribution economies by virtue of their size, bargaining power, and the elimination of duplicated functions. As a result, VMSs have become the dominant form of channel arrangement, particularly in the distribution of consumer goods and services. The remainder of discussion of channel management focuses on how firms can develop and maintain such systems. First, we discuss the three VMSs, their relative advantages, and the conditions under which each is most appropriate. Next, we examine the sources of power and the inducements and incentives that channel administrators use to gain the support of other system members.

Figure 6: Vertical marketing systems

The *corporate* VMS combines all stages of the marketing channel, from producers to consumers, under a single ownership. For example, Shell established a corporate VMS operating corporate owned production facilities and service stations. Supermarket chains that own food processing plants and large retailers that

purchase wholesaling and production facilities are other examples of corporate VMSs. Bally Frame who owns a production plant, a wholesale and retail organization under his own name. Figure 7 contrasts a conventional marketing channel with a VMS, which consolidates marketing functions and institutions[10].

Figure 7: Comparison of a conventional marketing channel and a vertical marketing system.



In an *administered* VMS, channel members are independent, but a high level of inter-organisational management is achieved by informal co-ordination. Members of and administered VMS may agree, for example, to adopt uniform accounting and ordering procedures and to co-operate in promotional activities. Although individual channel members maintain their autonomy, as in conventional marketing channels, one channel member (such as the producer or a large retailer) dominates the administered VMS, so that distribution decisions take into account the system as a whole. Because of its size and power as a retailer, Marks & Spencer exercises a strong influence over the independent manufacturers in its marketing channels. Also

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[10] Figure 7 is adapted from *Strategic Marketing*, by David J. Kollat et.al, The Dryden Press, 1972

Kellogg's (cereals) and Volvo (cars and trucks) dominate its marketing channels.

Under a *contractual* VMS, the most popular type of vertical marketing system, interorganisational relationship are formalised through contracts. Channel members are linked by legal agreements that spell out each member's rights and obligations. As for instance in franchising[11]

A channel member might coordinate two successive stages in the distribution channel by offering franchise contracts that give others the right to participate in the business provided they accept the agreement terms and pay a fee. Such contracts usually specify a variety of operational details - including which members of the system will perform specific functions and how - as well as mechanisms to evaluate members' performance and to terminate members who fail to perform adequately.

[11] Based on Stern and El-Ansary, *Marketing Channels*, 4th edition, Englewood Cliffs, NJ.: Prentice Hall, 1992, pp. 332-48.

Franchising has great versatility. Such systems operate in almost every business area and cover a wide variety of goods and services, including the following.[12]

accounting and tax services	car washes	lawn care
art galleries	credit and collection	motels and hotels
auto rentals	employment agencies	pet stores
auto repair	entertainment	printing
auto accessories	fast food	real estate
beauty salons	food stores	retail stores
building services	health aids	schools
candy stores	ice cream	travel
carpet cleaning	laundry	vending machines

The popularity of franchise systems derives from their being able to offer consistent quality at a convenient location at a reasonable price.

Advantages Franchising has advantages to the franchiser and the franchisee. For the franchiser, the benefits include a ready source of funds for expansion coupled with the ability to establish policies for operating each franchise. For franchisees, the advantages include greater name recognition, participation in advertising programs, better prices from suppliers, and business advice.

Because of such advantages, owners of existing independent businesses are often interested in operating as a franchisee. To become a franchisee and get these advantages, an independent business undergoes a process called franchise conversion. This involves entering into a franchise agreement and changing over to the franchise's name and operating formula.

Drawbacks Of course, franchising arrangements do not always work out. From the franchiser's standpoint, it can sometimes be hard to find enough qualified franchisees. Also, the activities of franchisees are harder to control than those of employees. For the franchisee, this type of arrangement can be frustrating when the franchiser does not provide adequate support such as effective advertising or seems to lack understanding of the franchisee's local market.

The critical question, though, is how can a manufacturer convince independent middlemen to participate in and accurately carry out detailed merchandising plans when the firm neither owns nor enjoys contractual agreements with them? The answer is that successful channel administrators draw on their power within the system to induce cooperation from its other members.

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[12] Breton R. Schenlender, "Working on the Chain Gang," *The Wall Street Journal*, May 19, 1986, p. 140.

V. SOURCES OF CHANNEL POWER[13]

Firm A has *power* over firm B to the extent that A can get B to do something that B would not do if left to its own devices.[14] The extent of firm A's power over B is inversely proportional to firm B's dependence on A to attain desired rewards or avoid unwanted consequences. **Sources** (or **bases**) **of power** within channel relationships include the following:

- **Economic power** exists when channel members perceive that a firm can mediate economic rewards for them if they follow its directives. Most often, those rewards take the form of increased sales and profits. Thus, the producer of a brand with the largest share or the most prestige in its product category can often gain the cooperation of distributors or retailers who believe that their efforts can behalf of the brand are likely to be rewarded with handsome sales and profits. Even producers of new or less-dominant brands can exercise economic power by offering additional rewards to other channel members, such as large margins, promotional allowances, or introductory discounts. Nabisco ensured adequate shelf space for its Almost Home soft cookies, for example, by offering an additional 10 percent discount on any Nabisco product to every retailer that agreed to devote four feet of space to the new line.
- **Coercive power** is based on a perception that one channel member will punish another for failure to cooperate. It is the inverse of economic power, since such punishments usually take the form of a reduction in or withholding of economic rewards. For example, a manufacturer might threaten to withdraw a retailer's exclusive territorial rights or its promotional allowances if the retailer's performance does not meet expectations. Coercive power should be used sparingly, though. Frequent threats of punishment often lead to conflict, resentment, and dissatisfaction among other channel members.[15]
- **Expert power** stems from a perception that one channel member has special knowledge or expertise that can benefit other members of the system. Because of the reputations of firms like Unilever and Procter & Gamble as marketers, middlemen are often willing to abide by their merchandising suggestions. The assumption is that their programs are more likely to lead to sales success than anything the middlemen could come up with on their own. However, the recent proliferation of scanners in retail stores has increased the expert power of retailers. They now have more detailed and up-to-date information about local sales of individual brands and the effectiveness of specific promotions than the manufacturers have.[16]
- **Referent power** is based on perceptions of the benefits and satisfactions that have been generated - and are likely to continue to be generated - from a long-term

[13] Based on Harper W. Boyd, jr. and Orville C. Walker, jr., *Marketing management: A Strategic Approach,* Irwin, 1990

[14] John F. Gaski, "The Theory of Power and Conflict in Channels of Distribution," Journal of Marketing, Summer 1984, pp. 9-29.

[15] Gary L. Frazier and John O. Summers, "Interfirm Influence Strategies and Their Application within Distribution Channels, "*Journal of Marketing*, Summer 1984, pp. 43-55.

[16] Thayer C. Taylor, *The Great Scanner Face-Off*, "Sales and Marketing Management, September 1986, pp. 43-46

relationship with a channel member. A member that has received good service and earned substantial profits from a relationship with a manufacturer over the years may be willing to accede to its suggestions or requests, without demanding any additional rewards, simply to preserve the relationship into the future.
- **Legitimate power** flows from the perception that one channel member has the right to make certain decisions or demands and to expect compliance from other members. Legitimate power is usually the result of ownership or contractual agreements. But in some instances it is based on "moral authority" or common beliefs about what is right and proper. For example, most middlemen would agree that a food manufacturer has the right to print expiration dates on its packages and to expect middlemen to pull out-dated packages off the shelves as a means of protecting the product's quality and the consumer's health.

VI. SELECTING AND MANAGING A MARKETING CHANNEL[17]

In this section we will examine several channel-decision problems facing a marketer in designing and managing his channel. The problem with designing a marketing channel is that the marketer has to struggle between what he considers as an ideal channel, what is feasible, and what is available. Defining the best channel is not the problem, but finding the appropriate and available intermediaries and motivating them in handling the product correctly is of another dimension. Managing a marketing channel means that the marketer must constantly adjust his distribution policy to the changing market. In addition, he has to motivate and evaluate the participants in his marketing channel in order to realize the desired *service output levels*.
According to Kotler (1994) designing a marketing channel system calls for analyzing customer needs, establishing channel objectives, identifying the major channel alternatives, and evaluating them. The management process deals with relationship management. In this section we successively will pay attention to all these aspects.

VI.1. The desired service output

The leading issue in building a marketing channel is the service output desired by the target customer groups. Bucklin (1972)[18] makes a distinction between five service outputs a channel can produce:

- *Lot Size*: The lot size is the number of units that the marketing channel permits a typical customer to buy on a buying occasion. In buying cars for its fleet, Hertz prefers a channel from which it can buy a large lot size; and a household wants a channel that would permit buying a lot size of one. Obviously different channels

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[17] Based on Philip Kotler (1994), *Marketing Management, Analysis, Planning, Implementation, and Control,* eighth edition, Englewood Cliffs, NJ: Prentice Hall
[18] see Philip Kotler (1994), *Marketing Management, Analysis, Planning, Implementation, and Control,* eighth edition, Englewood Cliffs, NJ: Prentice Hall, page 531

must be set up for fleet car buyers and household buyers. The smaller the lot size, the greater the service output level that the channel must provide.

- *Waiting Time*: Waiting time is the average time that customers of that channel wait for receipt of the goods. Customers normally prefer fast delivery channels. Faster service requires a greater service output level.
- *Spatial Convenience*: Spatial convenience expresses the degree to which the marketing channel makes it easy for customers to purchase the product. VW, for example, offers greater spatial convenience than Porsche, in that there are a much greater number of VW dealers. VW's greater market decentralization helps customers save on transportation and search costs in buying and repairing an automobile. Spatial convenience is being further augmented by the use of direct marketing.
- *Product Variety*: Product variety represents the assortment breadth provided by the marketing channel. Normally customers prefer greater assortment breadth because it increases the chance of exactly meeting their need. Thus car buyers would rather buy from a dealership carrying multiple manufacturer brands than only one manufacturer's brand.
- *Service Backup*: Service backup represents the add-on services (credit, delivery, installation, repairs) provided by the channel. The greater the service backup, the greater the work provided by the channel.

The marketer should select channels that meet the desired service output of the target customer groups. In addition he has to pay attention to the number of customers (households), the geographical dispersion and the purchasing patterns of the target consumer groups.

VI.2. Channel objectives and constraints

The target service output levels should be the starting point for the channel objectives. According to Bucklin (1972), under competitive conditions, channel institutions should arrange their functional tasks so as to minimize total channel costs with respect to desired levels of service outputs. Usually, several segments can be identified that desire differing service output levels. Effective channel planning requires determining which market segments to serve and the best channels to use in each case. Each producer develops its channel objectives in the face of several constraints.

As with all elements in the marketing-mix, the distribution objectives should match the overall company marketing objectives. As far as distribution is concerned two major issues are at hand: which marketing channel will be the most *efficient* and which will generate the desired *market share*.

The most efficient marketing channel is that channel that yields the highest sales against the lowest costs. Sales, and of course market share, depends largely on the marketing efforts of the intermediaries and their market coverage. The costs of distribution are caused by the physical distribution costs and the marketing costs. Examples of physical distribution costs are:[19]

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[19] J.Paul Peter and James Donnely, jr. (1991) *A Preface to Marketing Management*, 5th edition Irwin 1991 page 182

- transporting costs;
- order processing costs;
- lost order costs when the organization is unable to meet demand;
- costs of carrying inventory;
- packaging costs for shipment of the product;
- materials handling costs.

The marketing costs consist of the costs made to build up and sustain the relation with the intermediaries. One could think of selling costs, reduction of margins, information costs, costs of advice and training, etcetera.

To measure the efficiency of a particular channel, the marketer must be able to monitor these costs.

Channel objectives vary with the characteristics of the product itself. Marketers need to ask what kind of marketing channel is most suitable for the type of product. Sometimes certain product characteristics override other factors in the selection process of marketing channels. In the case of highly *persishable* products such as flowers or meat, the selected channel has to be as short as possible. The same goes for *high value/low volume* products like jewellery. The risk of losses and theft is to high for distributing them by using a long channel.with these products. On the other hand, *bulky* products and products with a high level of *standardization* can be distributed most efficiently by a long channel with highly specialized intermediaries. By doing so logistic costs can be minimized. *Life cycle stage* is also important. Notably new products may need established intermediaries to give them credibility, while products in the maturaty stage can be sold with a high market coverage. The desired image of the product and customer's actual perceptions also are related to the channel selection. Making a product available only through a limited number of highly sophisticated retailers has a high quality impact. This is why Bally of Switzerland only sells his shoes through their own retail outlets or through the outlets of retailers at the high end of the market.

The selection process of the *intermediaries* is often influenced by the assortment strategies of the intermediaries. Before designing a detailed distribution strategy, one should first look whether the necessary intermediaries are available and are willing and able to carry the product. If so, the marketer needs to evaluate the potential intermediaries. Some background information worth to acquire includes the intermediaries sales, profits, liability, clientele, and assortment policy. In many cases the producers don't have very much choice while selecting their marketing channels. They have to live with existing market channel structures and have to make the best of it.

Finally, producers making decisions about distribution channels must consider forces in the total marketing environment - that is, such issues as competition, ecology, economic conditions, technology, society and law. Technology, for example, has made possible electronic scanners, computerised inventory systems such as EPOS (electronic point of sale) and electronic shopping devices, all of which are altering present distribution systems and making it harder for technologically unsophisticated firms to remain competitive. Changing family patterns and the emergence of important minority consumer groups are driving producers to seek new distribution methods for reaching market segments, and sometimes this search results in non-traditional approaches which increase competitive pressures. Interest rates, inflation and other economic variables affect members of distribution channels

at every level. Environmental forces are numerous and complex and must be taken into account if distribution efforts are to be appropriate, efficient and effective.

VI.3. Identifying the major alternatives

After defining the target market and the desired positioning, the marketer should identify the channel alternatives. Alternatives can be described by three elements: *the type of business intermediaries,* the *intensity of market coverage,* and the *terms and responsibilities of the intermediaries.*
The **type of business intermediaries** depends largely on the channel objectives and constraints. There are many different types of intermediaries, ranging from the companies own sales force, agents, full service wholesalers, limited service wholesalers, logistic partners, to service and price retailers. For example: a unique form of full service wholesaling that has enyoed relatively rapid growth in recent years is *rack jobbing* or *service merchandising.* To offer greater shopping convenience to their customers and to increase their own profit margins, many retailers - such as supermarkets and drugstores - have added non-traditional product lines, such as magazines, housewares, and health and beauty aids to their stores. Because those retailers know little about merchandising those products, rack jobbers or service merchandisers have prospered by not only performing a full range of wholesaling activities but also by taking over some of the retailer functions as well. They often provide display racks and promotional materials for the retailer's store, stock the racks on a regular basis, and sell on consignment (which means that they retain title of the merchandise and bill the retailer only for the goods actually sold)[20]. A producer of housewares could decide to integrate forward and set up his own rack jobbing system, or he could find a rack jobber to distribute his products. An over-view of the most important middlemen is given in figure 8.

[20] Harper W. Boyd & Orville C. Walker, (1990), *Marketing Management, a Strategic Approach,* Irwin, page 503

Figure 8: Middlemen types

Institution	Definition
Merchant wholesalers	Take title to the goods they handle sell primarily to other *resellers* (e.g., retailers), *industrial and commercial customers* rather than to individual consumers.
Agent middlemen	Include manufacturers' representatives and brokers. Also sell to other *resellers, industrial or commercial customers*; but *do not take title* to the goods. Usually specialize in the selling function and represent client manufacturers on a commission basis.
Retailers	Sell goods and services directly to *ultimate consumers* for their personal, nonbusiness use. Usually *take title* to goods they handle; are compensated by the margin between the price they pay for those goods and the price they receive from their customers.
Facilitating agencies	Include advertising agencies, marketing research firms, collection agencies, trucking firms, and railroads; *specialize in one or more marketing functions; work on a fee-for-service basis* to help clients perform those functions more effectively and efficiently.

VI.4. The intensity of market coverage

The **intensity of market coverage**, that is, the number and kinds of outlets in which a product or service should be offered, depends largely on the behaviour patterns of the buyers. In general we can make a distinction between convenience, shopping and specialty goods. This classification is based on consumer behaviour. While customer buying efforts differ among these categories, the availability of the goods or services has to be different to. In considering products for purchase, take into account the replacement rate, product adjustments (service), duration of consumption, time required to find the product and similar factors[21]. These variables directly affect the intensity of market coverage. Three strategies are available: intensive, selective and exclusive distribution.

VI.4.1. Intensive distribution.

In intensive distribution a manufacturer chooses as many distribution outlets as possible. This is an approach that supports a mass marketing strategy. It is especially suitable for products that have a low cost per unit and are purchased frequently. Convenience goods like chewing gum, newspapers, beer, chocolate, gasoline,

[21] Leo Aspinwall, *The Marketing Characteristics of Goods*, in "Four Marketing Theories", Boulder: University of Colorado Press, 1961, pp. 27-32

tobacco products are distributed this way. Intensive distribution means a high degree of availability. To the consumers this means a store located nearby and minimum time necessary to search for the product at the store. Sales may have a direct relationship to availability.

VI.4.2. Selective distribution.

Another distribution strategy is selective distribution, in which a manufacturer chooses only a limited number of outlets to distribute his products. The selection of the outlet is based on certain quality aspects like the location, and the level of services offered by the retailer. The manufacturer chooses those retailers that support his products best. Due to the limited number of retailers selling the manufacturers product line, there will be less price competition. Moreover, the firm can reduce its total marketing costs, while establishing better working relationships within the channel. *Cooperative Advertising* (in which the manufacturer and the retailer develop and pay a joint advertising campaign) can be utilized for mutual benefit, and marginal retailers can be avoided.
Selective distribution is desirable when a special effort - such as customer service from a channel member - is important. Shopping goods require differentiation at the point of purchase. To motivate retailers to provide adequate pre-sale service, selective distribution and company owned stores are often used. Many industrial products are sold on a selective basis to maintain a certain degree of control over the distribution process.
VW Germany is an example of this approach. VW rates its dealers on the basis of customer satisfaction. It knows when a dealer scores 85 out of 100, on average, 96 percent of German customers will come back to that dealership for a new car. VW also segments its dealers on the basis of their rankings. The segments are then used in the dealer promotions program[22].

VI.4.3. Exclusive Distribution.

Exclusive distribution is the use of a single retailer or wholesaler to serve a large geographical area. The wholesaler or retailer gains exclusive rights to sell the manufacturers product (line) in his market area. It is to be considered as an extreme form of selective distribution. Exclusive distribution is used when the manufacturer wants to have a great deal of control over the service level and the service outputs offered by the resellers. Often it involves *exclusive dealing* where the resellers are not allowed to carry competing brands. Producers of high-priced shopping goods, specialty goods and accessory equipment often require such agreements as assurance by the marketing intermediary of total concentration on the firm's product line. Exclusive distribution requires greater partnership between seller and reseller. Through granting exclusive distribution, the producer hopes to obtain more

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[22] Wolfang Muller (1991), *European Firms Set Management Principles for Customer Satisfaction*, in "Marketing News", February 4 page 6

aggressive and knowledgeable selling. Exclusive distribution normally has a positive effect on the product's image and allow higher margins for the producers and the resellers.

Concerning the market coverage we see a tendency of moving from exclusive or selective distribution to more intensive distribution. In the short run this has the advantage of higher sales, but in the long run it damages the firm's market position[23]. Figure 9 gives an overview of the strengths and weaknesses of the three different strategies for market coverage.

Figure 9: strengths and weaknesses of different forms of market coverage.

	Retail coverage	**Major strength**	**Major weakness**	**Products most appropriate for**
Intensive	Maximum	Maximizes product availability	Lack of retailer support	Low-involvement consumer convenience goods
Exclusive	Single	Matches retailer clientele with target market; facilitates close cooperation with retailer	Risk of relying on single retailer	High-involvement speciality or shopping goods
Selective	Limited	Provides adequate coverage but not at expense of manufacturer-retailer cooperation	Difficult to implement given interstore competition, especially where discounts may occur	Infrequently purchased shopping goods

VI.6. Conditions and responsibilities

The next step in the channel management process is to determine the conditions and responsibilities of the intermediaries. The main elements to be discussed within the "channel relation mix" are *pricing policies, conditions of sale, territorial rights,* and *specific services to be performed by each party.*

Price policy calls for the producer to establish a price list and schedule of discounts. The middlemen must see these as equitable and sufficient.

Conditions of scale refer to payment terms and producer guarantees. Most

[23] see Philip Kotler (1994), *Marketing Management, Analysis, Planning, Implementation, and Control,* eighth edition, Englewood Cliffs, NJ: Prentice Hall, page 534

producers grant cash discounts to their distributors for early payment. Producers might also guarantee distributors against defective merchandise or price declines. A guarantee against price declines induces distributors to buy larger quantities.

Distributors' territorial rights are another element in the trade-relations mix. Distributors want to know where the producer will enfranchise other distributors. They would also like to receive full credit for all sales taking place in their territory, whether or not they did the selling.

Mutual services and responsibilities must be carefully spelled out, especially in franchised and exclusive-agency channels. For example, McDonald's provides franchisees with a building, promotional support, a record-keeping system, training, and general administrative and technical assistance. In turn, franchisees are expected to satisfy company standards regarding physical facilities, cooperate with new promotional programs, furnish requested information, and buy specified food products.

VI.7. Evaluation of the major alternatives

Before choosing a specific marketing channel a producer has to know which channel is most suitable for reaching his marketing objectives. The evaluation of the different channel alternatives can take place on the basis of three important evaluation criteria, namely: *profits, control,* and *adaptive criteria.*
Profits are generated by sales and costs. In order to find the most profitable marketing channel the producer must compare the different alternatives on their sales potential and the costs of these sales. In addition the producer has to evaluate the possibilities for an adequate control mechanism. Using intermediaries poses a control problem. Indeed, every middleman seeks to realize his own objectives. The question is whether the producer will be able to control the efforts the middleman gives to his product in order to guarantee an adequate qualitative an quantitative distribution. A adequate control mechanism gives the producer an opportunity to formulate and execute a profitable distribution policy. The third evaluation criteria deals with the degrees of freedom the producer has in order to adapt his distribution policy to changing market conditions. Once a distribution channel is chosen channel members reached some degree of commitment for a certain period of time. This automaticly deminshes the possibility of the producer to adapt his distribution channel to changing market conditions. In situations of rapidly changing, uncertain product markets this criteria becomes more and more important.

VII. MANAGING THE CHANNEL RELATIONSHIPS: COOPERATION, CONFLICT, AND LEADERSHIP

Once a distribution channel is chosen, the participants have to cooperate in order to realize the desired service output levels. Each channel member performs a different

role in the distribution system and agrees (implicitly or explicitly) to accept certain rights, responsibilities, rewards and sanctions for non-conformity. Moreover, each channel member expects certain things of every other channel member. Retailers, for instance, expect wholesalers to maintain adequate inventories and to deliver goods on time. For their part, wholesalers expect retailers to honour payment agreements and to keep them informed of inventory needs. It must be remembered that often channel members are companies in their own right, with profit goals, cash flow needs, shareholders and their own marketing strategies and programmes. This section discusses several issues related to channel member behaviour, including co-operation, conflict and leadership. Marketers need to understand these behavioral issues to make effective channel decisions.
Channel cooperation is vital if each member is to gain something from other members[24]. Mutual trust can be considered as an important basis for cooperation. For example, when channel members agree on serving a common target market by providing high quality goods and services, their quality focus can be a basis for cooperation. The channel members can do more than simply conduct transactions; they can forge long-term relationships, perhaps even partnerships or strategic alliances[25]. In fact, the marketing channel can be seen as an unified system, competing with other systems[26]. This way, opportunistic behaviour of individual members in seeking their own advantages can be minimized and controlled. Producers can strengthen the inter channel relationships by learning the needs of their intermediary customers as well as the end users of their products. The aim of the distribution policy of the producer is to satisfy the needs of the end users as well as the intermediaries. The distribution policy formulated on behalf of the intermediaries is called *account management.*
As indicated above, channel members work towards the same goal, but perform different tasks within the marketing channel. This results in a certain degree of inter-dependence. In a channel relation, each member becomes dependent on the other members to reach his organizational objectives. The greater the level of interde-pendence, the greater the chance for conflict situations. Conflicts arise when for example a channel member doesn't perform his channel tasks properly. Retailers expect producers to monitor quality control, to support the product on a national basis, and to produce and deliver on time, while producers expect retailers to market the product effectively on a local basis. These types of conflicts are called *vertical conflicts.*
Horizontal conflicts also may occur among channel members. This type of conflict involve channel members at the same level, such as two or more wholesalers or two or more retailers. Horizontal conflicts arise because different marketing intermediaries handle the same product. They may occur when an intermediary seeks to gain sales at the expense of others. They also may arise when an intermediary believes that its objectives are hurt by other channel members carrying the same product.
Taken together, conflicts among channel members can occur for several reasons:

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[24] Wroe Alderson, (1965), *Dynamic Marketing Behavior,* Irwin, page 239
[25] See Frederick E. Webster jr. (1992), *The Changing Role of Marketing in the Corporation*, "Journal of Marketing" (Oktober): p. 1-17
[26] Reijnders Will J.M. and Theo M.M. Verhallen, *Commercial Cooperation in the Distribution*, in Análisa Psicológica, 1 (XII) pp. 56-75

Disagreements among channel members can occur for several reasons:

- *Incompatible goals*. Each channel member is interested in maximizing its own share of the total profits generated by the system. Consequently, manufacturers and middlemen frequently disagree over the size of margins and incentives offered at each channel level and over which members should bear the cost of performing specific functions such as inventory storage. Conflicts can also arise because the manufacturer is concerned with increasing the market share of its brand while its dealers want to offer an assortment of competing brands to satisfy a range of customers.
- *Unclear rights and responsibilities*. Sometimes a manufacturer's marketing policies are unclear to its middlemen. Or, they may seem to be incompatible with the traditional activities and expectations of those middlemen. For example, IBM uses its own company salesforce to sell personal computers to large business accounts. But its licensed retail dealers also call on such accounts. This has caused confusion and conflict about who should be calling on whom and who should get credit for major sales, as well as a good deal of duplication of effort within the channel.
- *Misperceptions and poor communication*. Sometimes conflicts arise when there are no substantive reasons for them to occur. This is because members at different channel levels can interpret events in very different ways. When Toro began selling direct to mass merchandisers, for instance, its distributors concluded that it was a first step toward the total elimination of the wholesale level in Toro's distribution channel. Even though Toro never intended to bypass its distributors, it took years of effort - and a major change in policy - to win back their support.

Because channel conflict is inevitable, the challenge is not to eliminate it but to minimize it and mange it better. Firms have pursued several approaches aimed at recognizing and resolving potential conflicts early before they cause a breakdown of cooperation within the system[27].

- *Involve channel members in policy decisions*. Some companies have formed dealer advisory boards or survey a sample of middlemen on a regular basis to gauge their reactions to company policies and programs. Du Pont, for instance, has a Distributor Marketing Steering Committee that meets regularly to discuss problems and trends. And Parker Hannifin sends out an annual mail survey asking distributors to rate the company's performance on key dimensions.
- *Increase interaction among personnel at all levels*. Increased contacts among the employees of a manufacturer and its middlemen can lead to an improved understanding of each party's problems and objectives and to more accurate and open communications. Thus, Square D - a manufacturer of electrical equipment - has its salespeople spend a day "working the counter" with each of its distributors to better understand the distributor's business. Dayco Corporation runs an annual week-long retreat where 20 distributor executives.
- *Focus on common goals*. When channel members can be persuaded to focus on a common purpose or a common external threat, such as foreign competition, they

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[27] see James A Narus and James C Anderson, (1986), *Turn Your Industrial Distributors into Partners* in Harvard Business Review, March-April, pp. 66-71

may be more willing to compromise their individual concerns for the good of the system. When Lee Iacocca became president of Chrysler, for instance, he gained dealer cooperation by stressing the common objective of survival in the face of threatening competitive and financial circumstances.
- *Mediation and arbitration*. Sometimes the use of outside administrative mechanisms such as third parties to mediate or arbitrate disputes is an effective method or resolving conflict. Successful action here rests on clarifying the issues, examining alternative solutions, keeping the parties in contact with each other, and encouraging agreement to certain proposals.

The effectiveness of a marketing channel depends on **channel leadership**. Producers, wholesalers, or retailers can perform the leadership role. In general the channel leader is the most powerful channel member. The channel leader takes responsibility for the channel policy and the coordination of the different functions within the channel. By using his power, in the form of the five powerbases as discussed earlier in this chapter, he manages the different participants in the channel. Conflict resolution within the channel can be considered as one of the main tasks of the channel leader.

VIII. SUMMARY

A marketing channel is the set of interdepending organizations involved in the process of making a product or service available for consumption or use by consumers or industrial users. Usually a number of specialized institutions are involved in a distribution channel because such specialization and division of labour increase the functional, scale, and transactional efficiencies of the performance of necessary marketing functions.

Among the types of institutions a manufacturer might include in the distribution channel are (1) merchant wholesalers who take title to the product and sell to other resellers, institutions, or industrial customers; (2) agent middlemen who also operate at the wholesale level but are paid by commission rather than taking ownership of the goods; (3) retailers who take title and sell to consumers; and (4) facilitating agencies - such as advertising agencies and trucking firms - that are employed on an as needed basis and paid fees for their specialized services. Firms can organize one or more of these institutions into a channel for a specific product or service in a variety of ways. It is becoming increasingly common for manufacturers to use multiple channel structures for distributing a single product in order to reach distinct target segments of customers.

Managing the distribution of a product or service requires a manufacturer to make two interrelated sets of decisions: those concerning channel design and those involving the management of the various institutions included within the channel. Major channel design decisions include (1) specifying the manufacturer's objectives for its distribution system; (2) determing the appropriate number of retail outlets; (3) deciding on physical distribution; and (4) choosing specific types of institutions for each level in the channel.

Channel management decisions are primarily concerned with improving the manufacturer's control and coordination of channel members' activities. To

accomplish that purpose, some manufacturers (and a few large wholesalers and retailers) have vertically integrated to form *corporate vertical marketing systems* in which they have the formal authority to coordinate activities at various levels. Such systems are particularly common when the product is complex, specialized knowledge or facilities are required to sell or service the product, and few independent middlemen capable of performing the necessary activities are available.

Other firms have improved their control and coordination of channel activities by forming contractual vertical marketing systems, in which independent firms at various levels agree to legal contracts that spell out each party's rights and duties within the system. Marketers categorize such contractual systems into three basic types: wholesaler-sponsored voluntary chains, retailer cooperatives, and franchise systems.

Finally, through informal guidance and influence, one of the parties coordinates administered vertical marketing systems. The channel administrator - who is usually a manufacturer but may be a large wholesaler or retailer - relies on its power within the system to motivate cooperation from the other members. Manufacturers attempt to improve their economic power to administer the distribution channel through: (1) a pull strategy in which consumer advertising and promotion efforts build selective demand for the product, and resellers are motivated by the promise of future sales and profits; or (2) a push strategy in which direct incentives - such as quantity discounts and cooperative and cooperative advertising programs - are offered to induce cooperation from channel members.

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