Basic Marketing

14/e

A Global-Managerial Approach

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Preface

Basic Marketing Is Designed to Satisfy Your Needs

This book is about marketing and marketing strategy planning. And, at its essence, marketing strategy planning is about figuring out how to do a superior job of satisfying customers. We take that point of view seriously and believe in practicing what we preach. So you can trust that this new edition of *Basic Marketing*—and all of the other teaching and learning materials that accompany it—will satisfy *your* needs. We're excited about this edition of *Basic Marketing*, and we hope that you will be as well.

In developing this edition we've made hundreds of big and small additions, changes, and improvements in the text and all of the supporting materials that accompany it. We'll highlight some of those changes in this preface, but first it's useful to put this newest edition in a longer-term perspective.

Building on Pioneering Strengths

Basic Marketing pioneered an innovative structure—using the "four Ps" with a managerial approach—for the introductory marketing course. It quickly became one of the most widely used business textbooks ever published because it organized the best ideas about marketing so that readers could both understand and apply them. The unifying focus of these ideas was on how to make the marketing decisions that a manager must make in deciding what customers to focus on and how best to meet their needs.

Over many editions of *Basic Marketing* there has been constant change in marketing management and the marketing environment. Some of the changes have been dramatic, and others have been subtle. As a result, we have made ongoing changes to the text to reflect marketing's best practices and ideas. Throughout all of these changes, *Basic Marketing* and the supporting materials that accompany it have been more widely used than any other teaching materials for introductory marketing. It is gratifying that the four Ps has proved to be an organizing structure that has worked well for millions of students and teachers.

Continuous Innovation and Improvement

The success of *Basic Marketing* is not the result of a single strength—or one long-lasting innovation. Rather, the text's four Ps framework, managerial orientation, and strategy planning focus have proved to be foundation pillars that are remarkably robust for supporting new developments in the field and innovations in the text and package. Thus, with each new edition of *Basic Marketing* we have continued to innovate to better meet the needs of students and faculty. In fact, we have made ongoing changes in how we develop the logic of the four Ps and the marketing strategy planning process. As always, though, our objective is to provide a flexible, high-quality text and choices from comprehensive and reliable support materials—so that instructors and students can accomplish their learning objectives. For example, included with the other innovations for this new edition are

- Integrated coverage, throughout the text, of the significant impacts that e-commerce, the Internet, and related information technologies are having on marketing.
- A complete revision of the *Student CD-ROM to Accompany Basic Marketing* that comes with the text, with a new interface that integrates the rich variety of multimedia learning resources it includes.
- A completely new and expanded archive of PowerPoint electronic lecture-support slides, with links to full-motion videos, ads, and photos, to provide instructors with flexible support for lectures and presentations.
- The *Instructor CD-ROM to Accompany Basic Marketing* that provides Windows software and all of the text's teaching support materials in easy-to-use electronic form.
- A sharper focus, throughout the text, on how the strategy planning process should lead to decisions about a target market and marketing mix that represents the best opportunity and competitive advantage for the firm and superior value for consumers.
- Interesting new video cases and teaching videos focused on current marketing issues.
- High-involvement Internet exercises integrated throughout each chapter of the text.

We Believe in Continuous Quality Improvement

McCarthy pioneered *Basic Marketing* and worked on the text without a coauthor for seven editions. Twenty years ago Perreault joined the team. We formed our partnership with a shared commitment to ongoing improvements, and we're both proud that we were implementing continuous quality improvements in preparing *Basic Marketing* long before the idea became popular in the world of business. We work to be creative in our coverage and approaches—because creativity is at the heart of the marketing spirit. The most creative teaching innovations are ones that meet students' needs and instructors' objectives. That's also why our first priority has always been, and always will be, producing quality materials that really work well for students and teachers. Students take the first marketing course only once. It is an investment and opportunity from which there should be a solid return. So we take it as a serious personal responsibility to support that investment with materials that are interesting and motivating—and that really build the skills and ideas that students need in their lives and careers.

Our belief that attention to continuous quality improvement in every aspect of the text and support materials *does make a difference* is consistently reaffirmed by the enthusiastic response of students and teachers alike to each new edition.

Leading Technology Innovations for Teaching and Learning

It has always been our belief that it is our responsibility to lead the marketing discipline in developing new, breakthrough approaches for teaching and learning in the first marketing course. Our constant thrust has been to use technology to provide better and easier options for teaching and richer and more interesting approaches for learning. Along with other innovations, we were the first to develop and offer spreadsheet-based computer-aided problems, custom-produced videos, a computerized test bank, a PC-based marketing simulation, a hypertext reference, bar-coded laser disks, CD-ROM–based interactive versions of the text, PowerPoint presentation slides with linking by objectives, CD-ROM multimedia archives and presentation software for instructors, multimedia case support, and the multimedia CD for students. Now we continue these traditions of innovation with a completely redesigned *Student CD-ROM to Accompany Basic Marketing*, *myPowerWeb* online readings, and a host of new and improved teaching and learning materials available at the *Basic Marketing* website at www.mhhe.com/fourps.

Critically Revised, Updated, and Rewritten

This new edition of *Basic Marketing* is the highest-quality teaching and learning resource ever published for the introductory marketing course. The whole text and all of the supporting materials have been critically revised, updated, and rewritten. As in past editions, clear and interesting communication has been a priority. *Basic Marketing* is designed to make it easy, interesting, and fast for students to grasp the key concepts of marketing. Careful explanations provide a crisp focus on the important "basics" of marketing strategy planning. At the same time, we have thoroughly

- Researched and incorporated new concepts.
- Integrated hundreds of new examples that bring the concepts alive.
- Illustrated marketing ideas and "best practices" in a rich variety of contexts.

We have deliberately used marketing examples from a host of different contexts. Examples span organizations that have moved to e-commerce and those that have found other ways to innovate, profit and nonprofit organizations, large and small firms, domestic and international settings, purchases by organizations as well as by final consumers, services and ideas or "causes" as well as physical goods, and established products as well as new technologies—because this variety reinforces the point that effective marketing is critical to all organizations.

Clear Focus on Changes in Today's Dynamic Markets

This edition focuses special attention on changes taking place in today's dynamic markets. Throughout every chapter of the text we have integrated discussion and examples of

- Best practices in marketing, and how to avoid the mistakes of death-wish marketing (including errors and omissions all too common among many failed dot-com operators).
- Effective e-commerce innovations and changes in marketing over the Internet.
- The costs and benefits of different approaches for customer acquisition and retention.
- Relationship building in marketing.
- The importance of providing superior customer value as the means to achieve customer satisfaction and competitive advantage.
- International perspectives.
- Ethical issues.

Similarly, we've also integrated new material on many important and fast-evolving topics. The following are but a sampling:

- Integrated marketing communications, direct-response promotion, and customer-initiated interactive marketing communications.

- Promotional campaigns that build "buzz" among consumers.
- The Euro, the World Trade Organization, exchange rates, and other topics central to international markets.
- The growth of business-to-business (B2B) exchanges on the Web and the expanding use of reverse auctions and interactive bidding.
- The circumstances when using a website for direct distribution or dual distribution makes sense and when it doesn't.
- The expanding role of sales technologies and self-service technology.
- The increasing channel power of large retail chains.
- Competitor analysis and how to develop competitive advantage.
- How to use flexible pricing and evaluate price sensitivity.
- Marketing control, including marketing cost analysis.

Driving Home Competitive Advantage

Throughout the 14th edition we've continued to put more emphasis on the *process* of marketing strategy planning. In today's dynamic markets it's not enough to simply figure out an attractive opportunity and an effective marketing mix. The real challenge is to quickly but logically zero in on the target market and marketing mix that is really best for the firm, while recognizing that strategies need to be refined and improved as market conditions change. This highlights the need for breakthrough opportunities, the problems with me-too imitation, and the crucial role of competitive advantage in providing customers with superior value. In other words, we sharpen the focus on how to figure out the best blend of the four Ps and crush the mistaken view fostered by some texts that the marketing job is just coming up with *some* marketing mix.

Coupled with this, you'll learn how breakthroughs in information technology are driving changes in all aspects of marketing—whether it's e-commerce ordering, getting marketing information, preparing salespeople to interact with customers, or analyzing the "fire-hydrant" flow of data on sales and costs. We'll also highlight the many ways that relationships among marketing partners are changing—ranging from coordination of logistics to alliances among firms focused on the same market opportunity. You'll see how intense competition, both in the United States and around the world, is affecting marketing strategy planning. You'll see what it takes to transform an effective new-product development process into profitable business.

Some other marketing texts are attempting to describe such changes. But that's not adequate. What sets *Basic Marketing* apart is that the explanations and examples equip students to see *why* these changes are taking place and what changes to expect in the future. That is an important distinction—because marketing is dynamic. Our objective is to prepare students to analyze marketing situations and develop exceptional marketing strategies—not just recite endless sets of lists.

A Fresh Design—to Make Important Concepts Even Clearer

Along with the new content, we've given the text a fresh design. The changes range from the new cover to hundreds of new photographs, ads, web pages, and illustrations. We've created many new exhibits—conceptual organizers, charts, and tables—and updated proven pieces from past editions, all with a fresh new design.

The aim of all this revising, refining, editing, and illustrating is to make important concepts and points even clearer to students. We want to make sure that each student really does get a good feel for a market-directed system and how he or she can help it—and some company—run better. We believe marketing is important and interesting—and we want every student who reads *Basic Marketing* to share our enthusiasm.

Twenty-Two Chapters—with an Emphasis on Marketing Strategy Planning

The emphasis of *Basic Marketing* is on marketing strategy planning. Twenty-two chapters introduce the important concepts in marketing management and help the student see marketing through the eyes of the marketing manager. The organization of the chapters and topics is carefully planned. But we took special care in writing so that

- It is possible to rearrange and use the chapters in many different sequences—to fit different needs.
- All of the topics and chapters fit together into a clear, overall framework for the marketing strategy planning process.

Broadly speaking, the chapters fall into two groupings. The first eight chapters introduce marketing and a broad view of the marketing strategy planning process. They cover topics such as segmentation, differentiation, the marketing environment, and buyer behavior, as well as how marketing information systems and research provide information about these forces to improve marketing decisions. The second half of the text goes into the details of planning the four Ps, with specific attention to the key strategy decisions in each area. Then we conclude with an integrative review and coverage of overarching topics such as implementation and control, marketing's link with other functional areas, and an assessment of marketing's challenges and opportunities.

The first two chapters deal with the nature of marketing—focusing both on its macro role in a global society and its micro role in businesses and other organizations. The first chapter stresses that the effectiveness of our macro-marketing system depends on the decisions of many producers and consumers. That sets the stage for the second chapter—and the rest of the book—which focuses on how businesspeople and, in particular, marketing managers develop marketing strategies to satisfy specific target markets. This chapter introduces the marketing concept and develops the customer value and four Ps frameworks.

Chapter 3 introduces an integrative model of the marketing strategy planning process that serves as an organizing framework for the whole text. Chapter 3 sets the stage by overviewing how analysis of the market and external market environment relate to segmentation and differentiation decisions as well as the criteria for narrowing down to a specific target market and marketing mix. Broadly speaking, it introduces a strategic planning view of how a manager leads his or her firm to new market opportunities and competitive advantage.

This strategic view alerts students to the importance of evaluating opportunities in the external environments affecting marketing—and these are discussed in Chapter 4. This chapter also highlights the critical role of screening criteria for narrowing down from possible opportunities to those that the firm will pursue.

The next three chapters take a closer look at *customers*—so students will better understand how to segment markets and satisfy target market needs. Chapter 5 introduces the demographic dimensions of the global consumer market and provides up-to-date coverage on important geodemographic trends. The next chapter studies the behavioral aspects of the final consumer market. Chapter 7 looks at how business and organizational customers—like manufacturers, channel members, and government purchasers—are using e-commerce and the other ways that they are similar to and different from final consumers. You have to understand customers to understand marketing.

Chapter 8 is a contemporary view of getting information—from marketing information systems and marketing research—for marketing management planning. This chapter includes discussion of how information technology—ranging from intranets to speedy collection of market research data—is transforming the marketing manager's job. This sets the stage for discussions in later chapters about how research and marketing information improve each area of marketing strategy planning.

The next group of chapters—Chapters 9 to 18—is concerned with developing a marketing mix out of the four Ps: Product, Place (involving channels of distribution, logistics, and distribution customer service), Promotion, and Price. These chapters are concerned with developing the "right" Product and making it available at the "right" Place with the "right" Promotion and the "right" Price—to satisfy target customers and still meet the objectives of the business. These chapters are presented in an integrated, analytical way—as part of the overall framework for the marketing strategy planning process—so students' thinking about planning marketing strategies develops logically.

Chapters 9 and 10 focus on product planning for goods and services as well as new-product development and the different strategy decisions that are required at different stages of the product life cycle. We emphasize the value of an organized new-product development process for developing really new products that propel a firm to profitable growth.

Chapters 11 through 13 focus on Place. Chapter 11 introduces decisions a manager must make about using direct distribution (for example, selling from the firm's website) or working with other firms in a channel of distribution. We put special emphasis on the need for channel members to cooperate and coordinate to better meet the needs of customers. Chapter 12 focuses on the fast-changing arena of logistics and the strides that firms are making in using e-commerce to reduce the costs of storing, transporting, and handling products while improving the distribution service they provide customers. Chapter 13 provides a clear picture of retailers, wholesalers, and their strategy planning—including exchanges taking place via the Internet. This composite chapter helps students see why the big changes taking place in retailing are reshaping the channel systems for many consumer products.

Chapters 14 to 16 deal with Promotion. These chapters build on the concepts of integrated marketing communications, direct-response promotion, and customer-initiated digital communication, which are introduced in Chapter 14. Chapter 15 deals with the role of personal selling and sales technology in the promotion blend. Chapter 16 covers advertising and sales promotion, including the ways that managers are taking advantage of the Internet to communicate more effectively and efficiently.

Chapters 17 and 18 deal with Price. Chapter 17 focuses on pricing objectives and policies, including use of information technology to implement flexible pricing, pricing in the channel, and the use of discounts, allowances, and other variations from a list price. Chapter 18 covers cost-oriented and demand-oriented pricing approaches and how they fit in today's competitive environments. The careful coverage of marketing costs helps equip students to deal with the renewed cost-consciousness of the firms they will join.

Chapter 19 offers completely updated coverage of how information technology is reshaping marketing implementation and control. This chapter also details how quality management approaches can improve implementation, including implementation of better customer service.

Chapter 20 deals with the links between marketing and other functional areas. The marketing concept says that people in an organization should work together to satisfy customers at a profit. No other text has a chapter that explains how to accomplish the "working together" part of that idea. Yet it's increasingly important in the business world today; that's what this important chapter is designed to do.

Chapter 21 reinforces the integrative nature of marketing management and reviews the marketing strategy planning process that leads to creative marketing plans and programs.

The final chapter considers how efficient the marketing process is. Here we evaluate the effectiveness of both micro- and macro-marketing—and we consider the competitive, technological, ethical, and social challenges facing marketing managers now and in the future. After this chapter, many students want to look at Appendix C—which is about career opportunities in marketing.

Careful Integration of Special Topics

Some textbooks treat "special" topics—like e-commerce, relationship marketing, international marketing, services marketing, marketing over the Internet, marketing for nonprofit organizations, marketing ethics, and business-to-business marketing—in separate chapters. We deliberatively avoid doing that because we are convinced that treating such topics separately leads to an unfortunate compartmentalization of ideas. We think they are too important to be isolated in that way. For example, to simply tack on a new chapter on e-commerce or marketing applications on the Internet completely ignores the reality that these are not just isolated topics but rather must be considered broadly across the whole fabric of marketing decisions. In fact, the huge losses piled up by failed dot-com firms over the past few years are evidence of what happens when managers fail to understand the need to integrate marketing strategy planning decisions and don't come to grips with issues such as competitor analysis, customer value, and the marketing concept. Conversely, there is virtually no area of marketing decision making where it's safe to ignore the impact of e-commerce, the Internet, or information technology. The same is true with other topics. So they are interwoven and illustrated throughout the text to emphasize that marketing thinking is crucial in all aspects of our society and economy. Instructor examination copies of this edition are again packaged with a grid that shows, in detail, how and where specific topics are integrated throughout the text. Talk is cheap, especially when it comes to the hype from some publishers about how important topics are treated in a new text. But the grid offers proof that in *Basic Marketing* we have delivered on the promise of integrated treatment.

Students Get "How-to-Do-It" Skill and Confidence

Really understanding marketing and how to plan marketing strategies can build self-confidence—and it can help prepare a student to take an active part in the business world. To move students in this direction, we deliberately include a variety of frameworks, models, classification systems, cases, and "how-to-do-it" techniques that relate to our overall framework for marketing strategy planning. Taken together, they should speed the development of "marketing sense" and enable the student to analyze marketing situations and develop marketing plans in a confident and meaningful way. They are practical and they work. In addition, because they are interesting and understandable, they motivate students to see marketing as the challenging and rewarding area it is.

Basic Marketing Motivates High-Involvement Learning

So students will see what is coming in each *Basic Marketing* chapter, behavioral objectives are included on the first page of each chapter. And to speed student understanding, important new terms are shown in red and defined immediately. Further, a glossary of these terms is presented at the end of the book. Within chapters, major section headings and second-level headings (placed in the margin for clarity) immediately show how the material is organized *and* summarize key points in the text. Further, we have placed annotated photos and ads near the concepts they illustrate to provide a visual reminder of the ideas and to show vividly how they apply in the current business world. In each chapter we have integrated Internet exercises related to the concepts being developed. The focus of these exercises is on important marketing issues, not just on "surfing the Net."

All of these aids help the student understand important concepts and speed review before exams. End-of-chapter questions and problems offer additional opportunities. They can be used to encourage students to investigate the marketing process and develop their own ways of thinking about it. These can be used for independent study or as a basis for written assignments or class discussion.

Varied Types of Cases

Understanding of the text material can be deepened by analysis and discussion of specific cases. *Basic Marketing* features several different types of cases. Each chapter starts with an in-depth case study developed specifically to highlight that chapter's teaching objectives and the specific marketing decision areas covered in that chapter. In addition, each chapter features a special case report in a highlighted box. These thought-provoking cases illustrate how companies handle topics covered in that chapter. All of these cases provide an excellent basis for critical evaluation and discussion. And we've included relevant Internet addresses so that it is easy for students to quickly get updated information about the companies and topics covered in the cases. Of course, website addresses referenced in the cases may change. Some companies change their websites to get a fresh look, to take advantage of new Web capabilities, or just to update the information that's available. However, when that occurs, our *Basic Marketing* website at www.mhhe.com/fourps provides up-to-date links relevant to the chapters in the text. Our CD-ROMs also include links to the website so you can bookmark the site in your Internet browser.

In addition, there are several suggested cases at the end of each chapter. The focus of these cases is on problem solving. They encourage students to apply, and really get involved with, the concepts developed in the text. Each of the first 19 chapters also features a computer-aided problem. These case-based exercises stimulate a problem-solving approach to marketing strategy planning and give students hands-on experience that shows how logical analysis of alternative strategies can lead to improved decision making. For the convenience of students and faculty alike, printed versions of the cases for the computer-aided problems are incorporated in the book itself. Further, the award-winning spreadsheet software we developed specifically for use with these problems has been revised so that it is fully integrated with the other applications on the Student CD-ROM that comes with the text.

New Multimedia Video Cases are Integrative

In the last edition we included a custom-produced set of exciting video cases. The response to them was great, and this time we've expanded the set and updated some of the best from the previous set. Each of these combines a written case with an accompanying video. These cases are a bit longer than the text-only cases and open up the opportunity for students to analyze an organization's whole marketing program in more depth and with even greater integration. Marketing professors wrote the scripts for both the videos and text portions of the cases—so the videos reinforce real content while bringing a high-involvement multimedia dimension to the learning experience. And to assure consistency with all of the other *Basic Marketing* materials, we've carefully edited and coordinated the whole effort. These cases were developed so that they focus on different areas of the text, and thus they deal with a variety of issues:

- The expanding role of marketing in developing export opportunities for a raw material that was previously just viewed as a commodity.
- How a well-known company won profits and customer loyalty by developing a marketing mix that's carefully matched to the needs of its target market.
- New-product development for a major component part that is sold to producers who serve consumer markets.
- The growth strategy for a vineyard that is working to develop a major brand.
- The development of a new market awareness and strategy by a major nonprofit organization.
- A case on the promotional program for the introduction of an exciting new automobile.
- An integrated case on the marketing strategy for an innovative household appliance.

We designed these cases so that students can analyze them before or after seeing the video, or even without seeing the video at all. They can be used in a variety of ways, either for class discussion or individual assignments. To get the ball rolling, students get their own copy of segments of the case videos on the Student CD-ROM. We're proud of these video cases, and we're sure that they provide you with a valuable new way to learn about marketing.

Comprehensive, Current References for Independent Study

Some professors and students want to follow up on text readings. Each chapter is supplemented with detailed references—to both classic articles and current readings in business publications. These can guide more detailed study of the topics covered in a chapter.

Instructor Creates a System—with *Basic Marketing's P.L.U.S.*

Basic Marketing can be studied and used in many ways—the *Basic Marketing* text material is only the central component of our Professional Learning Units Systems (our *P.L.U.S.*) for students and teachers. Instructors (and students) can select from our units to develop their own personalized systems. Many combinations of units are possible—depending on course objectives. As a quick overview, in addition to the *Basic Marketing* text, the *P.L.U.S.* package includes a variety of new and updated supplements:

- A redesigned and updated *Student CD-ROM to Accompany Basic Marketing,* which includes clips for the video cases, a database of ads and annotations that illustrate keys concepts for each chapter, a new version of our computer-aided problems (CAP) spreadsheet software, self-test quizzes, and narrated self-study PowerPoint electronic slide shows, to introduce students to what's ahead. The CD also includes a revision of the *Basic Marketing Hypertext Reference* for use in developing marketing plans or reviewing for tests.
- An online learning center at our revised website (www.mhhe.com/fourps) for students and instructors, with features such as (constantly updated) links to just-published articles from myPowerWeb on topics in each chapter, chat rooms, software downloads, Internet website links, and other exciting features.
- A completely new and much expanded archive of PowerPoint lecture slides, incorporating full-motion video clips, photos, ads, and other multimedia assets to support the professor.
- An improved *Instructor CD-ROM to Accompany Basic Marketing*, which includes all of the instructor resources available for *Basic Marketing* in electronic form.

In addition, we've completely revised and updated

- The *Multimedia Lecture Support Package*.
- The *Learning Aid* workbook.
- *Applications in Basic Marketing*, an annually updated book of marketing clippings from the popular press, free and shrinkwrapped with the text and, new to this edition, supplemented with myPowerWeb digital articles on the Web.
- Over 200 color acetates (also available in electronic form).
- Over 200 transparency masters (also available as PowerPoint slides).
- *Instructor's Manual*.
- Author-prepared *Manual of Tests*, accompanied by the *Diploma* test-generator software that supports both printed and online testing.
- A complete set of new and updated *teaching videos* and seven great video cases (and instructor's manual).
- A new Windows version of the *The Marketing Game!* (and instructor's manual) that offers password-protected digital plan and report files and supports working over the Internet.

We've been busy. You may not want to use all of this. Some people don't want any of it. But whatever you elect to use—and in whatever medium you like to work—the teaching and learning materials work well together. We've designed them that way.

Hypertext—a Marketing Knowledge Navigator

We introduced the innovative *Basic Marketing Hypertext Reference* with the 11th edition of *Basic Marketing* and have expanded its capabilities ever since. This easy-to-use Windows software puts almost all of the key concepts from *Basic Marketing* at your fingertips. It features hyperlinks, which means that when you are reading about a concept on screen you can instantly jump to more detail on any topic. You simply highlight the concept or topic and click with a mouse or press the enter key. Books assemble information in some specific order—but hypertext allows you to integrate thinking on any topic or combination of topics, regardless of where it is treated in the text.

The new version of the software provides an even clearer and easier way to search for ideas while developing a marketing plan. You can also use the software to review topics in "book order"—starting with learning objectives and then "paging" through each set of ideas.

Free Applications Book—Updated Each Year

It is a sign of the commitment of our publisher to the introductory marketing course that it will publish a new edition of *Applications in Basic Marketing* every year and provide it free of charge shrinkwrapped with each new copy of the 14th edition of *Basic Marketing*. This annually updated collection of marketing "clippings"—from publications such as *Business Week*, *The Wall Street Journal*, *Advertising Age*, and *Fortune*—provides convenient access to short, interesting, and current discussions of marketing issues. Each edition features about 100 articles. There are a variety of short clippings related to each chapter in *Basic Marketing*. In addition, because we revise this collection each year, it includes timely material that is available in no other text.

Learning Aid—Deepens Understanding

There are more components to *P.L.U.S.* A separate *Learning Aid* provides several more units and offers further opportunities to obtain a deeper understanding of the material. The *Learning Aid* can be used by the student alone or with teacher direction. Portions of the *Learning Aid* help students to review what they have studied. For example, there is a brief introduction to each chapter, a list of the important new terms (with page numbers for easy reference), true-false questions (with answers and page numbers) that cover all the important terms and concepts, and multiple-choice questions (with answers) that illustrate the kinds of questions that may appear in examinations. In addition, the *Learning Aid* has cases, exercises, and problems—with clear instructions and worksheets for the student to complete. The *Learning Aid* also features computer-aided problems that build on the computer-aided cases in the text. The *Learning Aid* exercises can be used as classwork or homework—to drill on certain topics and to deepen understanding of others by motivating application and then discussion. In fact, reading *Basic Marketing* and working with the *Learning Aid* can be the basic activity of the course.

Compete and Learn—with New Edition of *The Marketing Game!*

Another valuable resource is *The Marketing Game! The Marketing Game!* is a PC-based competitive simulation. It was developed specifically to reinforce the target marketing and marketing strategy-planning ideas discussed in *Basic Marketing*. Students make marketing management decisions—blending the four Ps to compete for the business of different possible target markets. The innovative design of *The Marketing Game!* allows the instructor to increase the number of decision areas involved as students learn more about marketing. In fact, many instructors use the advanced levels of the game as the basis for a second course. *The Marketing Game!* is widely heralded as the best marketing strategy simulation available—and the new Windows edition widens its lead over the others available. Competitors don't even need to be on the same continent. It works great with password-protected decisions submitted over the Internet and reports returned the same way.

Multimedia Support for Preparation, Lectures, and Discussion

Basic Marketing and all of our accompanying materials have been developed to promote student learning and get students involved in the excitement and challenges of marketing management. Additional elements of *P.L.U.S.* have been specifically developed to help an instructor offer a truly professional course that meets the objectives he or she sets for students. Complete instructor's manuals accompany all of the *P.L.U.S.* components.

Electronic Presentation Slides with Many Uses

With this edition we are providing instructors with a completely new, much-expanded set of PowerPoint electronic slide presentations. This flexible package features a large number of PowerPoint graphics developed for every chapter in the text. An instructor can use the provided software to display the electronic slides with a computer-controlled video projector, in the order that they're provided or branching in whatever sequence is desired. Presentations can be based on composite slides, or the points on a slide can "build up" one point at a time.

Because we provide the native-format PowerPoint files, instructors can modify or delete any slide or add other slides by using their own copy of PowerPoint. And, of course, if electronic projection equipment isn't available, the instructor can print out the images to customized color acetates or black and white transparencies. All of the overhead masters are also available, in color, as PowerPoint slides.

While these electronic slides are intended mainly for instructor use in class discussions and lectures, they are easy to use and can be placed on the Internet, on the school's computer network, or in a computer lab as a supplement for independent review by students.

Complete Multimedia Lecture Support

With the PowerPoint electronic slide presentations we also provide detailed lecture notes, as well as lecture outlines. The PowerPoint slide show includes small versions of the slides for class handouts. All of these materials are packaged in our *Multimedia Lecture Support Package*. This supplement is available in an electronic form on the Instructor CD-ROM, and that makes it even more convenient to use. It gives instructors a great deal of flexibility and saves time that can be spent on other teaching activities. Instructors who prefer to use materials like those that were in the past included with our *Lecture Guide* won't be disappointed either. The new package will provide that material as well—in both printed form and in the form of word-processing files (which makes it easier for instructors to electronically cut and paste and incorporate their own materials or to save time and effort in creating a website for the course).

In addition, the *Multimedia Lecture Support Package* is accompanied by a high-quality selection of overhead masters and color transparencies—over 400 in all. The manual provides detailed suggestions about ways to use them. All of these items are also available on the CD-ROM.

Exciting New Videos—Created by Marketing Experts

The newly revised and expanded *Basic Marketing Videos* are also available to all schools that adopt *Basic Marketing*. Half of the video modules are completely new—based on scripts written by expert marketing scholars and carefully linked to key topics in the text. In addition, several of the most popular video modules from the previous edition—the ones instructors and students said they most wanted to keep—have been thoroughly revised and updated. These new videos are really great, but it doesn't stop there! As we noted earlier, there are also seven great new videos to accompany the video cases.

Testing that Works for Faculty and Students

In addition, thousands of objective test questions—*written by the authors* to really work with the text—give instructors a high-quality resource. The *Diploma* program for Windows computers allows the instructor to select from any of these questions, change them as desired, or add new questions—and quickly print out a finished test customized to the instructor's course. As an added benefit, the instructor can publish questions to a website and students can take tests online.

The Responsibilities of Leadership

In closing, we return to a point raised at the beginning of this preface. *Basic Marketing* has been a leading textbook in marketing since its first edition. We take the responsibilities of that leadership seriously. We know that you want and deserve the very best teaching and learning materials possible. It is our commitment to bring you those materials—today with this edition and in the future with subsequent editions.

We recognize that fulfilling this commitment requires a process of continuous improvement. Improvements, changes, and development of new elements must be ongoing—because needs change. You are an important part of this evolution, of this leadership. We encourage your feedback. The most efficient way to get in touch with us is to send an e-mail message to Bill_Perreault@unc.edu. There's also a comment form built into the book's website, and if you prefer the traditional approach, send a letter to 2104 N. Lakeshore Dr., Chapel Hill, NC, 27514. Thoughtful criticisms and suggestions from students and teachers alike have helped to make *Basic Marketing* what it is. We hope that you will help make it what it will be in the future.

William D. Perreault, Jr.
E. Jerome McCarthy

When You Finish This Chapter, You Should

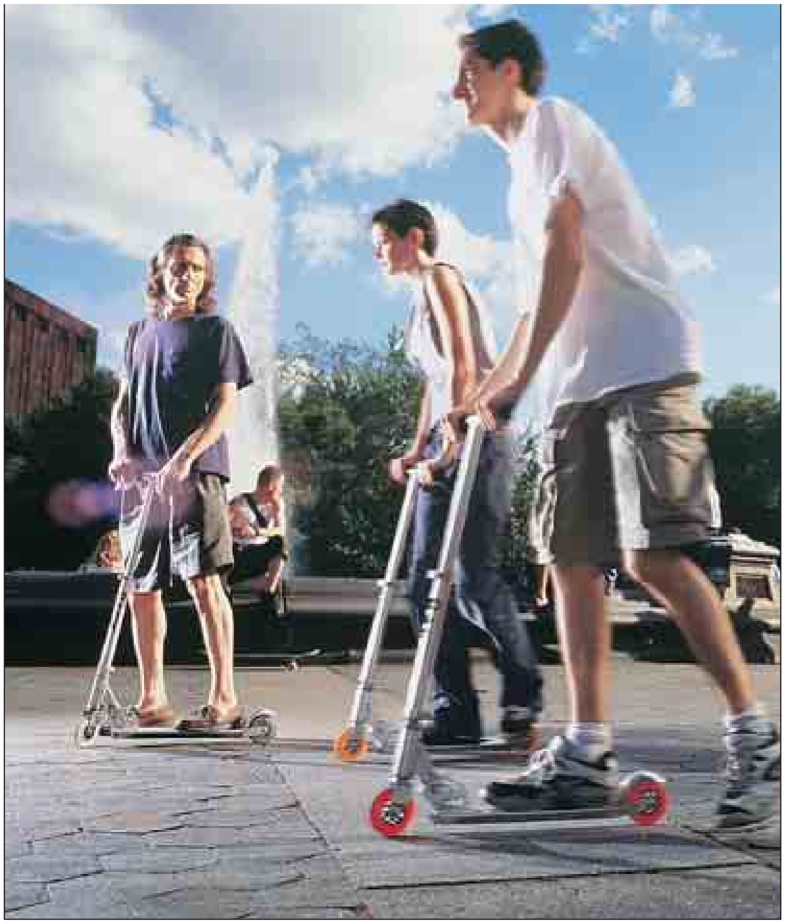
1. Know what marketing is and why you should learn about it.
2. Understand the difference between micro-marketing and macro-marketing.
3. Know why and how macro-marketing systems develop.
4. Understand why marketing is crucial to economic development and our global economy.
5. Know why marketing specialists—including middlemen and facilitators—develop.
6. Know the marketing functions and who performs them.
7. Understand the important new terms (shown in red).

Chapter One

Marketing's Role in the Global Economy

When it's time to roll out of bed in the morning, does your Sony alarm clock wake you with a buzzer or playing your favorite radio station? Is the station playing hip-hop, classical, or country music—or perhaps a Red Cross ad asking you to contribute blood? Will you slip into your Levi's jeans, your shirt from Abercrombie and Fitch, and your Nikes, or does the day call for your Brooks Brothers interviewing suit? Will breakfast be Lender's Bagels with cream cheese or Kellogg's Frosted Flakes—made with grain from America's heartland—or some extra-large eggs and Oscar Mayer bacon cooked in a Panasonic microwave oven imported from Japan? Will you drink Maxwell House decaf coffee grown in Colombia or some Tropicana Orange Juice? Will you eat at home or is this a day to meet a friend at the Marriott-run cafeteria—where you'll pay someone else to serve your breakfast? To figure

place price promotion produc



A family in China may have little choice about what food they will eat or where their clothing will come from. A farmer in the mountains of Jamaica may awake in a barren hut with little more than the hope of raising enough to survive. A businessperson in a large city like Tokyo may have many choices but not be familiar with products that have names like Maxwell House, General Motors, and Oscar Mayer.

What explains these differences, and what do they have to do with marketing? In this chapter, we'll answer questions like these. You'll see what marketing is all about and why it's important to you. We'll also explore how marketing affects the quality of life in different societies and why it is so crucial to economic development and our global economy.

out what the day holds, will you need to log on to AOL to check your e-mail, or perhaps check the calendar on your Palm? Will you head off to school or work in a VW Beetle or on a bus that the city bought from General Motors, or is this the right kind of day to dust off your Razor scooter?

When you think about it, you can't get very far into a day without bumping into marketing—and what the whole marketing system does for you. It affects every aspect of our lives—often in ways we don't even consider.

In other parts of the world, people wake up each day to different kinds of experiences.

www.mhhe.com/fourps

price

place

product

promotion

t

Service Master helps hospitals improve a new mom's satisfaction with the hospital by serving "celebration meals."

Marketing—What's It All About?

Marketing is more than selling or advertising

If forced to define marketing, most people, including some business managers, say that marketing means "selling" or "advertising." It's true that these are parts of marketing. But *marketing is much more than selling and advertising*.

How did all those bicycles get here?

To illustrate some of the other important things that are included in marketing, think about all the bicycles being peddled with varying degrees of energy by bike riders around the world. Most of us weren't born sitting on a bicycle. Nor do we make our own bicycles. Instead, they are made by firms like Schwinn, Performance, Huffy, and Murray.

Most bikes are intended to do the same thing—get the rider from one place to another. But a bike rider can choose from a wide assortment of models. They are designed in different sizes, with different frames for men and women, and with or without gears. Off-road bikes have large knobby tires, and the tires on racing bikes are narrow. Some bikes have hand brakes and others have foot brakes. Kids and older people may want more wheels—to make balancing easier; clowns want only one wheel, to make balancing more interesting. And some bikes need baskets or even trailers for cargo or an infant seat for a small passenger. You can buy a basic bike for less than $50. Or, you can spend more than $2,500 for a custom frame—not including the handcrafted wheels that you order over the Internet.

This variety of styles and features complicates the production and sale of bicycles. The following list shows some of the many things a firm should do before and after it decides to produce a bike.

1. Analyze the needs of people who might buy a bike and decide if they want more or different models.
2. Predict what types of bikes—handlebar styles, type of wheels, weights, and materials—different customers will want and decide which of these people the firm will try to satisfy.

3. Estimate how many of these people will be riding bikes over the next several years and how many bikes they'll buy.
4. Predict exactly when these people will want to buy bicycles.
5. Determine where in the world these bike riders will be and how to get the firm's bikes to them.
6. Estimate what price they are willing to pay for their bikes and if the firm can make a profit selling at that price.
7. Decide which kinds of promotion should be used to tell potential customers about the firm's bikes.
8. Estimate how many competing companies will be making bikes, how many bikes they'll produce, what kind, and at what prices.
9. Figure out how to provide warranty service if a customer has a problem after buying a bike.

The above activities are not part of **production**—actually making goods or performing services. Rather, they are part of a larger process—called *marketing*—that provides needed direction for production and helps make sure that the right goods and services are produced and find their way to consumers.

Our bicycle example shows that marketing includes much more than selling or advertising. We'll describe marketing activities in the next chapter. And you'll learn much more about them before you finish this book. For now, it's enough to see that marketing plays an essential role in providing consumers with need-satisfying goods and services and, more generally, in creating customer satisfaction. Simply put, **customer satisfaction** is the extent to which a firm fulfills a customer's needs, desires, and expectations.

How Marketing Relates to Production

Production is a very important economic activity. Whether for lack of skill and resources or just lack of time, most people don't make most of the products they use. Picture yourself, for example, building a 10-speed bicycle, a DVD player, or an electronic watch—starting from scratch! We also turn to others to produce services—like health care, air transportation, and entertainment. Clearly, the high standard of living that most people in advanced economies enjoy is made possible by specialized production.

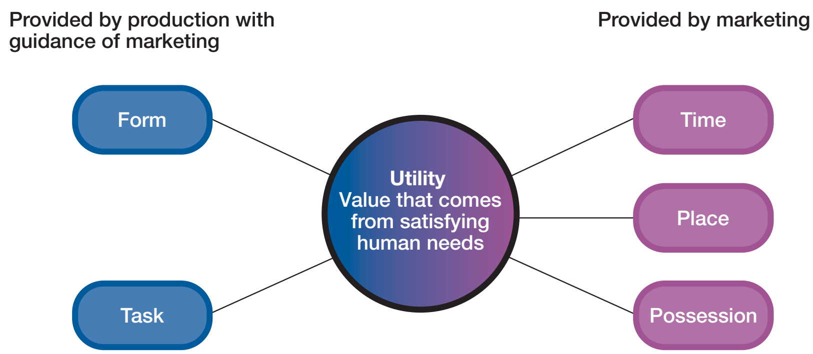
Bicycles, like mousetraps, don't sell themselves

Although production is a necessary economic activity, some people overrate its importance in relation to marketing. Their attitude is reflected in the old saying: "Make a better mousetrap and the world will beat a path to your door." In other words, they think that if you just have a good product, your business will be a success.

The "better mousetrap" idea probably wasn't true in Grandpa's time, and it certainly isn't true today. In modern economies, the grass grows high on the path to the Better Mousetrap Factory—if the new mousetrap is not properly marketed. We have already seen, for example, that there's a lot more to marketing bicycles than just making them. This is true for most goods and services.

The point is that production and marketing are both important parts of a total business system aimed at providing consumers with need-satisfying goods and services. Together, production and marketing supply five kinds of economic utility—form, task, time, place, and possession utility—that are needed to provide consumer satisfaction. Here, **utility** means the power to satisfy human needs. See Exhibit 1-1.

Exhibit 1-1
Types of Utility and How They Are Provided



Bicycles do not automatically provide utility

Form utility is provided when someone produces something tangible—for instance, a bicycle. **Task utility** is provided when someone performs a task for someone else—for instance, when a bank handles financial transactions. But just producing bicycles or handling bank accounts doesn't result in consumer satisfaction. The product must be something that consumers want or there is no need to be satisfied—and no utility.

This is how marketing thinking guides the production side of business. Marketing decisions focus on the customer and include decisions about what goods and services to produce. It doesn't make sense to provide goods and services consumers don't want when there are so many things they do want or need. Let's take our "mousetrap" example a step further. Some customers don't want *any kind* of mousetrap. They may want someone else to produce a service and exterminate the mice for them, or they may live where mice are not a problem. Marketing is concerned with what customers want, and it should guide what is produced and offered. This is an important idea that we will develop more completely later.

Even when marketing and production combine to provide form or task utility, consumers won't be satisfied until time, place, and possession utility are also provided.

Time utility means having the product available *when* the customer wants it. And **place utility** means having the product available *where* the customer wants it. Bicycles that stay at a factory don't do anyone any good. Time and place utility are very important for services too. For example, neighborhood emergency care health clinics have become very popular. People just walk in as soon as they feel sick, not a day later when their doctor can schedule an appointment.

Possession utility means obtaining a good or service and having the right to use or consume it. Customers usually exchange money or something else of value for possession utility.

Stated simply, marketing provides time, place, and possession utility. It should also guide decisions about what goods and services should be produced to provide form utility and task utility. We'll look at how marketing does this later in this chapter. First, we want to discuss why you should study marketing, and then we'll define marketing.

Marketing Is Important to You

Marketing is important to every consumer

One important reason for learning about marketing is that marketing affects almost every aspect of your daily life. All the goods and services you buy, the stores where you shop, and the radio and TV programs paid for by advertising are there because of marketing. Even your job résumé is part of a marketing campaign to sell

By working to understand the needs of its customers, wherever they are, Toyota has successfully adapted to marketers all around the world.

yourself to some employer! Some courses are interesting when you take them but never relevant again once they're over. Not so with marketing—you'll be a consumer dealing with marketing for the rest of your life.

Another reason for studying marketing is that you—as a consumer—pay for the cost of marketing activities. In advanced economies, marketing costs about 50 cents of each consumer dollar. For some goods and services, the percentage is much higher.

Marketing will be important to your job

Marketing Manager for Consumer Electronics

We've got a new opportunity that should help our business grow into the next century. Put your college degree and experience in marketing consumer durables to work. Come help us analyze our markets and plan our marketing mix in a logical, creative, and enthusiastic way. This job offers income above industry standards, dynamic colleagues, relocation to desirable midwest suburb, and fast-track upward mobility. Check our website for more detail or reply in confidence, with a copy of your resume, to Box 4953.

Still another reason for studying marketing is that there are many exciting and rewarding career opportunities in marketing. Marketing is often the route to the top. Throughout this book you will find information about opportunities in different areas of marketing—in sales, advertising, product management, marketing research, distribution, and other areas. And Appendix C is all about career planning in marketing.

Even if you're aiming for a nonmarketing job, you'll be working with marketing people. Knowing something about marketing will help you understand them better. It will also help you do your own job better. Throughout the book, we'll discuss ways that marketing relates to other functional areas—and Chapter 20 focuses on those issues. Further, remember that marketing is important to the success of every organization. A company that can't successfully sell its products doesn't need accountants, financial managers, production managers, personnel managers, computer programmers, or credit managers.

Even if you're not planning a business career, marketing concepts and techniques apply to nonprofit organizations too. Many nonprofit organizations have a marketing manager. And the same basic principles used to sell soap are also used to "sell" ideas, politicians, mass transportation, health care services, conservation, museums, and even colleges. Think about the school where you take this course. If you didn't know about its offerings—or if they didn't interest you—you would simply pick some other school.[1]

Marketing affects economic growth

An even more basic reason for studying marketing is that marketing plays a big part in economic growth and development. Marketing stimulates research and new ideas—resulting in innovative new goods and services. Marketing gives customers a choice among products. If these products satisfy customers, fuller employment, higher incomes, and a higher standard of living can result. An effective marketing system is important to the future of all nations.[2]

How Should We Define Marketing?

As we said earlier, some people think of marketing too narrowly as "selling and advertising." On the other hand, one author defined marketing as the "creation and delivery of a standard of living."[3] That definition is too broad.

An important difference between the two definitions may be less obvious. The first definition is a *micro*-level definition. It focuses on activities performed by an individual organization. The second is a *macro*-level definition. It focuses on the economic welfare of a whole society.

Micro- or macro-marketing?

Which view is correct? Is marketing a set of activities done by individual firms or organizations? Or is it a social process?

To answer this question, let's go back to our bicycle example. We saw that a producer of bicycles has to perform many customer-related activities besides just making bikes. The same is true for an insurance company, an art museum, or a family-service agency. This supports the idea of marketing as a set of activities done by individual organizations.

On the other hand, people can't survive on bicycles and art museums alone! In advanced economies, it takes thousands of goods and services to satisfy the many needs of society. For example, a typical Wal-Mart store carries more than 100,000 different items, and its Supercenter carries more than 20,000 additional grocery items, many of them perishable. A society needs some sort of marketing system to organize the efforts of all the producers and middlemen needed to satisfy the varied needs of all its citizens. So marketing is also an important social process.

Internet

Internet Exercise You can check out the online shopping experience of Wal-Mart on the Web by going to the Wal-Mart home page (www.walmart.com) and clicking on "Go Shopping."

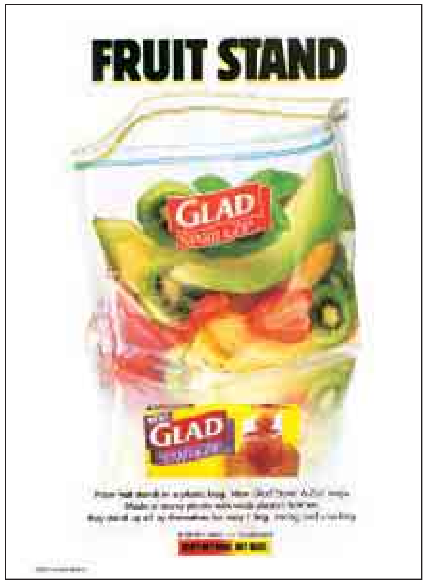
The answer to our question is that *marketing is both a set of activities performed by organizations and a social process*. In other words, marketing exists at both the micro and macro levels. Therefore, we will use two definitions of marketing—one for micro-marketing and another for macro-marketing. Micro-marketing looks at customers and the organizations that serve them. Macro-marketing takes a broad view of our whole production–distribution system.

Micro-Marketing Defined

Micro-marketing is the performance of activities that seek to accomplish an organization's objectives by anticipating customer or client needs and directing a flow of need-satisfying goods and services from producer to customer or client.

Let's look at this definition.[4]

The aim of marketing is to identify customers' needs—and to meet those needs so well that the product almost sells itself.



Applies to profit and nonprofit organizations

To begin with, this definition applies to both profit and nonprofit organizations. Profit is the objective for most business firms. But other types of organizations may seek more members—or acceptance of an idea. Customers or clients may be individual consumers, business firms, nonprofit organizations, government agencies, or even foreign nations. While most customers and clients pay for the goods and services they receive, others may receive them free of charge or at a reduced cost through private or government support.

More than just persuading customers

You already know that micro-marketing isn't just selling and advertising. Unfortunately, many executives still think it is. They feel that the job of marketing is to "get rid of" whatever the company happens to produce. In fact, the aim of marketing is to identify customers' needs and meet those needs so well that the product almost "sells itself." This is true whether the product is a physical good, a service, or even an idea. If the whole marketing job has been done well, customers don't need much persuading. They should be ready to buy. And after they do buy, they'll be satisfied and ready to buy the same way again the next time.

Begins with customer needs

Marketing should begin with potential customer needs—not with the production process. Marketing should try to anticipate needs. And then marketing, rather than production, should determine what goods and services are to be developed—including decisions about product design and packaging; prices or fees; credit and collection policies; use of middlemen; transporting and storing policies; advertising and sales policies; and, after the sale, installation, customer service, warranty, and perhaps even disposal policies.

Does not do it alone

This does not mean that marketing should try to take over production, accounting, and financial activities. Rather, it means that marketing—by interpreting customers' needs—should provide direction for these activities and try to coordinate them. After all, the purpose of a business or nonprofit organization is to satisfy customer or client needs. It is not to supply goods and services that are convenient to produce and *might* sell or be accepted free.

Builds a relationship with the customer

When marketing helps everyone in a firm really meet the needs of a customer both before and after a purchase, the firm doesn't just get a single sale. Rather, it has a sale and an ongoing *relationship* with the customer. Then, in the future, when the customer has the same need again—or some other need that the firm can meet—other sales will follow. That's why we emphasize that marketing concerns a *flow* of need-satisfying goods and services to the customer. Often, that flow is not just for a single transaction but rather is part of building a long-lasting relationship that is beneficial to both the firm and the customer.

The Focus of This Text—Management-Oriented Micro-Marketing

Since you are probably preparing for a career in management, the main focus of this text will be on micro-marketing. We will see marketing through the eyes of the marketing manager.

It is important to keep in mind that the micro-marketing ideas and decision areas we will be discussing throughout this text apply to a wide variety of situations. They are important not only for large and small business firms but also for all types of public sector and nonprofit organizations. They apply to new ventures started by a single entrepreneur as well as to ongoing efforts by teams of people in corporations. They are useful in domestic markets and international markets and regardless of whether the organization focuses on marketing physical goods, services, or an idea or cause. They are equally critical whether the relevant customers or clients are individual consumers, businesses, or some other type of organization. In short, every organization needs to think about its markets and how effectively it meets its customers' or clients' needs. For editorial convenience, and to reflect the fact that most readers will work in business settings, when we discuss marketing concepts we will sometimes use the term *firm* as a shorthand way of referring to any type of organization, whether it is a political party, a religious organization, a government agency, or the like. However, to reinforce the point that the ideas apply to all types of organizations, throughout the book we will illustrate marketing management concepts with examples that represent a wide variety of marketing situations.

Although micro-marketing is the primary focus of the text, marketing managers must remember that their organizations are just small parts of a larger macro-marketing system. Therefore, the rest of this chapter will look at the macro view of marketing. Let's begin by defining macro-marketing and reviewing some basic ideas. Then, in Chapter 2, we'll explain the marketing management decision areas we will be discussing in the rest of the book.

Macro-Marketing Defined

Macro-marketing is a social process that directs an economy's flow of goods and services from producers to consumers in a way that effectively matches supply and demand and accomplishes the objectives of society.

Emphasis is on whole system

Like micro-marketing, macro-marketing is concerned with the flow of need-satisfying goods and services from producer to consumer. However, the emphasis with macro-marketing is not on the activities of individual organizations. Instead, the emphasis is on *how the whole marketing system works*. This includes looking at how marketing affects society, and vice versa.

Every society needs a macro-marketing system to help match supply and demand. Different producers in a society have different objectives, resources, and skills. Likewise, not all consumers share the same needs, preferences, and wealth. In other words, within every society there are both heterogeneous (highly varied) supply capabilities and heterogeneous demands for goods and services. The role of a macro-marketing system is to effectively match this heterogeneous supply and demand *and* at the same time accomplish society's objectives.

Is it effective and fair?

The effectiveness and fairness of a particular macro-marketing system must be evaluated in terms of that society's objectives. Obviously, all nations don't share the same objectives. For example, Swedish citizens receive many "free" services—like health care and retirement benefits. Goods and services are fairly evenly distributed among the Swedish population. By contrast, Iraq places little emphasis on producing goods and services for individual consumers and more on military spending. In India the distribution of goods and services is very uneven—with a big gap between the "have-nots" and the elite "haves." Whether each of these systems is judged "fair" or "effective" depends on the objectives of the society.

Let's look more closely at macro-marketing.[5] And to make this more meaningful to you, consider (1) what kind of a macro-marketing system you have and (2) how effective and fair it is.

Every Society Needs an Economic System

All societies must provide for the needs of their members. Therefore, every society needs some sort of **economic system**—the way an economy organizes to use scarce resources to produce goods and services and distribute them for consumption by various people and groups in the society.

How an economic system operates depends on a society's objectives and the nature of its political institutions.[6] But regardless of what form these take, all economic systems must develop some method—along with appropriate economic institutions—to decide what and how much is to be produced and distributed by whom, when, to whom, and why. How these decisions are made may vary from nation to nation. But the macro-level objectives are basically similar: to create goods and services and make them available when and where they are needed—to maintain or improve each nation's standard of living or other socially defined objective.

How Economic Decisions Are Made

There are two basic kinds of economic systems: planned systems and market-directed systems. Actually, no economy is entirely planned or market-directed. Most are a mixture of the two extremes.

Government planners may make the decisions

In a **planned economic system,** government planners decide what and how much is to be produced and distributed by whom, when, to whom, and why. Producers generally have little choice about what goods and services to produce. Their main task is to meet their assigned production quotas. Prices are set by government planners and tend to be very rigid—not changing according to supply and demand. Consumers usually have some freedom of choice—it's impossible to control every single detail! But the assortment of goods and services may be quite limited. Activities such as market research, branding, and advertising usually are neglected. Sometimes they aren't done at all.

Government planning may work fairly well as long as an economy is simple and the variety of goods and services is small. It may even be necessary under certain conditions—during wartime, drought, or political instability, for example. However, as economies become more complex, government planning becomes more difficult. It may even break down. Planners may be overwhelmed by too many complex decisions. And consumers may lose patience if the planners don't respond to their needs. The collapse of communism in Eastern Europe dramatically illustrates this. Citizens of what was the Soviet Union were not satisfied with the government's plan—because products consumers wanted and needed were not available. To try to reduce consumer dissatisfaction, government planners tried to put more emphasis on making consumer goods available, but they were not able to produce the results consumers wanted. In short, it was consumer dissatisfaction with decisions made by government planners that brought about a revolution—one that is leading to the development of market-directed economies in the republics of Eastern Europe.[7]

Countries such as China, North Korea, and Cuba still rely primarily on planned economic systems. Even so, around the world there is a broad move toward market-directed economic systems—because they are more effective in meeting consumer needs.

A market-directed economy adjusts itself

In a **market-directed economic system,** the individual decisions of the many producers and consumers make the macro-level decisions for the whole economy. In a pure market-directed economy, consumers make a society's production decisions when they make their choices in the marketplace. They decide what is to be produced and by whom—through their dollar "votes."

Price is a measure of value

Prices in the marketplace are a rough measure of how society values particular goods and services. If consumers are willing to pay the market prices, then apparently they feel they are getting at least their money's worth. Similarly, the cost of labor and materials is a rough measure of the value of the resources used in the production of goods and services to meet these needs. New consumer needs that can be served profitably—not just the needs of the majority—will probably be met by some profit-minded businesses.

In summary, in a market-directed economic system the prices in both the production sector (for resources) and the consumption sector (for goods and services) vary to allocate resources and distribute income according to consumer preferences. Over time, the result is a balance of supply and demand and the coordination of the economic activity of many individuals and institutions.

Greatest freedom of choice

Consumers in a market-directed economy enjoy great freedom of choice. They are not forced to buy any goods or services, except those that must be provided for the good of society—things such as national defense, schools, police and fire protection, highway systems, and public-health services. These are provided by the community—and the citizens are taxed to pay for them.

Similarly, producers are free to do whatever they wish—provided that they stay within the rules of the game set by government *and* receive enough dollar "votes" from consumers. If they do their job well, they earn a profit and stay in business. But profit, survival, and growth are not guaranteed.

Conflicts can arise

Producers and consumers making free choices can cause conflicts and difficulties. This is called the **micro-macro dilemma.** What is "good" for some producers and consumers may not be good for society as a whole.

Gun control in the U.S. is an example. Each year thousands of people are killed with handguns. Yet there are producers who make and sell handguns at a profit. And there are many consumers who feel strongly about their right to own guns. But

others argue that handguns are a threat to society. They want handgun sales banned and sales of all weapons limited—as is the case in many countries. Should gun producers be allowed to sell guns to consumers who want them?

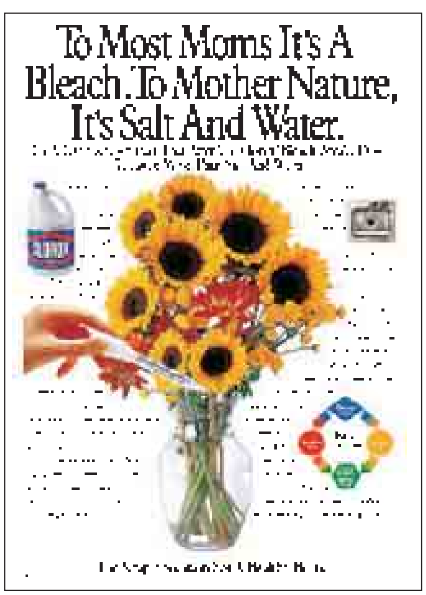
Decisions don't have to involve life and death issues to be important. Many Americans want the convenience of disposable products and products in easy-to-use, small-serving packages. But these same "convenient" products and packages often lead to pollution of the environment and inefficient use of natural resources. Should future generations be left to pay the consequences of pollution that is the result of "free choice" by today's consumers?

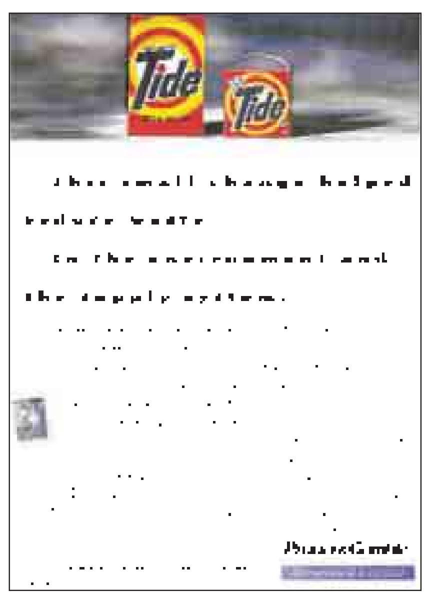
Questions like these are not easy to answer. The basic reason is that many different people may have a stake in the outcomes—and social consequences—of the choices made by individual managers *and* consumers in a market-directed system. As you read this book and learn more about marketing, you will also learn more about social responsibility in marketing and why it must be taken seriously.

The role of government

The American economy and most other Western economies are mainly market-directed—but not completely. Society assigns supervision of the system to the government. For example, besides setting and enforcing the "rules of the game," government agencies control interest rates and the supply of money. They also set import and export rules that affect international competition, regulate radio and TV broadcasting, sometimes control wages and prices, and so on. Government also tries to be sure that property is protected, contracts are enforced, individuals are not exploited, no group unfairly monopolizes markets, and producers deliver the kinds and quality of goods and services they claim to be offering.

Socially responsible marketing managers are concerned about the environmental impact of their decisions, and some firms are finding innovative ways to both help the environment and improve customer satisfaction.





You can see that we need some of these government activities to make sure the economy runs smoothly. However, some people worry that too much government "guidance" threatens the survival of a market-directed system and the economic and political freedom that goes with it. For example, in the past 15 years the U.S. government has done much less "interfering"—especially in markets for services such as electricity, banking, transportation, and communications. The vigorous competition among telephone companies is a good example of what follows. About 15 years ago AT&T was the only long-distance service provider and a government agency controlled its prices and services. Now many different types of telecom companies compete for that business, and decisions about prices and services are made by marketing managers and by what consumers choose.

The U.S. is not alone in reducing regulation and government control of markets. One clear indication of this is the trend toward privatization, which means that an activity previously owned and operated by the government is sold to private sector owners who manage it in a competitive market. For example, many countries that previously owned airlines have sold the airlines and changed regulations so that there is more competition among various carriers.

On the other hand, there are some areas where there seems to be a more active government role in planning and control—including health care and issues related to the environment. Some consumers might benefit by such changes, yet more government control would reduce consumer choice.[8]

All Economies Need Macro-Marketing Systems

At this point, you may be saying to yourself: All this sounds like economics—where does marketing fit in? Studying a *macro*-marketing system is a lot like studying an economic system except we give more detailed attention to the "marketing" components of the system—including consumers and other customers, wholesalers and retailers, and other marketing specialists. We focus on the activities they perform and how the interaction of the components affects the effectiveness and fairness of a particular system.

In general, we can say that no economic system—whether centrally planned, market-directed, or a mix of the two—can achieve its objectives without an effective macro-marketing system. To see why this is true, we will look at the role of marketing in primitive societies. Then we will see how macro-marketing tends to become more and more complex in advanced economic systems.

Marketing involves exchange

In a **pure subsistence economy,** each family unit produces everything it consumes. There is no need to exchange goods and services. Each producer–consumer unit is totally self-sufficient, although usually its standard of living is relatively low. No marketing takes place because *marketing doesn't occur unless two or more parties are willing to exchange something for something else.*

What is a market?

The term *marketing* comes from the word **market**—which is a group of potential customers with similar needs who are willing to exchange something of value with sellers offering various goods and/or services—that is, ways of satisfying those needs. Of course, some negotiation may be needed. This can be done face-to-face at some physical location (for example, a farmers' market). Or it can be done indirectly—through a complex network that links middlemen, buyers, and sellers living far apart.

In primitive economies, exchanges tend to occur in central markets. **Central markets** are convenient places where buyers and sellers can meet one-on-one to

In advanced economies, a complex network of wholesalers, retailers, and other marketing specialists bring goods and services to consumers; in developing economies like Vietnam, central markets are often more basic.

exchange goods and services. In our information age, central markets take a variety of forms—ranging from suburban shopping centers to websites that operate in cyberspace. But you will understand macro-marketing better if you see how and why central markets develop. We'll start with a very simple case, but thinking about it will clarify what happens when a more complex system is involved.

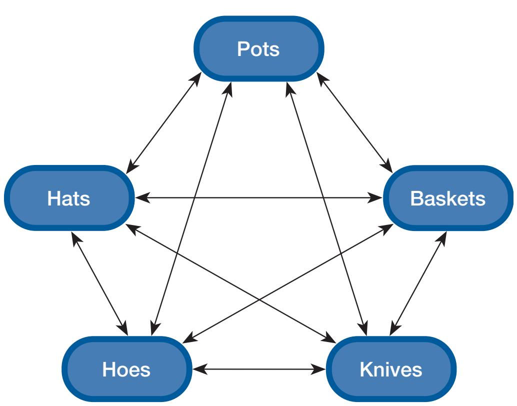
Central markets help exchange

Imagine a small village of five families—each with a special skill for producing some need-satisfying product. After meeting basic needs, each family decides to specialize. It's easier for one family to make two pots and another to make two baskets than for each one to make one pot and one basket. Specialization makes labor more efficient and more productive. It can increase the total amount of form utility created. Specialization also can increase the task utility in producing services, but for the moment we'll focus on products that are physical goods.

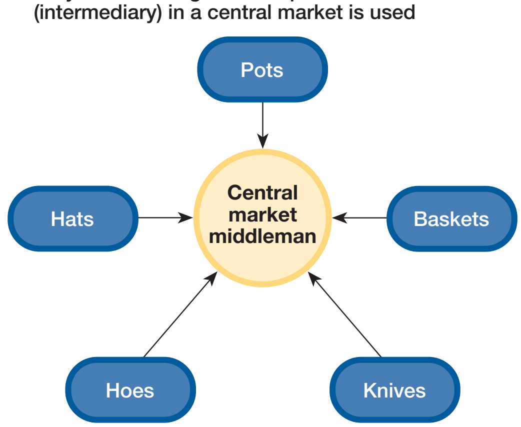
If these five families each specialize in one product, they will have to trade with each other. As Exhibit 1-2A shows, it will take the five families 10 separate exchanges to obtain some of each of the products. If the families live near each

Exhibit 1-2

A. Ten exchanges are required when a central market is not used



B. Only five exchanges are required when a middleman (intermediary) in a central market is used



www.mhhe.com/fourps

High-Tech Access to Market Information in the Low-Tech World

When consumers in the U.S. think about technology and marketing, many think about shopping on the Internet. After all, 135 million people in the U.S. have online access to the Internet. Fancy shopping malls seem old hat. Contrast that with Bangladesh, one of the poorest countries in the world, where about 90 percent of the 68,000 villages don't even have access to a phone. But Grameen Bank, a private firm based in Dhaka, Bangladesh, is doing something about that problem. It is making loans so that someone in a village can buy a cell phone and then provide phone service to others. For example, Delora Begum bought a phone and now reigns as the "phone lady" in her village. And her business is helping the market system work better. For example, farmers pay to use the cell phone to learn the fair value of their rice and vegetables; often in the past they were exploited because they did not get a fair price. One local businessman routinely had to take a two-hour bus ride to order furnace oil for his brick factory. Now he can just call and place an order—and save a bone-jarring half day on a bus. Similarly, a local carpenter uses the cell phone to check the current price for wood so that he can make a profit when he prices the chairs and cabinets he makes. These are just a few examples, but in a country with an extremely ineffective macro-marketing system the Grameen Bank's cell phone venture is doing a lot to improve the quality of life of people in remote villages.[9]

other, the exchange process is relatively simple. But if they are far apart, travel back and forth will take time. Who will do the traveling—and when?

Faced with this problem, the families may agree to come to a central market and trade on a certain day. Then each family makes only one trip to the market to trade with all the others. This reduces the total number of trips to five, which makes exchange easier, leaves more time for producing and consuming, and also provides for social gatherings.

A money system simplifies trading

While a central meeting place simplifies exchange, the individual bartering transactions still take a lot of time. Bartering only works when someone else wants what you have, and vice versa. Each trader must find others who have products of about equal value. After trading with one group, a family may find itself with extra baskets, knives, and pots. Then it has to find others willing to trade for these products.

A common money system changes all this. Sellers only have to find buyers who want their products and agree on the price. Then sellers are free to spend this income to buy whatever they want. If some buyers and sellers use *different* money systems—some use dollars and others use yen—they must also agree on the rate at which the money will be exchanged.

Middlemen intermediaries may help exchange even more

The development of a central market and a money system simplifies the exchange process among the five families in our imaginary village. But the families still need to make 10 separate transactions. So it still takes a lot of time and effort for the five families to exchange goods.

This clumsy exchange process is made much simpler by a **middleman** (or **intermediary**)—someone who specializes in trade rather than production. A middleman is willing to buy each family's goods and then sell each family whatever it needs. The middleman intermediary charges for this service, of course. But this charge may be more than offset by savings in time and effort.

In our simple example, using an intermediary at a central market reduces the necessary number of exchanges for all five families from 10 to 5. See Exhibit 1-2B. Each family has more time for production, consumption, and leisure. Also, each family can specialize in producing what it produces best—creating more form and task utility. Meanwhile, by specializing in trade, the intermediary provides additional time, place, and possession utility. In total, all the villagers may enjoy greater economic utility—and greater consumer satisfaction—by using an intermediary in the central market.

Note that the reduction in transactions that results from using an intermediary in a central market becomes more important as the number of families increases.

Intermediaries develop and offer specialized services that facilitate exchange between producers and customers.

For example, if the population of our imaginary village increases from 5 to 10 families, 45 transactions are needed without an intermediary. Using an intermediary requires only one transaction for each family.

Central market and intermediaries may develop in cyberspace

We've introduced the concept of a central market, the role of a money system for exchange, and the development of middlemen specialists by discussing a simple example in the context of a primitive society. But, you should realize that these same ideas are just as relevant in a modern society. Today, the intermediaries have permanent trading facilities and are known as *wholesalers* and *retailers*. In fact, the advantages of working with intermediaries multiply with increases in the number of producers and consumers, their distance from or difficulties in communicating with each other, and the number and variety of competing products. That is why there are so many wholesalers and retailers in modern economies.

On the other hand, technology is allowing some customers and some producers to meet for exchange in a central market that is located in "cyberspace"—that is, on the Internet—rather than in a mutually convenient geographic location. Computer systems developed by a new form of market specialist allow sellers and buyers to communicate and engage in exchange even if they are thousands of miles apart. In fact, the Internet makes it possible for sellers to hold auctions in which thousands of potential buyers from different parts of the world bid against each other to determine the price that will ultimately be paid for a good or service. Obviously, this is a very different type of central market, but it is important to see that it is simply a variation of the same basic idea. From a macro-marketing perspective, the main purpose of markets and market intermediaries is to make exchange easier and allow greater time for production, consumption, and other activities—including leisure.[10]

Internet

Internet Exercise eBay features a number of online auctions in which different sellers auction off computers, consumer electronics, and other products to buyers. Visit the eBay website (www.ebay.com) and review an open auction for a consumer electronics product. What are the advantages and disadvantages of this market for sellers? For buyers?

The Role of Marketing in Economic Development

Effective marketing system is necessary

Although it is tempting to conclude that more effective macro-marketing systems are the result of greater economic development, just the opposite is true. *An effective macro-marketing system is necessary for economic development*. Improved marketing is often the key to growth in less-developed nations.

Breaking the vicious circle of poverty

Without an effective macro-marketing system, many people in less-developed nations are not able to leave their subsistence way of life. They can't produce for the market because there are no buyers. And there are no buyers because everyone else is producing for their own needs. As a result, distribution systems and intermediaries do not develop.

Breaking this "vicious circle of poverty" may require major changes in the inefficient micro- and macro-marketing systems that are typical in less-developed nations. At the least, more market-oriented middlemen are needed to move surplus output to markets—including foreign markets—where there is more demand.[11]

Less-developed nations have inefficient systems

In Chapter 5 we will go into more detail on how countries at different levels of economic development differ. However, to get a sense for differences in macro-marketing systems, let's consider a case that involves India. This case also illustrates the links between the macro-marketing systems of countries at different stages of development.

Two-thirds of the over one billion people in India still live in rural farm areas. Many don't have life's basic comforts. For example, three out of four use wood as fuel to cook. Only about 40 percent have electricity, and less than 20 percent have piped water. Most can't afford a refrigerator. A person who works in the sugarcane fields, for example, only earns about $1 a day. Many rural Indians have never even held a tube of toothpaste. Rather, they clean their mouths with charcoal powder and the stem of a local plant.

Colgate is interested in introducing toothpaste in India, but it can't rely on U.S.-style ads—or the local drugstore—to do the selling job. Half of the rural population can't read, and very few have a TV. They also don't go to stores. Rather, once a week the men go to a central market in a nearby village to get basic supplies they can't grow themselves. To reach these people, Colgate sends a van that is equipped with a generator and video gear into a village on market day. Music attracts the shoppers, and then an entertaining half-hour video (infomercial) explains the benefits of using Colgate toothpaste. Of course, not many villagers can spend a day's wages to buy a standard tube. So Colgate offers a small (30 gram) tube for six rupees (about 18¢).

Colgate's micro-marketing effort in India is expensive because the macro-marketing system is ineffective. Colgate managers think that over the long run these efforts will pay off for the company. For now, they are paid for by Colgate's profits from more developed nations. So, you can see that it will take a long time before these villagers have basic comforts—or the type of efficient macro-marketing system—that those of us from the developed economies take for granted.[12]

Nations' Macro-Marketing Systems Are Connected

As a nation grows, its international trade grows

All countries trade to some extent—we live in an interdependent world. Trade expands as a country develops and industrializes. In fact, the largest changes in world trade are usually seen in rapidly developing economies. Over the last 20 years, for example, exports from China, India, and the "Four Dragons" (South Korea, Taiwan, Hong Kong, and Singapore) have risen dramatically and have fueled domestic economic growth at record levels.

Even so, the largest traders are highly developed nations. For example, the top industrial nations—the U.S., Canada, the countries of Western Europe, and Japan—account for about half of the world's total economic output, with the U.S. at about 23 percent, the countries of Western Europe at about 20 percent, and Japan at about 7 percent. These countries also account for about two-thirds of total world exports and about 63 percent of world imports. These statistics help you see why the U.S., Japan, and the countries of Western Europe are seen as the three economic superpowers presumably destined to compete for mastery in international markets on into the 21st century.[13]

Because trade among nations is so important in economic development, most countries—whether highly developed or not—are eager to be able to sell their goods and services in foreign markets. Yet at the same time they often don't want their local customers to spend cash on foreign-made products. They want the money—and the opportunities for jobs and economic growth—to stay in the local economy.

Tariffs and quotas may reduce trade

Taxes and restrictions at national or regional borders greatly reduce the free flow of goods and services between the macro-marketing systems of different countries. **Tariffs**—taxes on imported products—vary, depending on whether a country is trying to raise revenue or limit trade. Restrictive tariffs often block all movement. But even revenue-producing tariffs increase prices, discourage free movement of products, and cause red tape. This is what Caterpillar encounters trying to sell its construction equipment in Brazil. Brazil's 15 percent tariff adds nearly $40,000 to the cost of a $250,000 machine. Worse, Brazilian customs delays make it difficult for Caterpillar to honor its sales promise to deliver repair parts within 24 hours.[14]

Quotas act like restrictive tariffs. **Quotas** set the specific quantities of products that can move into or out of a country. Great market opportunities may exist in the markets of a unified Europe, for example, but import quotas (or export controls applied against a specific country) may discourage outsiders from entering.

The impact of such restrictions can be seen in the Russian market. At first it appeared that with the fall of communism, the Russian market would be more open to foreign automobile producers. However, big Russian import tariffs and taxes resulted in very high prices. For example, in 1997 a Taurus that sold for about $22,000 in the U.S. cost over $48,000 in Russia. Thus, the resulting high price severely limited the number of Russians who were willing or able to pay that much for a car. To get around this problem, Ford, Daewoo, and other producers decided to set up assembly plants in Russia.[15]

Trade restrictions can be a potential source of conflict between nations. For example, the U.S. government is hammering China for more access to its insurance, food, and telecommunications markets; China, in turn, complains about U.S. import quotas and tariffs on textiles. China isn't the only country affected. U.S. tariffs on textiles run as high as 30 percent.

As this suggests, the U.S. has held fast to some protectionist policies even though it is the world's cheerleader for free trade. U.S. consumers pay more for Florida orange juice because orange juice concentrate from groves in Brazil and other countries gets hit with a 30 percent tariff. Similarly, the U.S. is a big exporter of services, but Japanese and European airlines are not allowed to land in a U.S. city, pick up paying passengers, and fly to another U.S. destination.[16]

Markets may rely on international countertrade

To overcome the problems of trade restrictions, many firms have turned to **countertrade**—a special type of bartering in which products from one country are traded for products from another country. For example, McDonnell Douglas Helicopter turned to countertrade when the Ugandan government wanted to buy 18 helicopters to help stamp out illegal elephant hunting. Uganda didn't have $25 million to pay for the helicopters, so a countertrade specialist for the helicopter company set up local projects to generate the money. One Ugandan factory now turns local pineapples and passion fruit into concentrated juice. The concentrate is sold to European buyers identified by the countertrade specialist. Similarly, soft-drink bottlers in Mexico trade locally grown broccoli for Pepsi concentrate; then Pepsi finds a market for the broccoli in the U.S.

Distribution systems and middlemen intermediaries have not yet developed in these countries to handle this sort of exchange. So, in pursuing their own opportunities, companies like Pepsi and McDonnell Douglas are stimulating economic development. While deals such as this may seem unusual, that is not the case. Countertrade is becoming an extremely important part of foreign trade for both large and small companies. In fact, experts say that the use of countertrade doubled in the last decade. Now, about 20 to 25 percent of all U.S. exports rely on countertrade.[17]

Global trade is increasing

There are still many obstacles to free trade among nations. And trade "wars" among nations are likely to continue. Even so, the trend shows a slow movement toward fewer restrictions on trade among different countries. Perhaps the most visible evidence of this trend is the creation in 1995 of the **World Trade Organization (WTO)**—the only international body dealing with the rules of trade between nations. At its heart are the WTO agreements, the legal ground rules for international commerce and for trade policy. The agreements have three main objectives: (1) to help trade flow as freely as possible, (2) to provide an impartial means of settling disputes, and (3) to facilitate further negotiation. The WTO agreements in general try to encourage competition, discourage protectionism, and seek to provide more predictable policies.

Because each trade rule affects different countries in different ways, reaching agreements is a slow and complicated process. Even with the WTO in place, some people feel that there is more talk than change. Yet, progress is slowly being made. The WTO agreements cover services and intellectual property as well as goods; prior agreements were limited to goods. Thus, with the formation of the WTO global trade is becoming an even more important factor in economic development—and a more important source of opportunity for individual firms.[18]

Internet

Internet Exercise The World Trade Organization is a very important force behind the global move toward free trade, but sometimes there are still disputes. Go to the WTO website (www.wto.org) and find out how the WTO settles disputes. Do you think that this procedure favors the developed nations, the less-developed nations, or neither? Give your thinking.

Can Mass Production Satisfy a Society's Consumption Needs?

Urbanization brings together large numbers of people. They must depend on others to produce most of the goods and services they need to satisfy their basic needs. Also, in advanced economies, many consumers have higher discretionary incomes. They can afford to satisfy higher-level needs as well as basic ones. A modern economy faces a real challenge to satisfy all these needs.

Economies of scale mean lower cost

Fortunately, advanced economies can often take advantage of mass production with its **economies of scale**—which means that as a company produces larger numbers of a particular product, the cost for each of these products goes down. You can

Most consumers who drink tea live far from where it is grown. To overcome this spatial separation, someone must first perform a variety of marketing functions, like standardizing and grading the tea leaves, transporting and storing them, and buying and selling them.

see that a one-of-a-kind, custom-built car would cost much more than a mass-produced standard model.

Of course, even in advanced societies, not all goods and services can be produced by mass production or with economies of scale. Consider medical care. It's difficult to get productivity gains in labor-intensive medical services—like brain surgery. Nevertheless, from a macro-marketing perspective, it is clear that we are able to devote resources to meeting these "quality-of-life" needs because we are achieving efficiency in other areas.

Thus, modern production skills can help provide great quantities of goods and services to satisfy large numbers of consumers. But mass production alone does not solve the problem of satisfying consumers' needs. We also need effective marketing.

Effective marketing is needed to link producers and consumers

Effective marketing means delivering the goods and services that consumers want and need. It means getting products to them at the right time, in the right place, and at a price they're willing to pay. It means keeping consumers satisfied after the sale, and bringing them back to purchase again when they are ready. That's not an easy job—especially if you think about the variety of goods and services a highly developed economy can produce and the many kinds of goods and services consumers want.

Effective marketing in an advanced economy is more difficult because producers and consumers are often separated in several ways. As Exhibit 1-3 shows, exchange between producers and consumers is hampered by spatial separation, separation in time, separation of information and values, and separation of ownership. "Discrepancies of quantity" and "discrepancies of assortment" further complicate exchange between producers and consumers. That is, each producer specializes in producing and selling large amounts of a narrow assortment of goods and services, but each consumer wants only small quantities of a wide assortment of goods and services.[19]

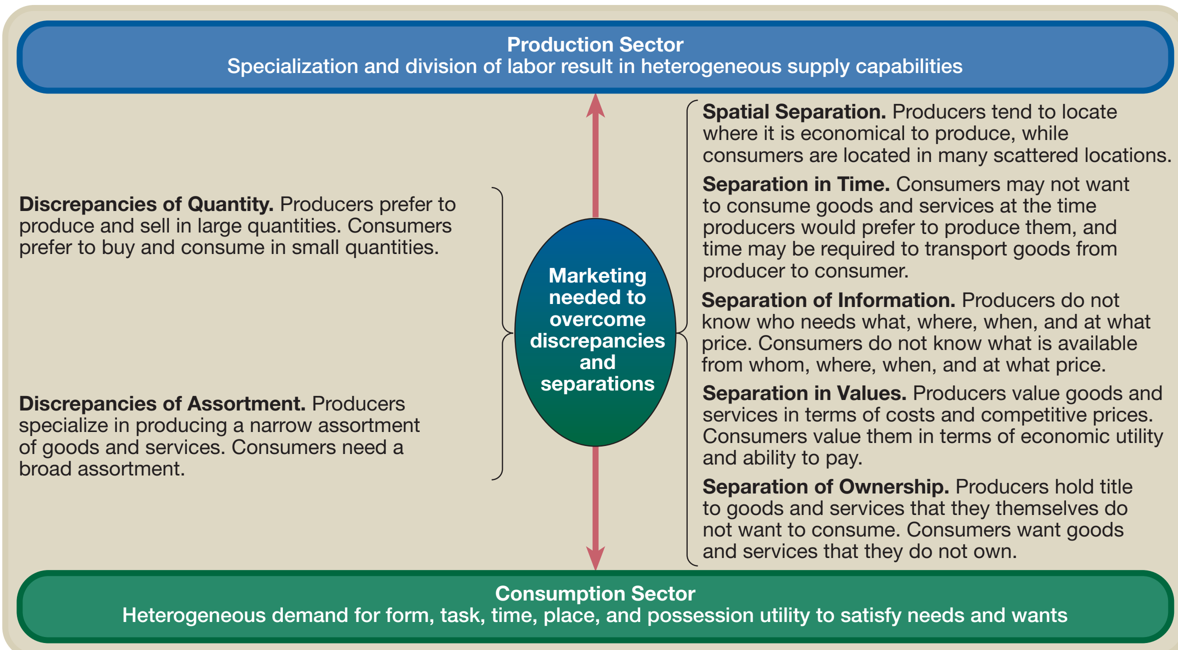
Marketing functions help narrow the gap

The purpose of a macro-marketing system is to overcome these separations and discrepancies. The "universal functions of marketing" help do this.

The **universal functions of marketing** are: buying, selling, transporting, storing, standardization and grading, financing, risk taking, and market information. They must be performed in all macro-marketing systems. *How* these functions are performed—and *by whom*—may differ among nations and economic systems. But they are needed in any macro-marketing system. Let's take a closer look at them now.

Exchange usually involves buying and selling. The **buying function** means looking for and evaluating goods and services. The **selling function** involves promoting the product. It includes the use of personal selling, advertising, and other direct and mass-selling methods. This is probably the most visible function of marketing.

Exhibit 1-3 Marketing Facilitates Production and Consumption



The **transporting function** means the movement of goods from one place to another. The **storing function** involves holding goods until customers need them.

Standardization and grading involve sorting products according to size and quality. This makes buying and selling easier because it reduces the need for inspection and sampling. **Financing** provides the necessary cash and credit to produce, transport, store, promote, sell, and buy products. **Risk taking** involves bearing the uncertainties that are part of the marketing process. A firm can never be sure that customers will want to buy its products. Products can also be damaged, stolen, or outdated. The **market information function** involves the collection, analysis, and distribution of all the information needed to plan, carry out, and control marketing activities, whether in the firm's own neighborhood or in a market overseas.

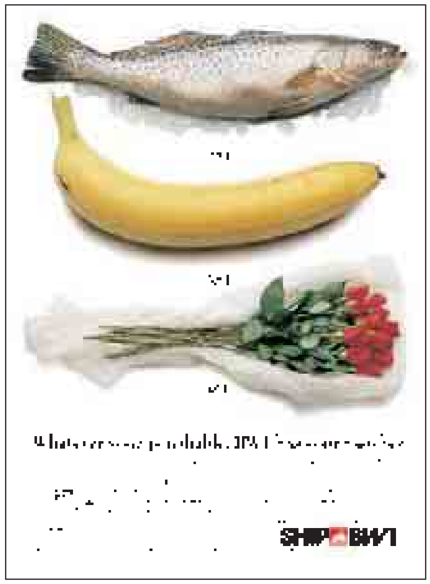
Who Performs Marketing Functions?

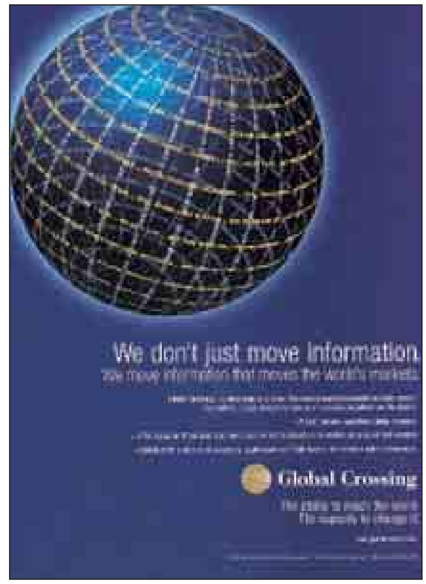
Producers, consumers, and marketing specialists

From a macro-level viewpoint, these marketing functions are all part of the marketing process and must be done by someone. None of them can be eliminated. In a planned economy, some of the functions may be performed by government agencies. Others may be left to individual producers and consumers. In a market-directed system, marketing functions are performed by producers, consumers, and a variety of marketing specialists (see Exhibit 1-4). Regardless of who performs the marketing functions, in general they must be performed effectively or the performance of the whole macro-marketing system will suffer.

Keep in mind that the macro-marketing systems for different nations may interact. For example, producers based in one nation may serve consumers in another country, perhaps with help from intermediaries and other specialists from both countries. What happened to food distribution in East Germany after the fall of the

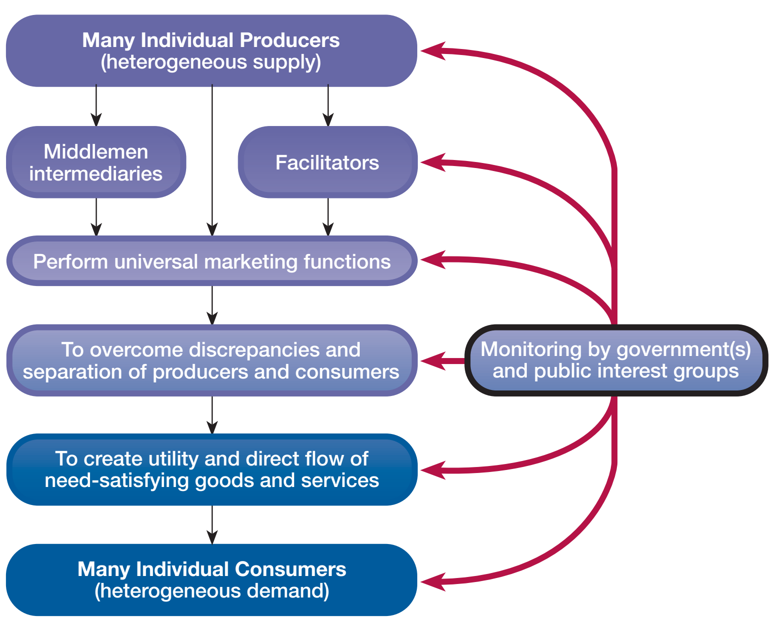
Facilitators—including the delivery firms that handle perishable cargo at Baltimore/Washington International Airport and Internet service providers like Global Crossing—may help a marketing manager with one or more of the marketing functions.





Berlin Wall illustrates this point. With the reunification of Germany, the political limits on trade were gone. Yet consumers still faced problems getting the food they wanted. Eastern Germany had no efficient wholesalers to supply the chain of 170 Konsum retail stores, which were previously state-owned. And it was expensive for producers in the West who wanted to reach the market in the East to do it without help. However, the Tegut grocery chain in the West saw the opportunity and quickly did something about it. Tegut established an automated warehouse in the East to supply the Konsum stores. The warehouse made it economical to assemble needed assortments of products from many different producers. Further, Tegut set up a computer network to provide timely reordering from the warehouse, online

Exhibit 1-4
Model of a Market-Directed Macro-Marketing System



management of inventories and distribution, and even payment control. With the help of middlemen like Tegut, both local and foreign producers are better able to meet consumer needs.[20]

Specialists perform some functions

Earlier in the chapter you saw how producers and consumers can benefit when a middleman takes over some buying and selling. The Tegut example shows that producers and consumers also benefit when marketing specialists perform the other marketing functions. In fact, we find marketing functions being performed not only by middlemen but also by a variety of other **facilitators**—firms that provide one or more of the marketing functions other than buying or selling. These include advertising agencies, marketing research firms, independent product-testing laboratories, Internet service providers, public warehouses, transporting firms, communications companies, and financial institutions (including banks). Through specialization or economies of scale, marketing intermediaries and facilitators are often able to perform the marketing functions better—and at a lower cost—than producers or consumers can. This allows producers and consumers to spend more time on production and consumption.

Functions can be shifted and shared

From a macro viewpoint, all of the marketing functions must be performed by someone. But *from a micro viewpoint, not every firm must perform all of the functions. Further, not all goods and services require all the functions at every level of their production.* "Pure services"—like a plane ride—don't need storing, for example. But storing is required in the production of the plane and while the plane is not in service.

Some marketing specialists perform all the functions. Others specialize in only one or two. Marketing research firms, for example, specialize only in the market information function. Further, technology may make a certain function easier to perform. For example, the buying process may require that a customer first identify relevant sellers and where they are. Even though that might be accomplished quickly and easily on the Internet, the function hasn't been cut out. The important point to remember is this: *Responsibility for performing the marketing functions can be shifted and shared in a variety of ways, but no function can be completely eliminated.*

How Well Does Our Macro-Marketing System Work?

It connects remote producers and consumers

A macro-marketing system does more than just deliver goods and services to consumers—it allows mass production with its economies of scale. Also, mass communication, computer information systems, including the Internet, and mass transportation allow products to be shipped where they're needed. Oranges from California are found in Minnesota stores—even in December—and electronic parts made in Taiwan are used in making products all over the world.[21]

It encourages growth and new ideas

In addition to making mass production possible, a market-directed, macro-marketing system encourages **innovation**—the development and spread of new ideas and products. Competition for consumers' money forces firms to think of new and better ways of satisfying consumer needs. And the competition that marketing fosters drives down prices and gives consumers more choices and a higher standard of living.

Macro-marketing system is becoming more efficient

In combination, the forces of competition and the choices made by customers to support those firms that do the best job of meeting their needs drive our macro-marketing system to be more efficient.

Some changes come quickly. A good example is the speed with which firms have adopted e-commerce. **E-commerce** refers to exchanges between individuals or

A market-directed, macro-marketing system encourages marketing managers to develop innovative ways to meet customers' needs.

organizations—and activities that facilitate those exchanges—based on applications of information technology. The technology-mediated exchanges fostered by e-commerce are helping to cut costs from almost every aspect of marketing while at the same time helping firms to better satisfy their customers. Collectively, these developments have had a significant impact on the efficiency of our macro-marketing system. For example, most experts believe that the growth of the U.S. economy during the last decade, coupled with low levels of price increases (inflation), is due to the fact that e-commerce has helped sellers reduce costs.

Throughout this text we will detail the many ways in which e-commerce is increasing the efficiency and effectiveness of different areas of marketing. On the other hand, keep in mind that the upward trend in the macro-marketing system does not ensure a successful outcome for any individual firm or its customers. The headlines of the past few years provide ample evidence of this. Many individual dot-com firms—companies established to do business over the Internet—failed. These companies were started by people who thought they had come up with "a better mousetrap," but customers didn't always see it that way. These failures are expensive, and ultimately that expense is shared by members of the society. That's because money spent on a business that fails—that does not make a positive contribution to the macro-marketing system—could have had a positive effect if it was spent more wisely in some other way. So, it is important to see that if individual managers make poor decisions it may affect many people. Throughout this text we will be focusing on how managers can make better decisions—to improve both micro-marketing performance and the performance of the whole macro-marketing system.

Marketing has its critics

In explaining marketing's role in society, we described some of the benefits of a market-directed macro-marketing system. We can see this in the macro-marketing system of the United States. It provides—at least in material terms—one of the highest standards of living in the world. It seems to be "effective" and "fair" in many ways.

We must admit, however, that marketing—as it exists in the United States and other developed societies—has many critics. Marketing activity is especially open to criticism because it is the part of business most visible to the public. There is nothing like a pocketbook issue for getting consumers excited!

Marketing has its critics, including those who express concern that advertising is too pervasive in all aspects of our lives.

A number of typical complaints about marketing are summarized in Exhibit 1-5. Think about these criticisms and whether you agree with them or not. What complaints do you have that are not covered by one of the categories in Exhibit 1-5?

Such complaints cannot and should not be taken lightly. They show that many people aren't happy with some parts of the marketing system. Certainly, the strong public support for consumer protection laws proves that not all consumers feel they are being treated like royalty.

As you consider the various criticisms of marketing, keep in mind that some of them deal with the marketing practices of specific firms and are micro-marketing oriented. Others are really criticisms of the whole macro-marketing system. This is an important distinction.[22]

Is it an ethical issue?

Certainly some complaints about marketing arise because some individual firm or manager was intentionally unethical and cheated the market. But at other times, problems and criticism may arise because a manager did not fully consider the ethical implications of a decision. In either case, there is no excuse for sloppiness when it comes to **marketing ethics**—the moral standards that guide marketing decisions and actions. Each individual develops moral standards based on his or her own values. That helps explain why opinions about what is right or wrong often vary from one person to another, from one society to another, and among different groups

Exhibit 1-5 Sample Criticisms of Marketing

- Advertising is everywhere, and it's often annoying, misleading, or wasteful.
- The quality of products is poor and often they are not even safe.
- There are too many unnecessary products.
- Packaging and labeling are often confusing and deceptive.
- Middlemen add too much to the cost of distribution and just raise prices without providing anything in return.
- Marketing serves the rich and exploits the poor.
- Service stinks, and when a consumer has a problem nobody cares.
- Marketing creates interest in products that pollute the environment.
- Private information about consumers is collected and used to sell them things they don't want.
- Marketing makes people too materialistic and motivates them toward "things" instead of social needs.
- Easy consumer credit makes people buy things they don't need and can't afford.

within a society. It is sometimes difficult to say whose opinions are "correct." Even so, such opinions may have a very real influence on whether an individual's (or a firm's) marketing decisions and actions are accepted or rejected. So marketing ethics are not only a philosophical issue, they are also a pragmatic concern. Throughout the text we will be discussing the types of ethical issues individual marketing managers face. But we won't be moralizing and trying to tell you how you should think on any given issue. Rather, by the end of the course we hope that *you* will have some firm personal opinions about what is and is not ethical in micro-marketing activities.[23]

Keep in mind, however, that not all criticisms of marketing focus on ethical issues; fortunately, the prevailing practice of most businesspeople is to be fair and honest. Moreover, not all criticisms are specific to the micro-marketing activities of individual firms. Some of the complaints about marketing really focus on the basic idea of a market-directed macro-marketing system—and these criticisms often occur because people don't understand what marketing is—or how it works. As you go through this book, we'll discuss some of these criticisms. Then in our final chapter, we will return to a more complete appraisal of marketing in our consumer-oriented society.

Conclusion

In this chapter, we defined two levels of marketing: micro-marketing and macro-marketing. Macro-marketing is concerned with the way the whole global economy works. Micro-marketing focuses on the activities of individual firms. We discussed the role of marketing in economic development and the functions of marketing and who performs them. We ended by raising some of the criticisms of marketing—both of the whole macro system and of the way individual firms work.

We emphasized macro-marketing in this chapter, but the major thrust of this book is on micro-marketing. By learning more about market-oriented decision making, you will be able to make more efficient and socially responsible decisions. This will help improve the performance of individual firms and organizations (your employers). And eventually, it will help our macro-marketing system work better.

We'll see marketing through the eyes of the marketing manager—maybe *you* in the near future. And we will show how you can contribute to the marketing process. Along the way, we'll discuss the impact of micro-level decisions on society, and the ethical issues that marketing managers face. Then in Chapter 22—after you have had time to understand how and why producers and consumers think and behave the way they do—we will evaluate how well both micro-marketing and macro-marketing perform in a market-directed economic system.

Questions and Problems

1. List your activities for the first two hours after you woke up this morning. Briefly indicate how marketing affected your activities.
2. It is fairly easy to see why people do not beat a path to a mousetrap manufacturer's door, but would they be similarly indifferent if some food processor developed a revolutionary new food product that would provide all necessary nutrients in small pills for about $100 per year per person?
3. If a producer creates a really revolutionary new product and consumers can learn about it and purchase it at a website on the Internet, is any additional marketing effort really necessary? Explain your thinking.
4. Distinguish between macro- and micro-marketing. Then explain how they are interrelated, if they are.
5. Distinguish between how economic decisions are made in a planned economic system and how they are made in a market-directed economy.
6. A committee of the American Marketing Association defined marketing as "the process of planning

and executing the conception, pricing, promotion, and distribution of ideas, goods, and services to create exchanges that satisfy individual and organizational objectives." Does this definition consider macro-marketing? Explain your answer.

7. Identify a "central market" in your city and explain how it facilitates exchange.
8. Identify a website on the Internet that serves as a "central market" for some type(s) of good(s) or service(s). Give the address (www.____.____) of the website and briefly explain the logic of your choice.
9. Explain why tariffs and quotas affect international marketing opportunities.
10. Discuss the nature of marketing in a socialist economy. Would the functions that must be provided and the development of wholesaling and retailing systems be any different from those in a market-directed economy?
11. Discuss how the micro-macro dilemma relates to each of the following products: high-powered engines in cars, nuclear power, bank credit cards, and pesticides that improve farm production.
12. Describe a recent purchase you made. Indicate why that particular product was available at a store and, in particular, at the store where you bought it.
13. Refer to Exhibit 1-3, and give an example of a purchase you made recently that involved separation of information and separation in time between you and the producer. Briefly explain how these separations were overcome.
14. Online computer shopping at websites on the Internet makes it possible for individual consumers to get direct information from hundreds of companies they would not otherwise know about. Consumers can place an order for a purchase that is then shipped to them directly. Will growth of these services ultimately eliminate the need for retailers and wholesalers? Explain your thinking, giving specific attention to what marketing functions are involved in these "electronic purchases" and who performs them.
15. Define the functions of marketing in your own words. Using an example, explain how they can be shifted and shared.
16. Explain, in your own words, why this text emphasizes micro-marketing.
17. Explain why a small producer might want a marketing research firm to take over some of its information-gathering activities.
18. Explain why a market-directed macro-marketing system encourages innovation. Give an example.

Suggested Cases

1. McDonald's "Seniors" Restaurant
4. Bidwell Carpet Cleaning, Inc.

Computer-Aided Problem

1. **Revenue, Cost, and Profit Relationships**

This problem introduces you to the computer-aided problem (CAP) software—which is on the CD that accompanies this text—and gets you started with the use of spreadsheet analysis for marketing decision making. This problem is simple. In fact, you could work it without the software. But by starting with a simple problem, you will learn how to use the program more quickly and see how it will help you with more complicated problems. Instructions for the software are available at the end of this text.

Sue Cline, the business manager at Magna University Student Bookstore, is developing plans for the next academic year. The bookstore is one of the university's nonprofit activities, but any "surplus" (profit) it earns is used to support the student activities center.

Two popular products at the bookstore are the student academic calendar and notebooks with the school name. Sue Cline thinks that she can sell calendars to 90 percent of Magna's 3,000 students, so she has had 2,700 printed. The total cost, including artwork and printing, is $11,500. Last year the calendar sold for $5.00, but Sue is considering changing the price this year.

Sue thinks that the bookstore will be able to sell 6,000 notebooks if they are priced right. But she knows that many students will buy similar notebooks (without the school name) from stores in town if the bookstore price is too high.

Sue has entered the information about selling price, quantity, and costs for calendars and notebooks in the spreadsheet program so that it is easy to evaluate the effect of different decisions. The spreadsheet is also set up to calculate revenue and profit, based on

$$\text{Revenue} = (\text{Selling price}) \times (\text{Quantity sold})$$

$$\text{Profit} = (\text{Revenue}) - (\text{Total cost})$$

Use the program to answer the questions below. Record your answers on a separate sheet of paper.

a. From the Spreadsheet Screen, how much revenue does Sue expect from calendars? How much revenue from notebooks? How much profit will the store earn from calendars? From notebooks?

b. If Sue increases the price of her calendars to $6.00 and still sells the same quantity, what is the expected revenue? The expected profit? (Note: Change the price from $5.00 to $6.00 on the spreadsheet and the program will recompute revenue and profit.) On your sheet of paper, show the calculations that confirm that the program has given you the correct values.

c. Sue is interested in getting an overview of how a change in the price of notebooks would affect revenue and profit, assuming that she sells all 6,000 notebooks she is thinking of ordering. Prepare a table—on your sheet of paper—with column headings for three variables: selling price, revenue, and profit. Show the value for revenue and profit for different possible selling prices for a notebook—starting at a minimum price of $1.60 and adding 8 cents to the price until you reach a maximum of $2.40. At what price will selling 6,000 notebooks contribute $5,400.00 to profit? At what price would notebook sales contribute only $1,080.00? (Hint: Use the What If analysis feature to compute the new values. Start by selecting "selling price" for notebooks as the value to change, with a minimum value of $1.60 and a maximum value of $2.40. Select the revenue and profit for notebooks as the values to display.)

For additional questions related to this problem, see Exercise 1-4 in the *Learning Aid for Use with Basic Marketing*, 14th edition.

When You Finish This Chapter, You Should

1. Know what the marketing concept is—and how it should affect strategy planning in a firm or nonprofit organization.

2. Understand what customer value is and why it is important to customer satisfaction.

3. Understand what a marketing manager does.

4. Know what marketing strategy planning is—and why it will be the focus of this book.

5. Understand target marketing.

6. Be familiar with the four Ps in a marketing mix.

7. Know the difference between a marketing strategy, a marketing plan, and a marketing program.

8. Understand the important new terms (shown in red).

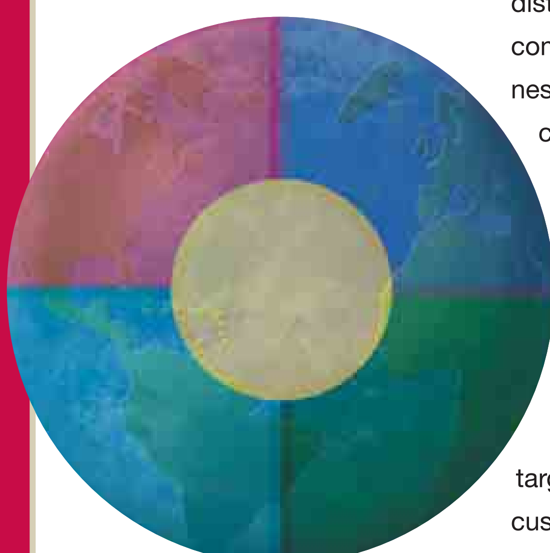
Chapter Two

Marketing's Role within the Firm or Nonprofit Organization

As you saw in Chapter 1, marketing and marketing management are important in our society—and in business firms and nonprofit organizations. To get you thinking about the marketing strategy planning ideas we will be developing in this chapter and the rest of the book, let's consider Dell Computers.

As a freshman in college, Michael Dell started buying and reselling computers from his dorm room. At that time, the typical marketing mix for PCs emphasized distribution through specialized computer stores that sold to business users and some final consumers. Often the dealers' service quality didn't justify the high prices they charged, the features of the PCs they had in stock didn't match what customers wanted, and repairs were a hassle.

Dell decided there was a target market of price-conscious customers who would respond to a



place price promotion produc

different marketing mix. He used direct-response advertising in computer magazines—and customers called a toll-free number to order a computer with the exact features they wanted. Dell built computers to match the specific orders that came in and used UPS to quickly ship orders directly to the customer. Prices were low, too—because the direct channel meant there was no retailer markup and the build-to-order approach reduced inventory costs. This approach also kept Dell in constant contact with customers. Problems could be identified quickly and corrected. Dell also implemented the plan well—with constant improvements—to make good on its promise of reliable machines and superior service. For example, Dell pioneered a system of guaranteed on-site service—within 24 hours. Dell also set up ongoing programs to train all employees to work together to please customers.

Of course, it's hard to satisfy everyone all of the time. For example, profits fell when Dell's laptop design didn't measure up. Customers simply didn't see them as a good value. However, smart marketers learn from and fix mistakes. Dell quickly got its product line back on the bull's eye.

As sales grew, Dell put more money into advertising. Its ad agency crafted ads to position Dell in consumers' minds as an aggressive, value-oriented source of computers. At the same time, Dell added a direct sales force to call on big government and corporate buyers—because they expected in-person selling and a relationship, not just a telephone contact. And when these important customers said they wanted Dell to offer high-power machines to run their corporate networks, Dell put money into R&D to create what they needed.

price place promotion product

Dell also saw the prospect for international growth. Many firms moved into Europe by exporting. But Dell set up its own operations there. Dell knew it would be tough to win over skeptical European buyers. They had never bought big-ticket items such as PCs on the phone. Yet, in less than five years, sales in Europe grew to 40 percent of Dell's total revenue and Dell pushed into Asian markets for more growth. That also posed challenges, so Dell's advertising manager invited major ad agencies to make presentations on how Dell could be more effective with its $80 million global advertising campaign.

By the mid 1990s, other firms were trying to imitate Dell's direct-order approach. For example, IBM set up Ambra, a direct-sales division. However, the retailers who were selling the bulk of IBM's computers were not happy about facing price competition from their own supplier! So IBM couldn't simply copy Dell's strategy. It was in conflict with the rest of IBM's marketing program.

As computer prices fell, many firms were worried about how to cope with slim profits. But Dell saw an opportunity for profitable growth by extending its direct model to a website (www.dell.com) that was recently generating about $1.5 billion in sales each month! Moreover, online selling lowered expenses and reduced supply and inventory costs. For example, when a customer ordered a PC produced in one factory and a monitor produced in another, the two pieces were brought together enroute to the customer. This cost cutting proved to be especially important when the economy softened and demand for PCs fell off. Building on its strengths, Dell cut prices in what many competitors saw as an "irrational" price war. But the design of Dell's website and sales system allowed it to charge different prices to different segments to match demand with supply. For example, high-margin laptops were priced lower to educational customers—to stimulate demand—than to government buyers who were less price sensitive. Similarly, if the supply of 17-inch monitors fell short, Dell could use an online promotion for 19-inch monitors and shift demand. To create more profit opportunities from its existing customers, Dell also put more emphasis on selling extended-care service agreements.

Clearly, the growth of the PC market is tapering off. That means that Dell's future profits will depend even more heavily on careful strategy planning. But perhaps Dell can continue to find new ways to satisfy customers' PC-related needs—or even identify other new, high-growth opportunities to pursue.[1]

We've mentioned only a few of many decisions marketing managers at Dell had to make in developing marketing strategies, but you can see that each of these decisions affects the others. Further, making marketing decisions is never easy and strategies may need to change. Yet, knowing what basic decision areas to consider helps you to plan a more successful strategy. This chapter will get you started by giving you a framework for thinking about all the marketing management decision areas—which is what the rest of this book is all about.

Marketing’s Role Has Changed a Lot Over the Years

From our Dell case, it’s clear that marketing decisions are very important to a firm’s success. But marketing hasn’t always been so complicated. In fact, understanding how marketing thinking has evolved makes the modern view clearer. So, we will discuss five stages in marketing evolution: (1) the simple trade era, (2) the production era, (3) the sales era, (4) the marketing department era, and (5) the marketing company era. We’ll talk about these eras as if they applied generally to all firms—but keep in mind that *some managers still have not made it to the final stages*. They are stuck in the past with old ways of thinking.

Specialization permitted trade—and middlemen met the need

When societies first moved toward some specialization of production and away from a subsistence economy where each family raised and consumed everything it produced, traders played an important role. Early “producers for the market” made products that were needed by themselves and their neighbors. (Recall the five-family example in Chapter 1.) As bartering became more difficult, societies moved into the **simple trade era**—a time when families traded or sold their “surplus” output to local middlemen. These specialists resold the goods to other consumers or distant middlemen. This was the early role of marketing—and it is still the focus of marketing in many of the less-developed areas of the world. In fact, even in the United States, the United Kingdom, and other more advanced economies, marketing didn’t change much until the Industrial Revolution brought larger factories a little over a hundred years ago.

Customer satisfaction isn’t always a life and death matter as it can be with Bell’s bike helmets, but over time firms that can’t satisfy their customers don’t survive.

From the production to the sales era

From the Industrial Revolution until the 1920s, most companies were in the production era. The **production era** is a time when a company focuses on production of a few specific products—perhaps because few of these products are available in the market. "If we can make it, it will sell" is management thinking characteristic of the production era. Because of product shortages, many nations—including China and many of the post-communist republics of Eastern Europe—continue to operate with production era approaches.

By about 1930, most companies in the industrialized Western nations had more production capability than ever before. Now the problem wasn't just to produce—but to beat the competition and win customers. This led many firms to enter the sales era. The **sales era** is a time when a company emphasizes selling because of increased competition.

To the marketing department era

For most firms in advanced economies, the sales era continued until at least 1950. By then, sales were growing rapidly in most areas of the economy. The problem was deciding where to put the company's effort. Someone was needed to tie together the efforts of research, purchasing, production, shipping, and sales. As this situation became more common, the sales era was replaced by the marketing department era. The **marketing department era** is a time when all marketing activities are brought under the control of one department to improve short-run policy planning and to try to integrate the firm's activities.

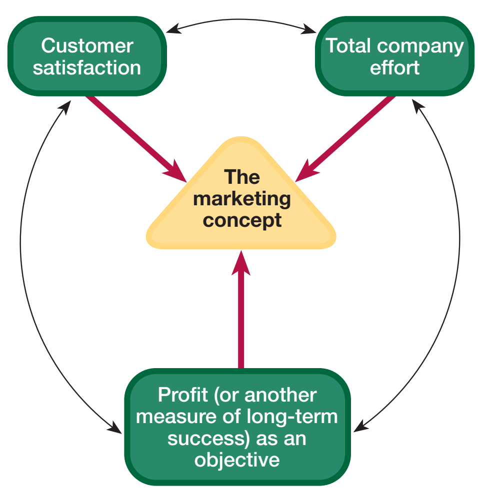
To the marketing company era

Since 1960, most firms have developed at least some staff with a marketing management outlook. Many of these firms have even graduated from the marketing department era into the marketing company era. The **marketing company era** is a time when, in addition to short-run marketing planning, marketing people develop long-range plans—sometimes five or more years ahead—and the whole company effort is guided by the marketing concept.

What Does the Marketing Concept Mean?

The **marketing concept** means that an organization aims *all* its efforts at satisfying its *customers*—at a profit. The marketing concept is a simple but very important idea. See Exhibit 2-1.

Exhibit 2-1
Organizations with a Marketing Orientation Carry Out the Marketing Concept



Ford Motor Company has a program, called Consumer Insight Experience, in which thousands of individual Ford customers have met with Ford employees from different departments to give them a deeper understanding of consumer wants and needs.

The marketing concept is not a new idea—it's been around for a long time. But some managers act as if they are stuck at the beginning of the production era—when there were shortages of most products. They show little interest in customers' needs. These managers still have a **production orientation**—making whatever products are easy to produce and *then* trying to sell them. They think of customers existing to buy the firm's output rather than of firms existing to serve customers and—more broadly—the needs of society.

Well-managed firms have replaced this production orientation with a marketing orientation. A **marketing orientation** means trying to carry out the marketing concept. Instead of just trying to get customers to buy what the firm has produced, a marketing-oriented firm tries to offer customers what they need.

Three basic ideas are included in the definition of the marketing concept: (1) customer satisfaction, (2) a total company effort, and (3) profit—not just sales—as an objective. These ideas deserve more discussion.

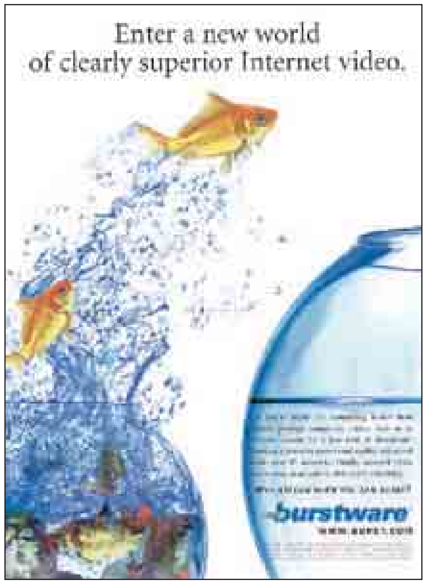
Customer satisfaction guides the whole system

"Give the customers what they need" seems so obvious that it may be hard for you to see why the marketing concept requires special attention. However, people don't always do the logical and obvious—especially when it means changing what they've done in the past. In a typical company 35 years ago, production managers thought mainly about getting out the product. Accountants were interested only in balancing the books. Financial people looked after the company's cash position. And salespeople were mainly concerned with getting orders for whatever product was in the warehouse. Each department thought of its own activity as the center of the business—with others working around "the edges." No one was concerned with the whole system. As long as the company made a profit, each department went merrily on—doing its own thing. Unfortunately, this is still true in many companies today.

Work together to do a better job

Ideally, all managers should work together as a team because the output from one department may be the input to another. And every department may directly or indirectly impact short-term and long-term customer satisfaction. But some managers tend to build "fences" around their own departments. There may be meetings to try to get them to work together—but they come and go from the meetings worried only about protecting their own turf.

We use the term *production orientation* as a shorthand way to refer to this kind of narrow thinking—and lack of a central focus—in a business firm. But keep in mind that this problem may be seen in sales-oriented sales representatives, advertising-oriented agency people, finance-oriented finance people, directors of nonprofit organizations, and so on. It is not a criticism of people who manage production. They aren't necessarily any more guilty of narrow thinking than anyone else.



Firms that adopt the marketing concept want consumers and others in the channel of distribution to know that they provide superior customer value.

The fences come down in an organization that has accepted the marketing concept. There may still be departments because specialization often makes sense. But the total system's effort is guided by what customers want—instead of what each department would like to do.

In Chapter 20, we'll go into more detail on the relationship between marketing and other functions. Here, however, you should see that the marketing concept provides a guiding focus that *all* departments adopt. It should be a philosophy of the whole organization, not just an idea that applies to the marketing department.

Survival and success require a profit

Firms must satisfy customers, or the customers won't continue to "vote" for the firm's survival and success with their money. But a manager must also keep in mind that it may cost more to satisfy some needs than any customers are willing to pay. Or, it may be much more costly to try to attract new customers than it is to build a strong relationship with—and repeat purchases from—existing customers. So profit—the difference between a firm's revenue and its total costs—is the bottom-line measure of the firm's success and ability to survive. It is the balancing point that helps the firm determine what needs it will try to satisfy with its total (sometimes costly!) effort.

Adoption of the Marketing Concept Has Not Been Easy or Universal

The marketing concept was first accepted by consumer products companies such as General Electric and Procter & Gamble. Competition was intense in their markets—and trying to satisfy customers' needs more fully was a way to win in this competition. Widespread publicity about the success of the marketing concept at these companies helped spread the message to other firms.[2]

Producers of industrial commodities—steel, coal, paper, glass, and chemicals—have accepted the marketing concept slowly if at all. Similarly, many traditional retailers have been slow to accept the marketing concept.

Service industries are catching up

Service industries—including airlines, power and telephone companies, banks, investment firms, lawyers, physicians, accountants, and insurance companies—were slow to adopt the marketing concept, too. But in recent years this has changed dramatically. This is partly due to changes in government regulations that forced many of these businesses to be more competitive.

Banks used to be open for limited hours that were convenient for bankers—not customers. Many closed during lunch hour! But now financial services are less regulated, and banks compete with companies like Fidelity Investments and BMW (the car company!) for checking accounts and retirement investments. Banks have ATMs or branches in grocery stores and other convenient places. They stay open longer, often during evenings and on Saturdays. They also offer more services, like banking over the Internet or a "personal banker" to give financial advice. Most banks aggressively promote their special services.[3]

It's easy to slip into a production orientation

The marketing concept seems so logical that you would think that most firms would have adopted it. But this isn't the case. Many firms are still production-oriented. Even firms that try to embrace the marketing concept can easily slip back into a production-oriented way of thinking. For example, a busy manager at a retail store might send the signal that a consumer with a complaint is a big inconvenience or "impossible to please." You've probably had that happen, even when all you wanted was for the store to deliver on its promises.

Problems also occur because some manager has a clever idea for a new offering and the firm rushes to bring it to market—rather than first finding out if it will fill an unsatisfied need or if it can be offered at a profit. Many firms in high-technology businesses fall into this trap. They think that technology is the source of their success. They forget that technology is only a means to meet customer needs and that ultimately profits come from satisfying customers. In recent years, thousands of new dot-com firms failed for these reasons. They may have had a vision of what the technology could do, but they didn't stop to figure out all that it would take to satisfy customers or make a profit. Imagine how parents felt when eToys.com failed to deliver online purchases of Christmas toys on time. If you had that experience, would you ever shop there again? What would you tell others?

Take a look at Exhibit 2-2. It shows some differences in outlook between adopters of the marketing concept and typical production-oriented managers. As the exhibit suggests, the marketing concept—if taken seriously—is really very powerful. It forces the company to think through what it is doing—and why. And it motivates the company to develop plans for accomplishing its objectives.

The Marketing Concept and Customer Value

Take the customer's point of view

A manager who adopts the marketing concept sees customer satisfaction as the path to profits. And to better understand what it takes to satisfy a customer, it's useful to take the customer's point of view.

A customer may look at a market offering from two perspectives. One deals with the potential benefits of that offering; the other concerns what the customer has to give up to get those benefits. For example, consider a student who has just finished an exam and is thinking about getting a cup of Mocha Latte from Starbucks. Our coffee lover might see this as a great-tasting snack, a personal reward, a quick pick-me-up, and even as a way to break the ice and get to know an attractive classmate. Clearly, there are different needs associated with these different benefits. The cost of getting these benefits would include the price of the coffee and any tip, but there might be other nondollar costs as well. For example, how far it is to the Starbucks and how difficult it will be to park are convenience costs. Slow service would be an aggravation. And you might worry about another kind of cost if the professor whose exam you have the next day sees you "wasting time" at Starbucks.

Exhibit 2-2 Some Differences in Outlook between Adopters of the Marketing Concept and the Typical Production-Oriented Managers

Topic	Marketing Orientation	Production Orientation
Attitudes toward customers	Customer needs determine company plans.	They should be glad we exist, trying to cut costs and bringing out better products.
An Internet website	A new way to serve customers.	If we have a website customers will flock to us.
Product offering	Company makes what it can sell.	Company sells what it can make.
Role of marketing research	To determine customer needs and how well company is satisfying them.	To determine customer reaction, if used at all.
Interest in innovation	Focus on locating new opportunities.	Focus is on technology and cost cutting.
Importance of profit	A critical objective.	A residual, what's left after all costs are covered.
Role of packaging	Designed for customer convenience and as a selling tool.	Seen merely as protection for the product.
Inventory levels	Set with customer requirements and costs in mind.	Set to make production more convenient.
Focus of advertising	Need-satisfying benefits of products and services.	Product features and how products are made.
Role of sales force	Help the customer to buy if the product fits customer's needs, while coordinating with rest of firm.	Sell the customer, don't worry about coordination with other promotion efforts or rest of firm.
Relationship with customer	Customer satisfaction before and after sale leads to a profitable long-run relationship.	Relationship is seen as short term—ends when a sale is made.
Costs	Eliminate costs that do not give value to customer.	Keep costs as low as possible.

Customer value reflects benefits and costs

As this example suggests, both benefits and costs can take many different forms, perhaps ranging from economic to emotional. They also may vary depending on the situation. However, it is the customer's view of the various benefits and costs that is important. And combining these two perspectives leads us to the concept of **customer value**—the difference between the benefits a customer sees from a market offering and the costs of obtaining those benefits. A consumer is likely to be more satisfied when the customer value is higher—when benefits exceed costs by a larger margin. On the other hand, a consumer who sees the costs as greater than the benefits isn't likely to become a customer.

Some people think that low price and high customer value are the same thing. But, you can see that may not be the case at all. To the contrary, a good or service that doesn't meet a consumer's needs results in low customer value, even if the price is very low. Yet, a high price may be more than acceptable when it obtains the desired benefits. Think again about our Starbucks example. You can get a cup of coffee for a much lower price, but Starbucks offers more than *just* a cup of coffee.

Customer may not think about it very much

It's useful for a manager to evaluate ways to improve the benefits, or reduce the costs, of what the firm offers customers. However, this doesn't mean that customers stop and compute some sort of customer value score before making each purchase. If they did, there wouldn't be much time in life for anything else. So, a manager's objective and thorough analysis may not accurately reflect the customer's

Many marketers are looking for ways to build long-term relationships with customers. For example, Payless Shoes gets the relationship off on the right foot by offering new parents a free pair of baby shoes. Williams-Sonoma offers a free online bridal registry, which builds relationships with newlyweds, a key target market.

impressions. Yet, it is the customer's view that matters—even when the customer has not thought about it.

Where does competition fit?

You can't afford to ignore competition. Consumers usually have choices about how they will meet their needs. So, a firm that offers superior customer value is likely to win and keep customers. This may be crucial when what different firms have to offer is very similar.

Some critics say that the marketing concept does not go far enough in today's highly competitive markets. They think of marketing as "warfare" for customers—and argue that a marketing manager should focus on competitors, not customers. That view, however, misses the point. Often the best way to improve customer value, and beat the competition, is to be first to find and satisfy a need that others have not even considered.

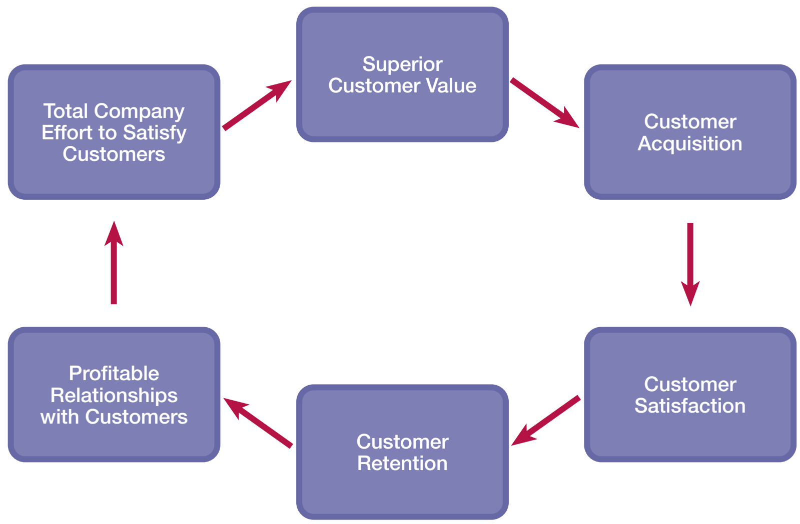
The competition between Pepsi and Coke illustrates this. Coke and Pepsi were spending millions of dollars on promotion—fighting head-to-head for the same cola customers. They put so much emphasis on the cola competition that they missed other opportunities. That gave firms like Snapple the chance to enter the market and steal away customers. For these customers, the desired benefits—and the greatest customer value—came from the variety of a fruit-flavored drink, not from one more cola.

Build relationships with customer value

Firms that embrace the marketing concept seek ways to build a profitable long-term relationship with each customer. This is an important idea. Even the most innovative firm faces competition sooner or later. And trying to get new customers by taking them away from a competitor is usually more costly than retaining current customers by really satisfying their needs. Satisfied customers buy again and again. This makes their buying job easier, and it also increases the selling firm's profits.

Building mutually beneficial relationships with customers requires that everyone in an organization work together to provide customer value before *and after* each purchase. If there is a problem with a customer's bill, the accounting people can't just leave it to the salesperson to straighten it out or, even worse, act like it's "the customer's problem." Rather, it's the firm's problem. The long-term relationship with the customer—and the lifetime value of the customer's future purchases—is threatened if the accountant, the salesperson, and anyone else who might be involved

Exhibit 2-3
Satisfying Customers with Superior Customer Value to Build Profitable Relationships



don't work together quickly to make things right for the customer. Similarly, the firm's advertising people can't just develop ads that try to convince a customer to buy once. If the firm doesn't deliver on the benefits promised in its ads, the customer is likely to go elsewhere the next time the need arises. And the same ideas apply whether the issue is meeting promised delivery dates, resolving warranty problems, giving a customer help on how to use a product, or even making it easy for the customer to return a purchase made in error.

In other words, any time the customer value is reduced—because the benefits to the customer decrease or the costs increase—the relationship is weakened.[4]

Exhibit 2-3 summarizes the important ideas we've been discussing. In a firm that has adopted the marketing concept everyone focuses on customer satisfaction. They offer superior customer value. That helps attract customers in the first place—and keeps them satisfied after they buy. Because customers are satisfied, they want to purchase from the firm again. The ongoing relationship with customers is profitable, so the firm is encouraged to continue to find new and better ways to offer superior customer value. In other words, when a firm adopts the marketing concept, it wins and so do its customers.

L. L. Bean delivers superior value

L. L. Bean illustrates these ideas. It is a firm that builds enduring relationships with its customers. It offers good customer value to consumers who are interested in enjoying the outdoors. Bean's quality products are well suited to a wide variety of outdoor needs—whether it's clothing for hikers or equipment for campers. The firm field-tests all its products—to be certain they live up to the firm's "100% satisfaction" guarantee. Although Bean operates a retail store in Freeport, Maine, its Internet website (www.llbean.com) and catalogs reach customers all over the world. Bean's computers track what each customer is buying, so new catalogs are mailed directly to the people who are most interested. To make ordering convenient, customers can call toll-free 24 hours a day—and they get whatever advice they need because the salespeople are real experts on what they sell. Bean also makes it easy for consumers to return a product, and encourages them to complain about any problem. That way, Bean can solve the problem before it disrupts the relationship. Bean's prices are competitive with other outdoor sporting specialty stores, but Bean retains its loyal customers because they like the benefits of the relationship.[5]

Internet

Internet Exercise The L. L. Bean website (www.llbean.com) offers consumers a lot of information, including an "Outdoors Online" section with information about national parks. Do you think that this helps Bean to build relationships with its target customers?

The Marketing Concept Applies in Nonprofit Organizations

Newcomers to marketing thinking

The marketing concept is as important for nonprofit organizations as it is for business firms. However, prior to 1970 few people in nonprofits paid attention to the role of marketing. Now marketing is widely recognized as applicable to all sorts of public and private nonprofit organizations—ranging from government agencies, health care organizations, educational institutions, and religious groups to charities, political parties, and fine arts organizations. Some nonprofit organizations operate just like a business. For example, there may be no practical difference between the gift shop at a museum and a for-profit shop located across the street. And some unprofitable dot-com firms have now resurfaced as nonprofits. On the other hand, some nonprofits differ from business firms in a variety of ways.

Support may not come from satisfied "customers"

As with any business firm, a nonprofit organization needs resources and support to survive and achieve its objectives. Yet support often does not come directly from those who receive the benefits the organization produces. For example, the World Wildlife Fund protects animals. If supporters of the World Wildlife Fund are not satisfied with its efforts—don't think the benefits are worth what it costs to provide them—they will, and should, put their time and money elsewhere.

Just as most firms face competition for customers, most nonprofits face competition for the resources and support they need. The Air Force faces a big problem if it can't attract new recruits. A shelter for the homeless may fail if supporters decide to focus on some other cause, such as AIDS education. A community theater group that decides to do a play that the actors and the director like—never stopping to consider what the audience might want to see—may find that the theater is empty.

What is the "bottom line"?

As with a business, a nonprofit must take in as much money as it spends or it won't survive. However, a nonprofit organization does not measure "profit" in the same way as a firm. And its key measures of long-term success are also different. The YMCA, colleges, symphony orchestras, and the post office, for example, all seek to achieve different objectives and need different measures of success.

Profit guides business decisions because it reflects both the costs and benefits of different activities. In a nonprofit organization, it is sometimes more difficult to be objective in evaluating the benefits of different activities relative to what

Marketing is now widely accepted by many nonprofit organizations, including the National Kidney Foundation, which wants to increase the number of organ donors.

they cost. However, if everyone in an organization agrees to *some* measure of long-run success, it helps serve as a guide to where the organization should focus its efforts.

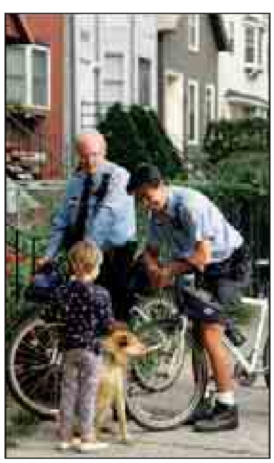
May not be organized for marketing

Some nonprofits face other challenges in organizing to adopt the marketing concept. Often no one has overall responsibility for marketing activities. A treasurer or accountant may keep the books, and someone may be in charge of "operations"—but marketing may somehow seem less crucial, especially if no one understands what marketing is all about. Even when some leaders do the marketing thinking, they may have trouble getting unpaid volunteers with many different interests to all agree with the marketing strategy. Volunteers tend to do what they feel like doing!

The marketing concept provides focus

We have been discussing some of the differences between nonprofit and business organizations. However, the marketing concept is helpful in *any* type of organization. Success is most likely when everyone pulls together to strive for common objectives that can be achieved with the available resources. Adopting the marketing concept helps to bring this kind of focus. After all, each organization is trying to satisfy some group of consumers in some way.[6]

Nonprofits achieve objectives by satisfying needs



A simple example shows how marketing thinking helped a small town reduce robberies. Initially the chief of police asked the town manager for a larger budget—for more officers and patrol cars. Instead of a bigger budget, the town manager suggested a different approach. She put two officers in charge of a community watch program. They helped neighbors to organize and notify the police of any suspicious situations. They also set up a program to engrave ID numbers on belongings. And new signs warned thieves that a community watch was in effect. Break-ins all but stopped—without increasing the police budget. What the town *really* needed was more effective crime prevention—not just more police officers.

Throughout this book, we'll be discussing the marketing concept and related ideas as they apply in many different settings. Often we'll simply say "in a firm" or "in a business"—but remember that most of the ideas can be applied in *any* type of organization.

The Marketing Concept, Social Responsibility, and Marketing Ethics

Society's needs must be considered

The marketing concept is so logical that it's hard to argue with it. Yet when a firm focuses its efforts on satisfying some consumers—to achieve its objectives—there may be negative effects on society. (Remember that we discussed this micro–macro dilemma in Chapter 1.) This means that marketing managers should be concerned with **social responsibility**—a firm's obligation to improve its positive effects on society and reduce its negative effects. Being socially responsible sometimes requires difficult trade-offs.

Consider, for example, the environmental problems created by CFCs, chemicals used in hundreds of critical products including fire extinguishers, cooling systems, and electronic circuit boards. We now know that CFCs deplete the earth's ozone layer. Yet when this was learned it was not possible to immediately stop producing and using all CFCs. For many products critical to society, there was no feasible short-term substitute for CFCs. Du Pont and other producers of CFCs worked hard to balance these conflicting demands. Yet you can see that there are no easy answers for how such conflicts should be resolved.[7]

The issue of social responsibility in marketing also raises other important questions—for which there are no easy answers.

Should all consumer needs be satisfied?

Some consumers want products that may not be safe or good for them in the long run. Some critics argue that businesses should not offer high-heeled shoes, alcoholic beverages, sugar-coated cereals, diet soft drinks, and many processed foods because they aren't "good" for consumers in the long run.

Similarly, bicycles and roller blades are among the most dangerous products identified by the Consumer Product Safety Commission. Should Schwinn stop production? What about skis, mopeds, and scuba equipment? Who should decide if these products will be offered to consumers? Is this a micro-marketing issue or a macro-marketing issue?

What if it cuts into profits?

Being more socially conscious often seems to lead to positive customer response. For example, many Wal-Mart customers praise the company as a "safe haven" for kids to shop because it does not carry "stickered" CDs (those with a warning label stating that the content might not be suitable for children), lewd videos, plastic guns that look authentic, and video games judged to be too violent. Green Mountain Power has had a very good response to electric power produced with less pollution (even though the price is higher). And some consumers buy only from firms that certify that their overseas factories don't rely on child labor.[8]

Yet as the examples above show, there are times when being socially responsible conflicts with a firm's profit objective. Concerns about such conflicts have prompted critics to raise the basic question: Is the marketing concept really desirable?

Many socially conscious marketing managers are trying to resolve this problem. Their definition of customer satisfaction includes long-range effects—as well as immediate customer satisfaction. They try to balance consumer, company, *and* social interests.

You too will have to make choices that balance these social concerns—either in your role as a consumer or as a manager in a business firm. So throughout the text we will be discussing many of the social issues faced by marketing management.

The marketing concept guides marketing ethics

Organizations that have adopted the marketing concept are concerned about marketing ethics as well as broader issues of social responsibility. It is simply not possible for a firm to be truly consumer-oriented and at the same time intentionally unethical.

Exhibit 2-4 Code of Ethics, American Marketing Association

CODE OF ETHICS

Members of the American Marketing Association (AMA) are committed to ethical professional conduct. They have joined together in subscribing to this Code of Ethics embracing the following topics:

Responsibilities of the Marketer

Marketers must accept responsibility for the consequences of their activities and make every effort to ensure that their decisions, recommendations, and actions function to identify, serve, and satisfy all relevant publics: customers, organizations and society.

Marketers' professional conduct must be guided by:

1. The basic rule of professional ethics: not knowingly to do harm;
2. The adherence to all applicable laws and regulations;
3. The accurate representation of their education, training and experience; and
4. The active support, practice and promotion of this Code of Ethics.

Honesty and Fairness

Marketers shall uphold and advance the integrity, honor, and dignity of the marketing profession by:

1. Being honest in serving consumers, clients, employees, suppliers, distributors and the public;
2. Not knowingly participating in conflict of interest without prior notice to all parties involved; and
3. Establishing equitable fee schedules including the payment or receipt of usual, customary and/or legal compensation for marketing exchanges.

Rights and Duties of Parties in the Marketing Exchange Process

Participants in the marketing exchange process should be able to expect that:

1. Products and services offered are safe and fit for their intended uses;
2. Communications about offered products and services are not deceptive;
3. All parties intend to discharge their obligations, financial and otherwise, in good faith; and
4. Appropriate internal methods exist for equitable adjustment and/or redress of grievances concerning purchases.

It is understood that the above would include, but is not limited to, the following responsibilities of the marketer:

In the area of product development and management,

- disclosure of all substantial risks associated with product or service usage;
- identification of any product component substitution that might materially change the product or impact on the buyer's purchase decision;
- identification of extra-cost added features.

In the area of promotions,

- avoidance of false and misleading advertising;
- rejection of high pressure manipulations, or misleading sales tactics;
- avoidance of sales promotions that use deception or manipulation.

In the area of distribution,

- not manipulating the availability of a product for purpose of exploitation;
- not using coercion in the marketing channel;
- not exerting undue influence over the reseller's choice to handle a product.

In the area of pricing,

- not engaging in price fixing;
- not practicing predatory pricing;
- disclosing the full price associated with any purchase.

In the area of marketing research,

- prohibiting selling or fund raising under the guise of conducting research;
- maintaining research integrity by avoiding misrepresentation and omission of pertinent research data;
- treating outside clients and suppliers fairly.

Organizational Relationships

Marketers should be aware of how their behavior may influence or impact on the behavior of others in organizational relationships. They should not demand, encourage or apply coercion to obtain unethical behavior in their relationships with others, such as employees, suppliers or customers.

1. Apply confidentiality and anonymity in professional relationships with regard to privileged information;
2. Meet their obligations and responsibilities in contracts and mutual agreements in a timely manner;
3. Avoid taking the work of others, in whole, or in part, and represent this work as their own or directly benefit from it without compensation or consent of the originator or owner;
4. Avoid manipulation to take advantage of situations to maximize personal welfare in a way that unfairly deprives or damages the organization or others.

Any AMA member found to be in violation of any provision of this Code of Ethics may have his or her Association membership suspended or revoked.

Individual managers in an organization may have different values. As a result, problems may arise when someone does not share the same marketing ethics as others in the organization. One person operating alone can damage a firm's reputation and even survival. Because the marketing concept involves a companywide focus, it is a foundation for marketing ethics common to everyone in a firm—and helps to avoid such problems.

To be certain that standards for marketing ethics are as clear as possible, many organizations have developed their own written codes of ethics. Consistent with the marketing concept, these codes usually state—at least at a general level—the ethical standards that everyone in the firm should follow in dealing with customers and other people. Many professional societies have also adopted such codes. For example, the American Marketing Association's code of ethics—see Exhibit 2-4—sets specific ethical standards for many aspects of the management job in marketing.[9]

The Management Job in Marketing

Now that you know about the marketing concept—a philosophy to guide the whole firm—let's look more closely at how a marketing manager helps a firm to achieve its objectives. The marketing manager is a manager, so let's look at the marketing management process.

The **marketing management process** is the process of (1) *planning* marketing activities, (2) directing the *implementation* of the plans, and (3) *controlling* these plans. Planning, implementation, and control are basic jobs of all managers—but here we will emphasize what they mean to marketing managers.

Exhibit 2-5 shows the relationships among the three jobs in the marketing management process. The jobs are all connected to show that the marketing management process is continuous. In the planning job, managers set guidelines for the implementing job—and specify expected results. They use these expected results in the control job—to determine if everything has worked out as planned. The link from the control job to the planning job is especially important. This feedback often leads to changes in the plans—or to new plans.

Marketing managers should seek new opportunities

Marketing managers cannot be satisfied just planning present activities. Markets are dynamic. Consumers' needs, competitors, and the environment keep changing. Consider Parker Brothers, a company that seemed to have a "Monopoly" in family games. While it continued selling board games, firms like Sega and Nintendo zoomed in with video game competition. Of course, not every opportunity is good for every company. Really attractive opportunities are those that fit with what the whole company wants to do and is able to do well.

Strategic management planning concerns the whole firm

The job of planning strategies to guide a whole company is called **strategic (management) planning**—the managerial process of developing and maintaining a match between an organization's resources and its market opportunities. This is a top-management job. It includes planning not only for marketing but also for production, finance, human resources, and other areas. In Chapter 20, we'll look at links between marketing and these areas.

Although marketing strategies are not whole-company plans, company plans should be market-oriented. And the marketing plan often sets the tone and direction for the whole company. So we will use *strategy planning* and *marketing strategy planning* to mean the same thing.[10]

Exhibit 2-5
The Marketing Management Process

What Is Marketing Strategy Planning?

Marketing strategy planning means finding attractive opportunities and developing profitable marketing strategies. But what is a "marketing strategy"? We have used these words rather casually so far. Now let's see what they really mean.

What is a marketing strategy?

A **marketing strategy** specifies a target market and a related marketing mix. It is a big picture of what a firm will do in some market. Two interrelated parts are needed:

1. A **target market**—a fairly homogeneous (similar) group of customers to whom a company wishes to appeal.
2. A **marketing mix**—the controllable variables the company puts together to satisfy this target group.

Exhibit 2-6
A Marketing Strategy

The importance of target customers in this process can be seen in Exhibit 2-6, where the customer—the "C"—is at the center of the diagram. The customer is surrounded by the controllable variables that we call the "marketing mix." A typical marketing mix includes some product, offered at a price, with some promotion to tell potential customers about the product, and a way to reach the customer's place.

The Learning Company's marketing strategy for its software aims at a specific group of target customers: young parents who have a computer at home and want their kids to learn while playing. The strategy calls for a variety of educational software products—like *Reader Rabbit* and *Where in the World Is Carmen Sandiego?* The firm's software is designed with entertaining graphics and sound, and it's tested on kids to be certain that it is easy to use. To make it convenient for target customers to buy the software, it can be ordered from the firm's own website (www.learningco.com) or from other retailers like Babbages. Promotion has helped build customer interest in the software. For example, when marketing managers released *Where in Time Is Carmen Sandiego?* they not only placed ads in family-oriented computer magazines but also sent direct-mail flyers to registered customers of the firm's other products. Some firms sell less-expensive games for kids, but parents are loyal to The

Learning Co. because it caters to their needs and offers first-class customer service—including a 90-day, no-questions-asked guarantee that assures the buyer of good customer value.[11]

Selecting a Market-Oriented Strategy Is Target Marketing

Target marketing is not mass marketing

Note that a marketing strategy specifies some *particular* target customers. This approach is called "target marketing" to distinguish it from "mass marketing." **Target marketing** says that a marketing mix is tailored to fit some specific target customers. In contrast, **mass marketing**—the typical production-oriented approach—vaguely aims at "everyone" with the same marketing mix. Mass marketing assumes that everyone is the same—and it considers everyone to be a potential customer. It may help to think of target marketing as the "rifle approach" and mass marketing as the "shotgun approach." See Exhibit 2-7.

Mass marketers may do target marketing

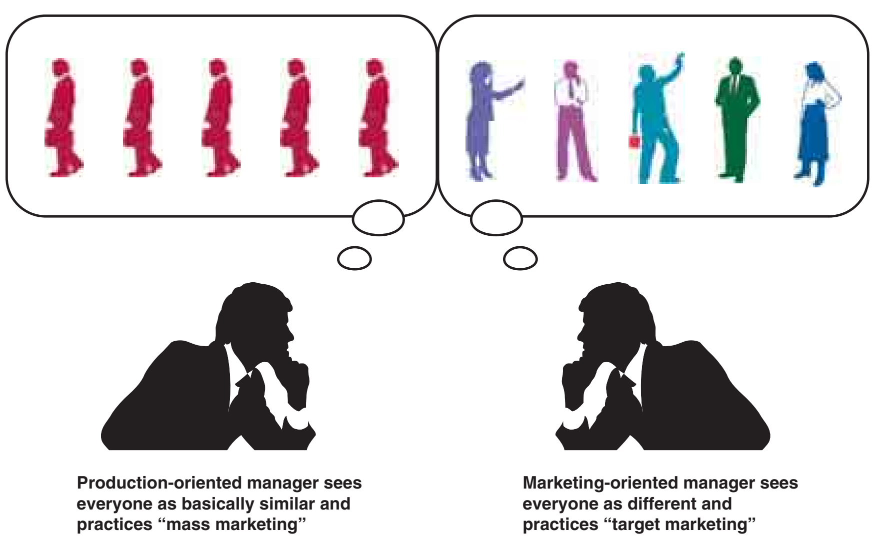
Commonly used terms can be confusing here. The terms *mass marketing* and *mass marketers* do not mean the same thing. Far from it! *Mass marketing* means trying to sell to "everyone," as we explained above. *Mass marketers* like Kraft Foods and Wal-Mart are aiming at clearly defined target markets. The confusion with mass marketing occurs because their target markets usually are large and spread out.

Target marketing can mean big markets and profits

Target marketing is not limited to small market segments—only to fairly homogeneous ones. A very large market—even what is sometimes called the "mass market"—may be fairly homogeneous, and a target marketer will deliberately aim at it. For example, a very large group of parents of young children are homogeneous on many dimensions—including their attitudes about changing baby diapers. In the United States alone, this group spends about $3.5 billion a year on disposable diapers—so it should be no surprise that it is a major target market for companies like Kimberly-Clark (Huggies) and Procter & Gamble (Pampers).

The basic reason to focus on some specific target customers is to gain a competitive advantage—by developing a more satisfying marketing mix that should also be more profitable for the firm. For example, Tianguis, a small grocery chain in Southern

Exhibit 2-7
Production-Oriented and Marketing-Oriented Managers Have Different Views of the Market



California, attracts Hispanic customers with special product lines and Spanish-speaking employees. E*trade uses an Internet site (www.etrade.com) to target knowledgeable investors who want a convenient, low-cost way to buy and sell stocks online without a lot of advice (or pressure) from a salesperson.

Developing Marketing Mixes for Target Markets

There are many marketing mix decisions

There are many possible ways to satisfy the needs of target customers. A product might have many different features. Customer service levels before or after the sale can be adjusted. The package, brand name, and warranty can be changed. Various advertising media—newspapers, magazines, cable, the Internet—may be used. A company's own sales force or other sales specialists can be used. The price can be changed, discounts can be given, and so on. With so many possible variables, is there any way to help organize all these decisions and simplify the selection of marketing mixes? The answer is yes.

The four "Ps" make up a marketing mix

It is useful to reduce all the variables in the marketing mix to four basic ones:

Product.
Place.
Promotion.
Price.

It helps to think of the four major parts of a marketing mix as the "four Ps." Exhibit 2-8 emphasizes their relationship and their common focus on the customer—"C."

Exhibit 2-8
A Marketing Strategy—Showing the Four Ps of a Marketing Mix

Customer is not part of the marketing mix

The customer is shown surrounded by the four Ps in Exhibit 2-8. Some students assume that the customer is part of the marketing mix—but this is not so. The customer should be the *target* of all marketing efforts. The customer is placed in the center of the diagram to show this. The C stands for some specific customers—the target market.

Exhibit 2-9 shows some of the strategy decision variables organized by the four Ps. These will be discussed in later chapters. For now, let's just describe each P briefly.

Product—the good or service for the target's needs

The Product area is concerned with developing the right "product" for the target market. This offering may involve a physical good, a service, or a blend of both. Keep in mind that Product is not limited to "physical goods." For example, the Product of H & R Block is a completed tax form. The Product of a political party is the set of causes it will work to achieve. The important thing to remember is that your good and/or service should satisfy some customers' needs.

Along with other Product-area decisions like branding, packaging, and warranties, we will talk about developing and managing new products and whole product lines.

Place—reaching the target

Place is concerned with all the decisions involved in getting the "right" product to the target market's Place. A product isn't much good to a customer if it isn't available when and where it's wanted.

A product reaches customers through a channel of distribution. A **channel of distribution** is any series of firms (or individuals) who participate in the flow of products from producer to final user or consumer.

Exhibit 2-9
Strategy Decision Areas Organized by the Four Ps

Product	Place	Promotion	Price
Physical good	Objectives	Objectives	Objectives
Service	Channel type	Promotion blend	Flexibility
Features	Market exposure	Salespeople	Level over product life cycle
Benefits	Kinds of middlemen	Kind	Geographic terms
Quality level	Kinds and locations of stores	Number	Discounts
Accessories	How to handle transporting and storing	Selection	Allowances
Installation	Service levels	Training	
Instructions	Recruiting middlemen	Motivation	
Warranty	Managing channels	Advertising	
Product lines		Targets	
Packaging		Kinds of ads	
Branding		Media type	
		Copy thrust	
		Prepared by whom	
		Sales promotion	
		Publicity	

Sometimes a channel system is quite short. It may run directly from a producer to a final user or consumer. This is especially common in business markets and in the marketing of services. The channel is direct when a producer uses an online website to handle orders by target customers, whether the customer is a final consumer or an organization. So, direct channels have become much more common since the development of the Internet.

On the other hand, often the channel system is much more complex—involving many different retailers and wholesalers. See Exhibit 2-10 for some examples. When a marketing manager has several different target markets, several different channels of distribution may be needed.

We will also see how physical distribution service levels and decisions concerning logistics (transporting, storing, and handling products) relate to the other Place decisions and the rest of the marketing mix.

A firm's product may involve a physical good, a service, or a combination of both.

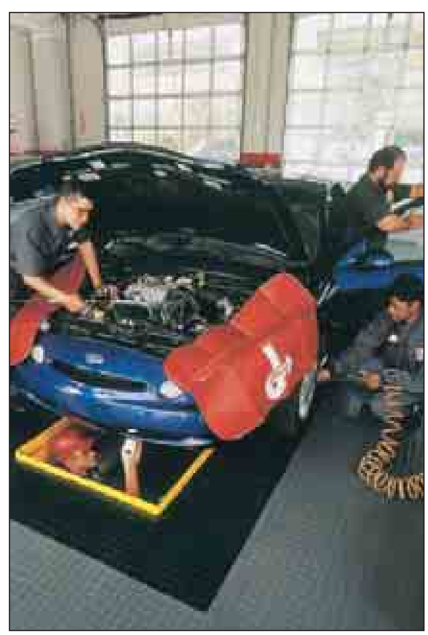
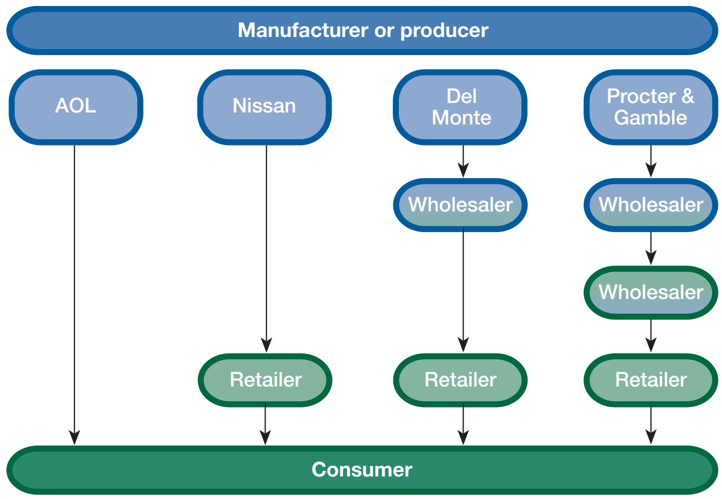


Exhibit 2-10
Four Examples of Basic Channels of Distribution for Consumer Products



Promotion—telling and selling the customer

The third P—Promotion—is concerned with telling the target market or others in the channel of distribution about the "right" product. Sometimes promotion is focused on acquiring new customers, and sometimes it's focused on retaining current customers. Promotion includes personal selling, mass selling, and sales promotion. It is the marketing manager's job to blend these methods of communication.

Personal selling involves direct spoken communication between sellers and potential customers. Personal selling usually happens face-to-face, but sometimes the communication occurs over the telephone. Personal selling lets the salesperson adapt the firm's marketing mix to each potential customer. But this individual attention comes at a price; personal selling can be very expensive. Often this personal effort has to be blended with mass selling and sales promotion.

Mass selling is communicating with large numbers of customers at the same time. The main form of mass selling is **advertising**—any *paid* form of nonpersonal presentation of ideas, goods, or services by an identified sponsor. **Publicity**—any *unpaid* form of nonpersonal presentation of ideas, goods, or services—is another important form of mass selling. Mass selling may involve a wide variety of media, ranging from newspapers and billboards to the Internet.

Sales promotion refers to those promotion activities—other than advertising, publicity, and personal selling—that stimulate interest, trial, or purchase by final customers or others in the channel. This can involve use of coupons, point-of-purchase materials, samples, signs, catalogs, novelties, and circulars.

Price—making it right

In addition to developing the right Product, Place, and Promotion, marketing managers must also decide the right Price. Price setting must consider the kind of competition in the target market and the cost of the whole marketing mix. A manager must also try to estimate customer reaction to possible prices. Besides this, the manager must know current practices as to markups, discounts, and other terms of sale. And if customers won't accept the Price, all of the planning effort is wasted.

Each of the four Ps contributes to the whole

All four Ps are needed in a marketing mix. In fact, they should all be tied together. But is any one more important than the others? Generally speaking, the answer is no—all contribute to one whole. When a marketing mix is being developed, all (final) decisions about the Ps should be made at the same time. That's why the four Ps are arranged around the customer (C) in a circle—to show that they all are equally important.

Lifetime Value of Customers Can Be Very High—or Very Low

Investors lost millions when stock market values of dot-com firms collapsed after an initial, frenzied run up. But why did values get so high in the first place, especially when most dot-coms were not yet profitable? The stock went up because many investors expected that the firms would earn profits in the future as more consumers went online and the early dot-coms accumulated customers. These hopes were fueled by dot-coms that made optimistic predictions about the lifetime value of the customers they were acquiring. The lifetime value of the customer concept is not new. For decades General Motors has known that a consumer who buys a GM car and is satisfied is likely to buy another one the next time. If that happens again and again, over a lifetime the happy customer would spend $250,000 on GM cars. Of course, this only works if the firm's marketing mix attracts the target customers and the relationship keeps them satisfied before, during, and after every purchase. If you don't satisfy and retain customers they don't have high lifetime value and don't generate sales. Of course, sales revenue alone does not guarantee profits. For example, a firm can't give away products—or spend so much on promotion to acquire new customers (or keep the ones it has)—that the revenue will never be able to offset the costs. Unfortunately, that is what happened with many of the dot-coms. They saw how the financial arithmetic might work—*assuming* that new customers kept buying and costs came under control. But without a sensible marketing strategy, that assumption was not realistic.[12]

www.mhhe.com/fourps

Let's sum up our discussion of marketing mix planning thus far. We develop a *Product* to satisfy the target customers. We find a way to reach our target customers' *Place*. We use *Promotion* to tell the target customers (and others in the channel) about the product that has been designed for them. And we set a *Price* after estimating expected customer reaction to the total offering and the costs of getting it to them.

Strategy jobs must be done together

It is important to stress—it cannot be overemphasized—that selecting a target market *and* developing a marketing mix are interrelated. Both parts of a marketing strategy must be decided together. It is *strategies* that must be evaluated against the company's objectives—not alternative target markets or alternative marketing mixes.

Understanding target markets leads to good strategies

The needs of a target market often virtually determine the nature of an appropriate marketing mix. So marketers must analyze their potential target markets with great care. This book will explore ways of identifying attractive market opportunities and developing appropriate strategies.

These ideas can be seen more clearly with an example in the children's fashion market.

Market-oriented strategy planning at Toddler University

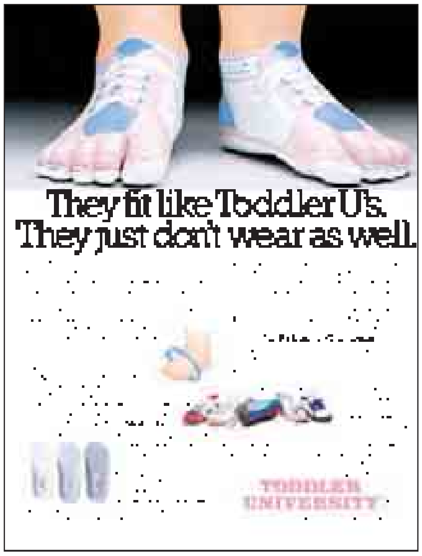
The case of Jeff Silverman and Toddler University (TU), Inc., a shoe company he started, illustrates the strategy planning process. During high school and college, Silverman worked as a salesperson at local shoe stores. He also gained valuable experience during a year working for Nike. From these jobs he learned a lot about customers' needs and interests. He also realized that some parents were not satisfied when it came to finding shoes for their preschool children.

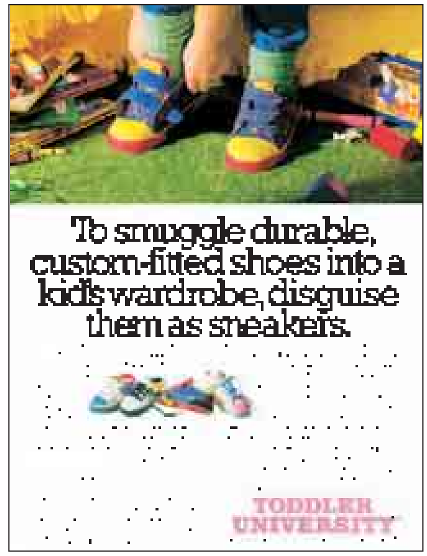
Silverman thought that there was a large, but hard to describe, mass market for general-purpose baby shoes—perhaps 60 or 70 percent of the potential for all kinds of baby shoes. Silverman did not focus on this market because it didn't make sense for his small company to compete head on with many other firms where he had no particular advantage. However, he identified four other markets that were quite different. In the following description of these markets, note that useful marketing mixes come to mind immediately.

The *Traditionalists* seemed to be satisfied with a well-manufactured shoe that was available from "quality" stores where they could seek help in selecting the right size and fit. They didn't mind if the design was old-fashioned and didn't change. They wanted a well-known brand that had a reputation for quality, even if it was a bit more expensive.

Many of the *Economy Oriented* parents were in the lower income group. They wanted a basic shoe at a low price. They saw baby shoes as all pretty much the

Toddler University's marketing strategy was successful because it developed a distinctive marketing mix that was precisely relevant to the needs of its target market.





same—so a "name" brand didn't have much appeal. They were willing to shop around to see what was on sale at local discount, department, or shoe stores.

The *Fashion Conscious* were interested in dressing up baby in shoes that looked like smaller versions of the latest styles that they bought for themselves. Fit was important, but beyond that a colorful design is what got their attention. They were more likely to look for baby-size shoes at the shop where they bought their own athletic shoes.

The *Attentive Parents* wanted shoes that met a variety of needs. They wanted shoes to be fun and fashionable and functional. They didn't want just a good fit but also design and materials that were really right for baby play and learning to walk. These well-informed, upscale shoppers were likely to buy from a store that specialized in baby items. They were willing to pay a premium price if they found the right product.

Silverman thought that Stride Rite and Buster Brown were meeting the needs of the Traditionalists quite well. The Economy Oriented and Fashion Conscious customers were satisfied with shoes from a variety of other companies, including Nike. But Silverman saw a way to get a toe up on the competition by targeting the Attentive Parents with a marketing mix that combined, in his words, "fit and function with fun and fashion." He developed a detailed marketing plan that attracted financial backers, and at age 24 his company came to life.

TU didn't have its own production facilities, so Silverman contracted with a producer in Taiwan to make shoes with his brand name and to his specs. And his specs were different—they improved the product for his target market. Unlike most rigid high-topped infant shoes, he designed softer shoes with more comfortable rubber soles. The shoes lasted longer because they are stitched rather than glued. An extrawide opening made fitting easier on squirming feet. He also patented a special insert so parents could adjust the width. This change also helped win support from retailers. Since there are 11 sizes of children's shoes—and five widths—retailers usually need to stock 55 pairs of each model. TU's adjustable width reduced this stocking problem and made it more profitable for retailers to sell the line. It also made it possible for TU to resupply sold-out inventory faster than competitors. Silverman's Product and Place decisions worked together well to provide customer value and also to give him a competitive advantage.

For promotion, Silverman developed print ads with close-up photos of babies wearing his shoes and informative details about their special benefits. Creative packaging also helped promote the shoe and attract customers in the store. For example, he put one athletic-style shoe in a box that looked like a gray gym locker.

Silverman also provided the stores with "shoe rides"—electric-powered rocking replicas of its shoes. The rides not only attracted kids to the shoe department, but since they were coin-operated, they paid for themselves in a year.

TU priced most of its shoes at $35 to $40 a pair. This is a premium price, but with today's smaller families, the Attentive Parents are willing to spend more on each child.

In just four years, TU's sales jumped from $100,000 to over $40 million. To keep growth going, Silverman expanded distribution to reach new markets in Europe. To take advantage of TU's relationship with its satisfied target customers, he also added shoes for older kids to the Toddler University product assortment. Then Silverman made his biggest sale of all: he sold his company to Genesco, one of the biggest firms in the footwear business.[13]

The Marketing Plan Is a Guide to Implementation and Control

Marketing plan fills out marketing strategy

As the Toddler University case illustrates, a marketing strategy sets a target market and a marketing mix. It is a big picture of what a firm will do in some market. A marketing plan goes farther. A **marketing plan** is a written statement of a marketing strategy *and* the time-related details for carrying out the strategy. It should spell out the following in detail: (1) what marketing mix will be offered, to whom (that is, the target market), and for how long; (2) what company resources (shown as costs) will be needed at what rate (month by month perhaps); and (3) what results are expected (sales and profits perhaps monthly or quarterly, customer satisfaction levels, and the like). The plan should also include some control procedures—so that whoever is to carry out the plan will know if things are going wrong. This might be something as simple as comparing actual sales against expected sales—with a warning flag to be raised whenever total sales fall below a certain level.

Implementation puts plans into operation

After a marketing plan is developed, a marketing manager knows *what* needs to be done. Then the manager is concerned with **implementation**—putting marketing plans into operation.

Strategies work out as planned only when they are effectively implemented. Many **operational decisions**—short-run decisions to help implement strategies—may be needed.

Managers should make operational decisions within the guidelines set down during strategy planning. They develop product policies, place policies, and so on as part of strategy planning. Then operational decisions within these policies probably will be necessary—while carrying out the basic strategy. Note, however, that as long as these operational decisions stay within the policy guidelines, managers are making no change in the basic strategy. If the controls show that operational decisions are not producing the desired results, however, the managers may have to reevaluate the whole strategy—rather than just working harder at implementing it.

It's easier to see the difference between strategy decisions and operational decisions if we illustrate these ideas using our Toddler University example. Possible four-P or basic strategy policies are shown in the left-hand column in Exhibit 2-11, and examples of operational decisions are shown in the right-hand column.

It should be clear that some operational decisions are made regularly—even daily—and such decisions should not be confused with planning strategy. Certainly, a great deal of effort can be involved in these operational decisions. They might take a good part of the sales or advertising manager's time. But they are not the strategy decisions that will be our primary concern.

Exhibit 2-11 Relation of Strategy Policies to Operational Decisions for Baby Shoe Company

Marketing Mix Decision Area	Strategy Policies	Likely Operational Decisions
Product	Carry as limited a line of colors, styles, and sizes as will satisfy the target market.	Add, change, or drop colors, styles, and/or sizes as customer tastes dictate.
Place	Distribute through selected "baby-products" retailers who will carry the full line and provide good in-store sales support and promotion.	In market areas where sales potential is not achieved, add new retail outlets and/or drop retailers whose performance is poor.
Promotion	Promote the benefits and value of the special design and how it meets customer needs.	When a retailer hires a new salesperson, send current training package with details on product line; increase use of local newspaper print ads during peak demand periods (before holidays, etc.).
Price	Maintain a "premium" price, but encourage retailers to make large-volume orders by offering discounts on quantity purchases.	Offer short-term introductory price "deals" to retailers when a new style is first introduced.

Our focus in this text is on developing marketing strategies. But, eventually marketing managers must develop, implement, and control marketing plans.[14]

Control is analyzing and correcting what you've done

The control job provides the feedback that leads managers to modify their marketing strategies. To maintain control, a marketing manager uses a number of tools—like computer sales analysis, marketing research surveys, and accounting analysis of expenses and profits. Chapter 19 considers the important topic of controlling marketing plans and programs.

In addition, as we talk about each of the marketing decision areas, we will discuss some of the control problems. This will help you understand how control keeps the firm on course—or shows the need to plan a new course.

All marketing jobs require planning and control

At first, it might appear that only high-level management or large companies need be concerned with planning and control. This is not true. Every organization needs planning—and without control it's impossible to know if the plans are working.

Several plans make a whole marketing program

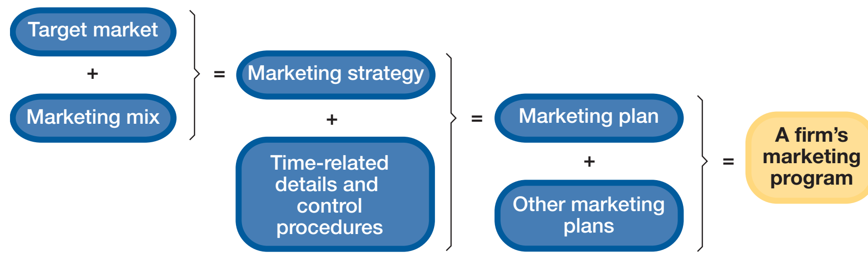
Most companies implement more than one marketing strategy—and related marketing plan—at the same time. They may have several products—some of them quite different—that are aimed at different target markets. The other elements of the marketing mix may vary too. Gillette's Right Guard deodorant, its Mach3 razor blades, and its Duracell Ultra batteries all have different marketing mixes. Yet the strategies for each must be implemented at the same time.[15]

A **marketing program** blends all of the firm's marketing plans into one "big" plan. See Exhibit 2-12. This program, then, is the responsibility of the whole company. Typically, the whole *marketing program* is an integrated part of the whole-company strategic plan we discussed earlier.

We will emphasize planning one marketing strategy at a time, rather than planning—or implementing—a whole marketing program. This is practical because it is important to plan each strategy carefully. Too many marketing managers fall into sloppy thinking. They try to develop too many strategies all at once—and don't develop any very carefully. However, when new strategies are evaluated, it makes sense to see how well they fit with the existing marketing program. And, we'll talk about merging plans into a marketing program in Chapter 21.

Marketing strategy planning may be very important to you soon—maybe in your present job or college activities. In Appendix C on marketing careers, we present some strategy planning ideas for getting a marketing job.

Exhibit 2-12
Elements of a Firm's Marketing Program



The Importance of Marketing Strategy Planning

We emphasize the planning part of the marketing manager's job for a good reason. The "one-time" strategy decisions—the decisions that decide what business the company is in and the strategies it will follow—usually determine success, or failure. An extremely good plan might be carried out badly and still be profitable, while a poor but well-implemented plan can lose money. The case history that follows shows the importance of planning and why we emphasize marketing strategy planning throughout this text.

Time for new strategies in the watch industry

The conventional watchmakers—both domestic and foreign—had always aimed at customers who thought of watches as high-priced, high-quality symbols to mark special events—like graduations or retirement. Advertising was concentrated around Christmas and graduation time and stressed a watch's symbolic appeal. Expensive jewelry stores were the main retail outlets.

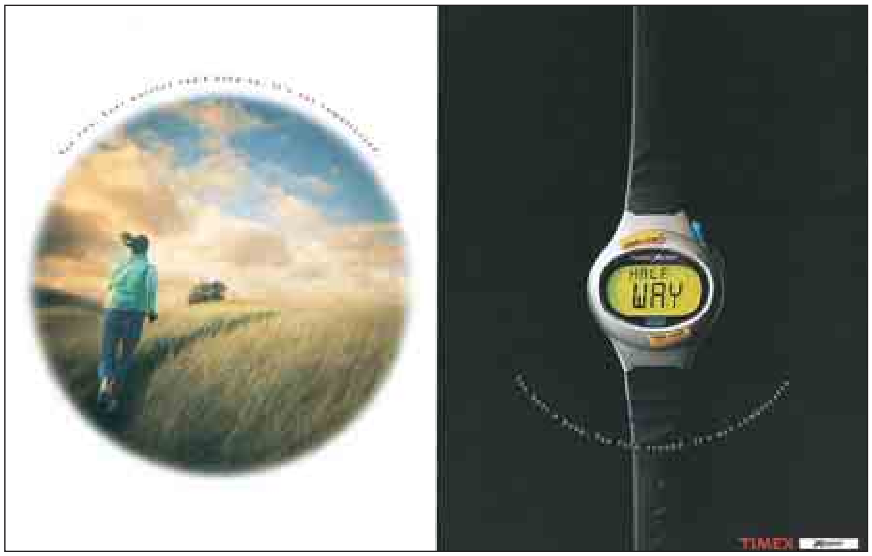
This commonly accepted strategy of the major watch companies ignored people in the target market that just wanted to tell the time and were interested in a reliable, low-priced watch. So the U.S. Time Company developed a successful strategy around its Timex watches and became the world's largest watch company. Timex completely upset the watch industry—both foreign and domestic—not only by offering a good product (with a one-year repair or replace guarantee) at a lower price, but also by using new, lower-cost channels of distribution. Its watches were widely available in drugstores, discount houses, and nearly any other retail stores that would carry them.

Marketing managers at Timex soon faced a new challenge. Texas Instruments, a new competitor in the watch market, took the industry by storm with its low-cost but very accurate electronic watches—using the same channels Timex had originally developed. But other firms quickly developed a watch that used a more stylish liquid crystal display for the digital readout. Texas Instruments could not change quickly enough to keep up, and the other companies took away its customers. The competition became so intense that Texas Instruments stopped marketing watches altogether.

While Timex and others were focusing on lower-priced watches, Japan's Seiko captured a commanding share of the high-priced gift market for its stylish and accurate quartz watches by obtaining strong distribution. All of this forced many traditional watchmakers—like some of the once-famous Swiss brands—to close their factories.

Then Switzerland's Swatch launched its colorful, affordable plastic watches and changed what consumers see when they look at their watches. Swatch promoted its watches as fashion accessories and set them apart from those of other firms, whose ads squabbled about whose watches were most accurate and dependable. Swatch was also able to attract new retailers by focusing its distribution on upscale fashion and department stores. The total size of the watch market increased because many consumers bought several watches to match different fashions.

The economic downturn in the early 1990s brought more changes. Consumers were more cost conscious and less interested in expensive watches like those made



To better meet the needs of a specific target market, Timex has developed a line of Rush sportwatches for women. It is also developing other watches to meet specific needs, such as its iControl watches that are very easy to program.

by Rolex that were the "in" status symbol a few years earlier. The reemergence of value-seeking customers prompted Timex to return to its famous advertising tagline of the 1960s: "It takes a licking and keeps on ticking." Its position as the inexpensive-but-durable choice has helped it strengthen its distribution and has given it a leg up in getting shelf space for new products, such as its Indiglo line of watches.

By the turn of the century, the total market for watches was growing at only about 5 percent a year. To spark higher sales of its lines, Timex pushed to introduce more watches that combine time-telling and other needs. For example, its women's fitness watch includes a pulse timer and on-screen displays; and its Internet Messenger Watch, for about $100 and a monthly service charge, can receive short text messages, like an alert from the wearer's stock broker that it's time to sell. Of course, all the new features can make a watch more complicated to use, so Timex is refocusing on the need for simple convenience with its iControl technology, which it promotes with trendy ads and the tagline "Ridiculously easy to use." Competitors are on the move as well. For example, Casio has a watch with a global positioning system and Swatch is considering a watch with a smart chip that will also make it a debit card. With such changes always underway, marketing strategies must constantly be updated and revised.[16]

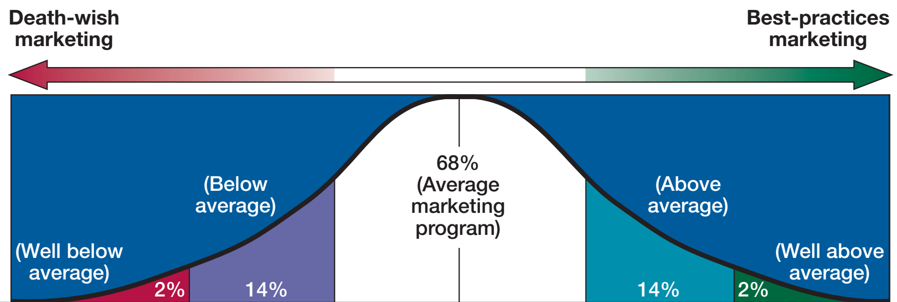
Internet

Internet Exercise Go to the Timex website (www.timex.com) and use the drop-down list or site map to go to the "Latest Products" section. Based on the needs that a product is designed to meet, can you identify the characteristics of the product's target market?

Creative Strategy Planning Needed for Survival

Dramatic shifts in strategy—like those described above—may surprise conventional, production-oriented managers. But such changes should be expected. Managers who embrace the marketing concept realize that they cannot just define

Exhibit 2-13 Distribution of Different Firms Based on Their Marketing Performance



MARKETING PERFORMANCE:	TOTAL FAILURE	POOR	FAIR	GOOD	EXCEPTIONAL
Marketing Share Growth	Precipitous Decline	Significant Decline	Modest Decline	Increase	Dramatic Increase
New Product Success Rate	0%	5%	10%	25%	40%+
Advertising ROI	Negative	0%	1–4%	5–10%	20%
Promotional Programs	Disaster	Unprofitable	Marginally Unprofitable	Profitable	Very Profitable
Customer Satisfaction	0–59%	60–69%	70–79%	80–89%	90–95%
Customer Acquisition Programs	Disturbing Losses	Significant Losses	Marginal Losses	Break Even	Profitable
Customer Retention/Loyalty	0–44%	45–59%	60–74%	75–89%	90–94%

their line of business in terms of the products they currently produce or sell. Rather, they have to think about the basic consumer needs they serve, how those needs may change in the future, and how they can improve the value they offer to customers. If they are too nearsighted, they may fail to see what's coming until too late.

Creative strategy planning is becoming even more important. Domestic and foreign competition threatens those who can't provide superior customer value and find ways to build stronger relationships with customers. New markets, new customers, and new ways of doing things must be found if companies are to operate profitably in the future—and contribute to the macro-marketing system.

Focus on "best practices" for improved results

The case studies and concepts in this chapter highlight effective marketing thinking. Throughout the text, we will continue with this thrust—focusing on marketing frameworks and concepts that produce good results. Some of these are new and innovative, and others are well established. What they have in common is that they all work well.

Sometimes we will warn you about marketing errors—so you can avoid them. But, we won't just give you laundry lists of different approaches and then leave it to you to guess what might work. Rather, our focus will be on "best-practices" marketing.

There is an important reason for this approach. In too many firms, managers do a poor job planning and implementing marketing strategies and programs. And, as shown in Exhibit 2-13, this type of "death-wish" marketing is both costly and ineffective. In fact, you can see that even the average marketing program isn't producing great results—and that accounts for the majority of firms!

Exhibit 2-13 was developed by experts at Copernicus, one of the premier marketing research and consulting firms in the world. As these experts indicate in the chart, some managers are creating marketing programs that produce exceptional results for their companies. This book will help you do exactly that.

Conclusion

Marketing's role within a marketing-oriented firm is to provide direction for the firm. The marketing concept stresses that the company's efforts should focus on satisfying some target customers—at a profit. Production-oriented firms tend to forget this. The various departments within a production-oriented firm let their natural conflicts of interest get in the way of providing superior customer value.

The job of marketing management is one of continuous planning, implementing, and control. The marketing manager must constantly study the environment—seeking attractive opportunities and planning new strategies. Possible target markets must be matched with marketing mixes the firm can offer. Then, attractive strategies—really, whole marketing plans—are chosen for implementation. Controls are needed to be sure that the plans are carried out successfully. If anything goes wrong along the way, continual feedback should cause the process to be started over again—with the marketing manager planning more attractive marketing strategies.

A marketing mix has four major decision areas: the four Ps—Product, Place, Promotion, and Price. Most of this text is concerned with developing profitable marketing mixes for clearly defined target markets. So after several chapters on the marketing strategy planning process and several on analyzing target markets, we will discuss each of the four Ps in greater detail.

While market-oriented strategy planning is helpful to marketers, it is also needed by accountants, production and personnel people, and all other specialists. A market-oriented plan lets everybody in the firm know what ballpark they are playing in and what they are trying to accomplish.

We will use the term *marketing manager* for editorial convenience, but really, when we talk about marketing strategy planning, we are talking about the planning that a market-oriented manager should do when developing a firm's strategic plans. This kind of thinking should be done—or at least understood—by everyone in the organization. And this means even the entry-level salesperson, production supervisor, retail buyer, or personnel counselor.

Questions and Problems

1. Define the marketing concept in your own words and then explain why the notion of profit is usually included in this definition.
2. Define the marketing concept in your own words and then suggest how acceptance of this concept might affect the organization and operation of your college.
3. Give examples of some of the benefits and costs that might contribute to the customer value of each of the following products: (*a*) a wrist watch, (*b*) a weight-loss diet supplement, (*c*) a cruise on a luxury liner, and (*d*) a checking account from a bank.
4. Distinguish between production orientation and marketing orientation, illustrating with local examples.
5. Explain why a firm should view its internal activities as part of a total system. Illustrate your answer for (*a*) a large grocery products producer, (*b*) a plumbing wholesaler, and (*c*) a department store chain.
6. Give an example of a recent purchase you made where the purchase wasn't just a single transaction but rather part of an ongoing relationship with the seller. Discuss what the seller has done (or could do better) to strengthen the relationship and increase the odds of you being a loyal customer in the future.
7. Distinguish clearly between a marketing strategy and a marketing mix. Use an example.
8. Distinguish clearly between mass marketing and target marketing. Use an example.
9. Why is the customer placed in the center of the four Ps in the text diagram of a marketing strategy (Exhibit 2-8)? Explain, using a specific example from your own experience.
10. If a company sells its products only from a website, which is accessible over the Internet to customers from all over the world, does it still need to worry about having a specific target market? Explain your thinking.
11. Explain, in your own words, what each of the four Ps involves.
12. Evaluate the text's statement, "A marketing strategy sets the details of implementation."
13. Distinguish between strategy decisions and operational decisions, illustrating for a local retailer.
14. Distinguish between a strategy, a marketing plan, and a marketing program, illustrating for a local retailer.

15. Outline a marketing strategy for each of the following new products: (*a*) a radically new design for a toothbrush, (*b*) a new fishing reel, (*c*) a new wonder drug, and (*d*) a new industrial stapling machine.
16. Provide a specific illustration of why marketing strategy planning is important for all businesspeople, not just for those in the marketing department.

Suggested Cases

2. Healthy Foods, Inc.
5. Republic Polymer Company
29. Metal Works, Inc.

Computer-Aided Problem

2. **Target Marketing**

Marko, Inc.'s managers are comparing the profitability of a target marketing strategy with a mass marketing "strategy." The spreadsheet gives information about both approaches.

The mass marketing strategy is aiming at a much bigger market. But a smaller percent of the consumers in the market will actually buy this product—because not everyone needs or can afford it. Moreover, because this marketing mix is not tailored to specific needs, Marko will get a smaller share of the business from those who do buy than it would with a more targeted marketing mix.

Just trying to reach the mass market will take more promotion and require more retail outlets in more locations—so promotion costs and distribution costs are higher than with the target marketing strategy. On the other hand, the cost of producing each unit is higher with the target marketing strategy—to build in a more satisfying set of features. But, because the more targeted marketing mix is trying to satisfy the needs of a specific target market, those customers will be willing to pay a higher price.

In the spreadsheet, "quantity sold" (by the firm) is equal to the number of people in the market who will actually buy one each of the product—multiplied by the share of those purchases won by the firm's marketing mix. Thus, a change in the size of the market, the percent of people who purchase, or the share captured by the firm will affect quantity sold. And a change in quantity sold will affect total revenue, total cost, and profit.

a. *On a piece of paper, show the calculations that prove that the spreadsheet "total profit" value for the target marketing strategy is correct. (Hint: Remember to multiply unit production cost and unit distribution cost by the quantity sold.) Which approach seems better—target marketing or mass marketing? Why?*

b. *If the target marketer could find a way to reduce distribution cost per unit by $.25, how much would profit increase?*

c. *If Marko, Inc., decided to use the target marketing strategy and better marketing mix decisions increased its share of purchases from 50 to 60 percent—without increasing costs—what would happen to total profit? What does this analysis suggest about the importance of marketing managers knowing enough about their target markets to be effective target marketers?*

For additional questions related to this problem, see Exercise 2-4 in the *Learning Aid for Use with Basic Marketing*, 14th edition.

When You Finish This Chapter, You Should

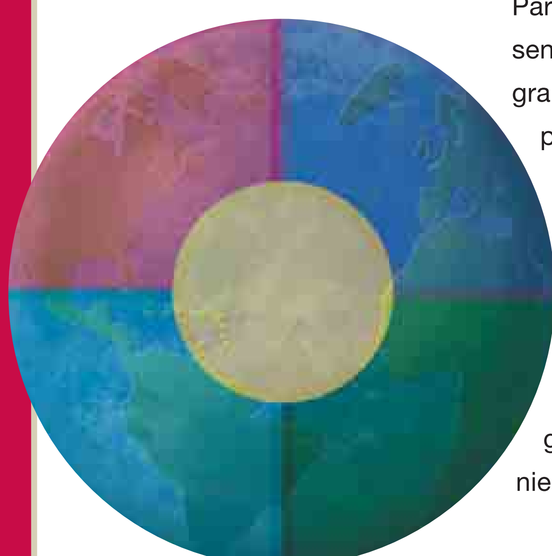
1. Understand why marketing strategy planning involves a process of narrowing down from broad opportunities to a specific target market and marketing mix.
2. Know about the different kinds of marketing opportunities.
3. Understand why opportunities in international markets should be considered.
4. Know about defining generic markets and product-markets.
5. Know what market segmentation is and how to segment product-markets into submarkets.
6. Know three approaches to market-oriented strategy planning.
7. Know dimensions that may be useful for segmenting markets.
8. Know what positioning is and why it is useful.
9. Understand the important new terms (shown in red).

Chapter Three

Focusing Marketing Strategy with Segmentation and Positioning

Polaroid desperately needed a profitable new opportunity. For several years the firm had been losing money. The objective of the new top executive was to make Polaroid profitable again—and soon. That was a needed first step for Polaroid to be able to compete longer term.

Polaroid got its start with a breakthrough invention. Its instant picture cameras and films were unique and met the needs of different groups of customers. Parents wanted to immediately send pictures of the new baby to grandparents. Realtors needed photos of just-listed homes for clients. Colleges had to make IDs quickly, and insurance adjusters had to document auto accidents. Over time, however, Polaroid faced competition for other types of goods and services. Convenient one-hour photo lab services



place price promotion produc

popped up everywhere. Then digital cameras made the competition even rougher. A hundred firms now offer all types of digital cameras, and digital pictures can be shared by e-mail or a website—without costly film or printing. Increased competition wasn't the only problem. Economic turmoil in Asia eroded revenue from Polaroid's new target markets in China and India.

Polaroid's new-product development manager helped overcome these weaknesses when he spotted a new opportunity. He saw teens having fun at an instant photo booth in a Japanese airport and had an idea for an inexpensive new pocket-sized camera that would appeal to teens with its instant, stamp-size photos. Some Polaroid engineers objected that the quality of the photos would be poor and would hurt Polaroid's position as a technology leader. But marketers at Polaroid pressed on because the product would help attract a new generation of teen customers. Many teens viewed Polaroid cameras as clunky holdovers from the past. Besides, picture quality wasn't the benefit that determined their interest. They just wanted fun and convenience—more a toy for making quick pictures rather than a serious camera.

The benefits of Polaroid's pocket camera proved to be right on target with the teen segment. It very quickly became a best seller and new-product revenue was the highest it had been in a decade. Targeted promotion helped to attract buyers, half of whom were girls age 13 to 17. Ads for Polaroid's I-Zone Pocket camera and film were placed in magazines like *Seventeen,* at clickclick.com and other websites popular with teens, and on TV shows like *Buffy the Vampire Slayer*. While ad media were slanted toward teen girls, the ad messages were broader so that they would appeal to a combined male and female teen market. To increase the opportunities for I-Zone Pocket camera fun, Polaroid came out with a special "sticky" film. The sticker-pictures could be peeled off and attached to lockers, notebooks, clothing, and just about anything else. One funny ad featured a young man sticking instant pictures of his girlfriend to his bare chest. Reaching this younger target market also called for new distribution channels, including online toy and music stores and more emphasis on mass-merchandisers like Wal-Mart. Trade ads targeted at these retailers helped bring in the orders and make the film more widely available. Frequent film purchases really boosted profits.

Of course, Kodak didn't take this sitting down; soon it was targeting teens with its one-use Max cameras. Marketers at Polaroid know that its teen target market can be fickle and that the I-Zone could become yesterday's fad. So it is introducing other new products for teens to strengthen its fun positioning. One is a combination camera that takes both digital pictures and pocket pictures, and another is the Webster—a miniature scanner to turn I-Zone pictures into digital images. Teens can post pictures from either product at Polaroid's special new website (www.i-zone.com).

Polaroid's new strategies and teen target market have certainly boosted profits. But Polaroid's traditional customer segments—with a variety of other instant picture needs—still account for the bulk of its business. So if Polaroid is going to have a clear profit picture long term, it will need to find ways to offer these segments superior customer value as they shift toward digital images.[1]

What Are Attractive Opportunities?

Marketing strategy planning tries to match opportunities to the firm's resources (what it can do) and its objectives (what top management wants to do). Successful strategies get their start when a creative manager spots an attractive market opportunity. Yet, an opportunity that is attractive for one firm may not be attractive for another. As the Polaroid case suggests, attractive opportunities for a particular firm are those that the firm has some chance of doing something about—given its resources and objectives.

Breakthrough opportunities are best

Throughout this book, we will emphasize finding **breakthrough opportunities**—opportunities that help innovators develop hard-to-copy marketing strategies that will be very profitable for a long time. That's important because there are always imitators who want to "share" the innovator's profits—if they can. It's hard to continuously provide superior value to target customers if competitors can easily copy your marketing mix.

Competitive advantage is needed—at least

Even if a manager can't find a breakthrough opportunity, the firm should try to obtain a competitive advantage to increase its chances for profit or survival. **Competitive advantage** means that a firm has a marketing mix that the target market sees as better than a competitor's mix. A competitive advantage may result from

Attractive new opportunities are often fairly close to markets the firm already knows.

efforts in different areas of the firm—cost cutting in production, innovative R&D, more effective purchasing of needed components, or financing for a new distribution facility. Similarly, a strong sales force, a well-known brand name, or good dealers may give it a competitive advantage in pursuing an opportunity. Whatever the source, an advantage only succeeds if it allows the firm to provide superior value and satisfy customers better than some competitor.

Sometimes a firm can achieve breakthrough opportunities and competitive advantage by simply fine-tuning its current marketing mix(es) or developing closer relationships with its customers. Other times it may need new facilities, new people in new parts of the world, and totally new ways of solving problems. But every firm needs some competitive advantage—so the promotion people have something unique to sell and success doesn't just hinge on offering lower and lower prices.[2]

Avoid hit-or-miss marketing with a logical process

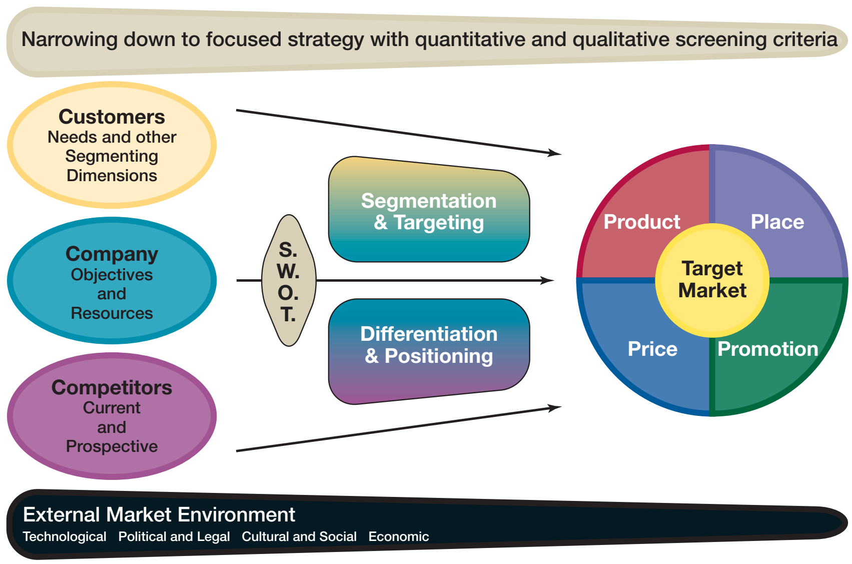
You can see why a manager *should* seek attractive opportunities. But that doesn't mean that everyone does—or that everyone can turn an opportunity into a successful strategy. As we discussed in Chapter 2 (Exhibit 2-13), too many firms settle for the sort of death-wish marketing that doesn't satisfy customers or make a profit—to say nothing about achieving a breakthrough or providing superior value. It's all too easy for a well-intentioned manager to react in a piecemeal way to what appears to be an opportunity. Then, by the time the problems are obvious, it's too late.

Developing a successful marketing strategy doesn't need to be a hit-or-miss proposition. And it won't be if you learn the marketing strategy planning process developed in this text. Exhibit 3-1 summarizes the decision areas for the marketing strategy planning process we'll be developing throughout the rest of the chapters.

Marketing Strategy Planning Process Highlights Opportunities

From Chapter 2, you know that a marketing strategy requires decisions about the specific customers the firm will target and the marketing mix the firm will develop to appeal to that target market. We can organize the many marketing mix decisions (review Exhibit 2-9) in terms of the four Ps—Product, Place, Promotion, and Price.

Exhibit 3-1
Overview of Marketing Strategy Planning Process



Thus, the "final" strategy decisions are represented by the target market surrounded by the four Ps. However, the idea isn't just to come up with *some* strategy. After all, there are hundreds or even thousands of combinations of marketing mix decisions and target markets (i.e., strategies) that a firm might try. Rather, the challenge is to zero in on the best strategy.

Process narrows down from broad opportunities to specific strategy

As Exhibit 3-1 suggests, it is useful to think of the marketing strategy planning process as a narrowing-down process. Later in this chapter and Chapter 4 we will go into more detail about strategy decisions relevant to each of the terms in this figure. Then, throughout the rest of the book, we will present a variety of concepts and "how to" frameworks that will help you improve the way you make these strategy decisions. As a preview of what's coming, let's briefly overview the general logic of the process depicted in Exhibit 3-1.

The process starts with a broad look at a market—paying special attention to customer needs, the firm's objectives and resources, and competitors. This helps to identify new and unique opportunities that might be overlooked if the focus is narrowed too quickly.

Segmentation helps pinpoint the target

A key objective of marketing is to satisfy the needs of some group of customers that the firm serves. Broadly speaking, then, in the early stages of a search for opportunities we're looking for customers with needs that are not being satisfied as well as they might be. Of course, potential customers are not all alike. They don't all have the same needs—nor do they always want to meet needs in the same way. Part of the reason is that there are different possible types of customers with many different characteristics. For example, individual consumers often have different needs than organizations, and people with certain attitudes or interests have different preferences for how they spend their time, what shows they watch, and the like. In spite of the many possible differences, there often are subgroups (segments) of consumers who are similar and could be satisfied with the same marketing mix. Thus, we try to identify and understand these different subgroups—with market segmentation. We will explain general approaches for segmenting markets later in this chapter. Then, in Chapters 5 to 7, we delve into the many interesting aspects of customer behavior. For now, however, you should know that really understanding

This Norwegian ad for the Audi Quattro simply says, "Sticks like quattro." Although it doesn't show the car at all, it helps to differentiate the Audi and its four-wheel drive system that holds the road especially well, even in the snow.

customers is at the heart of using market segmentation to narrow down to a specific target market. In other words, segmentation helps a manager decide to serve some segment(s)—subgroups of customers—and not others.

Narrow down to a superior marketing mix

A marketing mix must meet the needs of target customers, but a firm isn't likely to get a competitive advantage if it *just* meets needs in the same way as some other firm. So, in evaluating possible strategies the marketing manager should think about whether there is a way to differentiate the marketing mix. **Differentiation** means that the marketing mix is distinct from and better than what is available from a competitor. As suggested above, differentiation often requires that the firm fine-tune all of the elements of its marketing mix to the specific needs of a distinctive target market. Sometimes the difference is based mainly on one important element of the marketing mix—say, an improved product or faster delivery. Differentiation is more obvious to target customers, though, when there is a consistent theme integrated across the four Ps decision areas. That emphasizes the difference so target customers will think of the firm as being in a unique position to meet their needs. For example, in Norway, many auto buyers are particularly concerned about safety in the snow. So, Audi offers a permanent four-wheel drive system, called quattro, that helps the car to hold the road. Audi ads emphasize this differentiation. Rather than show the car, however, the ads feature things that are very sticky (like bubblegum!) and the only text is the headline "sticks like quattro" and the Audi brand name. Of course, handling is not Audi's only strength, but it is an important one in helping to position Audi as better than competing brands with this target market. In contrast, consider General Motors' decision to discontinue the 100-year-old Oldsmobile line. In spite of repeated efforts, marketers for Oldsmobile were no longer able to develop a differentiated position in the crowded U.S. auto market. And when target customers don't see an advantage with a firm's marketing mix, they just move on.[3]

In this chapter, we'll introduce concepts relevant to this sort of positioning. Then, in Chapters 9 to 18 we'll cover the many ways in which the four Ps of the marketing mix can be differentiated. For now, you can see that the thrust is to narrow down from all possible marketing mixes to one that is differentiated to meet target customers' needs particularly well. Of course, finding the best differentiation requires that we understand competitors as well as customers.

Screening criteria make it clear why you select a strategy

There are usually more different opportunities—and strategy possibilities—than a firm can pursue. Each one has its own advantages and disadvantages. Trends in the external market environment may make a potential opportunity more or less attractive. These complications can make it difficult to zero in on the best target market and marketing mix. However, developing a set of specific qualitative and quantitative screening criteria can help a manager define what business and markets the firm wants to compete in. It can also help eliminate potential strategies that are not well suited for the firm. We will cover screening criteria in more detail in Chapter 4. For now, you should realize that the criteria you select in a specific situation grow out of an analysis of the company's objectives and resources.

S.W.O.T. analysis highlights advantages and disadvantages

A useful aid for identifying relevant screening criteria and for zeroing in on a feasible strategy is **S.W.O.T. analysis**—which identifies and lists the firm's strengths and weaknesses and its opportunities and threats. The name S.W.O.T. is simply an abbreviation for the first letters of the words *s*trengths, *w*eaknesses, *o*pportunities, and *t*hreats. A good S.W.O.T. analysis helps the manager focus on a strategy that takes advantage of the firm's opportunities and strengths while avoiding its weaknesses and threats to its success. These can be compared with the pros and cons of different strategies that are considered.

The marketing strategy developed by Amilya Antonetti illustrates the basic ideas behind a S.W.O.T. analysis. Her son was allergic to the chemicals in standard detergents—and her research showed that many other children had the same problem. So she started SoapWorks and developed a line of hypoallergenic cleaning products to pursue this opportunity. Unlike the big firms, she didn't have relations with grocery chains or money for national TV ads. To get around these weaknesses, she used inexpensive radio ads in local markets and touted SoapWorks as a company created for moms by a mom who cared about kids. She had a credible claim that the big corporations couldn't make. Her ads also helped her get shelf space because they urged other mothers to ask for SoapWorks products and to tell friends about stores that carried them. This wasn't the fastest possible way to introduce a new product line, but her cash-strapped strategy played to her unique strengths with her specific target market.[4]

Exhibit 3-1 focuses on planning each strategy carefully. Of course, this same approach works well when several strategies are to be planned. Then, having an organized evaluation process is even more important. It forces everyone involved to think through how the various strategies fit together as part of an overall marketing program.

The discussion above makes it clear that finding attractive target markets is a crucial aspect of the marketing strategy planning process. But how do you identify a target market and decide if it offers good opportunities? In the rest of this chapter, we will begin to answer these questions. Opportunities that involve international markets present some special challenges, so we'll give them some special attention.[5]

Types of Opportunities to Pursue

Some alert marketers seem to be able to spot attractive opportunities everywhere they look. This seems reasonable when you recognize that most people have unsatisfied needs. Unfortunately, many opportunities seem "obvious" only after someone else identifies them. So, early in the marketing strategy planning process it's useful for marketers to have a framework for thinking about the broad kinds of opportunities they may find. Exhibit 3-2 shows four broad possibilities: market penetration, market development, product development, and diversification. We will look at

Exhibit 3-2
Four Basic Types of Opportunities

	Present products	New products
Present markets	Market penetration	Product development
New markets	Market development	Diversification

these separately, but some firms pursue more than one type of opportunity at the same time.

Market penetration

Market penetration means trying to increase sales of a firm's present products in its present markets—probably through a more aggressive marketing mix. The firm may try to strengthen its relationship with customers to increase their rate of use or repeat purchases, or try to attract competitors' customers or current nonusers. Coleman got a 50 percent increase in sales of its outdoor equipment, like camping lanterns and stoves, by reaching its target market with special promotional displays at outdoor events like concerts, fishing tournaments, and Nascar races. For example, about 250,000 auto racing fans camp on-site at Nascar races each year—so a display at the campground is an effective way to reach customers when they have leisure time to browse through product displays and demos.[6]

New promotion appeals alone may not be effective. A firm may need to add a home page on the Internet to make it easier and faster for customers to place an order. Or, it may need to add more stores in present areas for greater convenience. Short-term price cuts or coupon offers may help.

Market development

Market development means trying to increase sales by selling present products in new markets. This may involve searching for new uses for a product. E-Z-Go, a producer of golf carts, has done this. Its carts are now a quiet way for workers to get around malls, airports, and big factories. The large units are popular as utility vehicles on farms, at outdoor sports events, and at resorts. E-Z-Go even fits carts with ice compartments and cash drawers so they can be used for mobile food services.

Firms may also try advertising in different media to reach new target customers. Or they may add channels of distribution or new stores in new areas, including overseas. For example, to reach new customers, McDonald's has opened outlets in airports, zoos, casinos, and military bases. And it's rapidly expanded into international markets with outlets in places like Russia, Brazil, and China.[7]

Product development

Product development means offering new or improved products for present markets. By knowing the present market's needs, a firm may see new ways to satisfy customers. For example, kids are the big consumers of ketchup. So Heinz figured out how ketchup could be more fun. Producing ketchup in gross green and funky purple colors—in an EZ Squirt dispenser molded to fit little hands—increased sales so much that the factory had to run 24/7. Ski resorts have developed trails for hiking and biking to bring their winter ski customers back in the summer. Nike moved beyond shoes and sportswear to offer its athletic target market a running watch, digital audio player, and even a portable heart-rate monitor. And of course Intel boosts sales by developing newer and faster chips.[8]

Diversification

Diversification means moving into totally different lines of business—perhaps entirely unfamiliar products, markets, or even levels in the production-marketing system. McDonald's, for example, is opening two four-star hotels in Switzerland. The plan is to serve families on the weekend, but the target market during the week is business travelers. This means that McDonald's will need to satisfy a very different group of customers from the ones it already knows. A luxury hotel is also very different from a fast-food restaurant. Products and customers that are very different from a firm's current base may look attractive to the optimists—but these opportunities are usually hard to evaluate. That's why diversification usually involves the biggest risk.[9]

Internet

Internet Exercise Go to the website for McDonald's hotel and review the information given (www.goldenarchhotel.com). Based on what you see, do you think that the hotels will appeal to the weekend target market of traveling families? Do you think they will appeal to business travelers during the week?

Which opportunities come first?

Usually firms find attractive opportunities fairly close to markets they already know. This may allow them to capitalize on changes in their present markets—or more basic changes in the external environment. Moreover, many firms are finding that the easiest way to increase profits is to do a better job of hanging onto the customers that they've already won—by meeting their needs so well that they wouldn't consider switching to another firm.

For these reasons, most firms think first of greater market penetration. They want to increase profits where they already have experience and strengths. On the other hand, many firms are proving that market development—and the move into new international markets—is another profitable way to take advantage of current strengths.

International Opportunities Should Be Considered

It's easy for a marketing manager to fall into the trap of ignoring international markets, especially when the firm's domestic market is prosperous. Yet, there are good reasons to go to the trouble of looking elsewhere for opportunities.

The world is getting smaller

International trade is increasing all around the world, and trade barriers are coming down. In addition, advances in e-commerce, transportation, and communications are making it easier and cheaper to reach international customers. With an Internet website and a fax machine, even the smallest firm can provide international customers with a great deal of information—and easy ways to order—at very little expense. E-mail communications and interactive electronic ordering are fast and efficient whether the customer is a mile away or in another country. Around the world, potential customers have needs and money to spend. The real question is whether a firm can effectively use its resources to meet these customers' needs at a profit.

Develop a competitive advantage at home and abroad

If customers in other countries are interested in the products a firm offers—or could offer—serving them may improve economies of scale. Lower costs (and prices) may give a firm a competitive advantage both in its home markets *and* abroad. Black and Decker, for example, uses electric motors in many of its tools and appliances. By selling overseas as well as in the U.S., it gets economies of scale and the cost per motor is very low.

Lipton is pursuing new customers and growth in over 100 countries. For example, its multilingual website in Belgium explains how to make exotic cocktails from Ice Tea, and in Asia it encourages consumer trial with free samples.

Marketing managers who are only interested in the "convenient" customers in their own backyards may be rudely surprised to find that an aggressive, low-cost foreign producer is willing to pursue those customers—even if doing it is not convenient. Many companies that thought they could avoid the struggles of international competition have learned this lesson the hard way. The owner of Purafil, a small firm in Atlanta that makes air purification equipment, puts it this way: "If I'm not [selling to an oil refinery] in Saudi Arabia, somebody else is going to solve their problem, then come attack me on my home turf."[10]

Get an early start in a new market

Different countries are at different stages of economic and technological development, and their consumers have different needs at different times.

A company facing tough competition, thin profit margins, and slow sales growth at home may get a fresh start in another country where demand for its product is just beginning to grow. A marketing manager may be able to transfer marketing know-how—or some other competitive advantage—the firm has already developed. Consider JLG, a Pennsylvania-based producer of equipment used to lift workers and tools at construction sites. In the early 1990s competition was tough and JLG's sales were dropping so fast that profits all but evaporated. By cutting costs, the company improved its domestic sales. But it got an even bigger boost from expanding overseas. By 2000 its international sales were greater than its total sales five years before. Much of that was due to market growth in Europe, where sales increased by 47 percent in a single year. Now that JLG has stronger distribution, international sales should soon account for half of its business.[11]

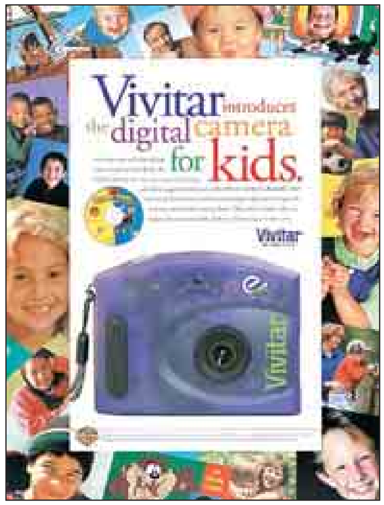
Find better trends in variables

Unfavorable trends in the marketing environment at home—or favorable trends in other countries—may make international marketing particularly attractive. For example, population growth in the United States has slowed and income is leveling off. In other places in the world, population and income are increasing rapidly. Many U.S. firms can no longer rely on the constant market growth that once drove increased domestic sales. Growth—and perhaps even survival—will come only by aiming at more distant customers. It doesn't make sense to casually assume that all of the best opportunities exist "at home."[12]

Search for Opportunities Can Begin by Understanding Markets

Find breakthrough opportunities

A marketing manager who really understands a target market may see breakthrough opportunities. But a target market's real needs—and the breakthrough opportunities that can come from serving those needs—are not always obvious.



The Olympus pocket camera competes directly with other 35-mm cameras, but it may also compete in a broader product-market against Vivitar's digital camera for kids or even Sony's innovative Mavica, which stores digital pictures on a 3-inch CD-R.

What is a company's market?

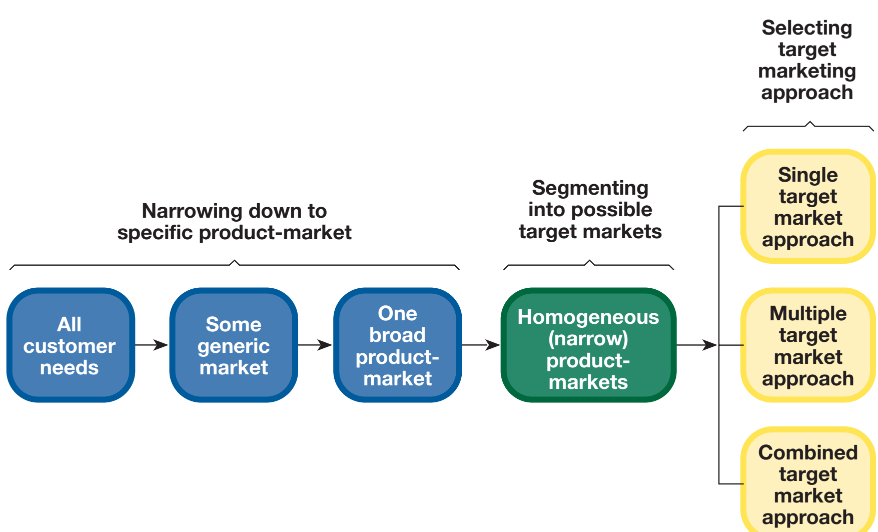
Identifying a company's market is an important but sticky issue. In general, a **market** is a group of potential customers with similar needs who are willing to exchange something of value with sellers offering various goods and/or services—that is, ways of satisfying those needs.

Marketing-oriented managers develop marketing mixes for *specific* target markets. Getting the firm to focus on specific target markets is vital. As shown in Exhibit 3-3, deciding on a specific target market involves a narrowing-down process—to get beyond production-oriented mass market thinking. But some managers don't understand this narrowing-down process.

Don't just focus on the product

Some production-oriented managers get into trouble because they ignore the tough part of defining markets. To make the narrowing-down process easier, they just describe their markets in terms of *products* they sell. For example, producers and retailers of

Exhibit 3-3
Narrowing Down to Target Markets



greeting cards might define their market as the "greeting-card" market. But this production-oriented approach ignores customers—and customers make a market! This also leads to missed opportunities. Hallmark isn't missing these opportunities. Instead, Hallmark aims at the "personal-expression" market. Hallmark stores offer all kinds of products that can be sent as "memory makers"—to express one person's feelings toward another. And as opportunities related to these needs change, Hallmark changes too. For example, at the Hallmark website (www.hallmark.com) it is easy to get shopping suggestions from an online "gift assistant," to order flowers, or to personalize an electronic greeting card to send over the Internet.[13]

From generic markets to product-markets

To understand the narrowing down process, it's useful to think of two basic types of markets. A **generic market** is a market with *broadly* similar needs—and sellers offering various—*often diverse*—ways of satisfying those needs. In contrast, a **product-market** is a market with *very* similar needs and sellers offering various *close substitute* ways of satisfying those needs.[14]

A generic market description looks at markets broadly and from a customer's viewpoint. Entertainment-seekers, for example, have several very different ways to satisfy their needs. An entertainment-seeker might buy a Sony satellite receiving system for a TV, sign up for a cruise on the Carnival Line, or reserve season tickets for the symphony. Any one of these *very different* products may satisfy this entertainment need. Sellers in this generic entertainment-seeker market have to focus on the need(s) the customers want satisfied—not on how one seller's product (satellite dish, vacation, or live music) is better than that of another producer.

It is sometimes hard to understand and define generic markets because *quite different product types may compete with each other.* For example, a person on a business trip to Italy might want a convenient way to record memories of the trip. Minolta's APS camera, Sony's digital camcorder, Kodak's PalmPix digital accessory for a Palm, and even postcards from local shops may all compete to serve our traveler's needs. If customers see all these products as substitutes—as competitors in the same generic market—then marketers must deal with this complication.

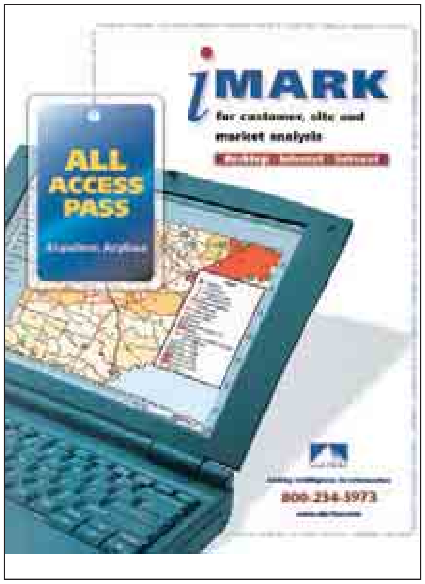
Suppose, however, that our traveler decides to satisfy this need with an APS camera. Then—in this product-market—Minolta, Kodak, Nikon, and many other brands may compete with each other for the customer's dollars. In this *product*-market concerned with APS format cameras *and* needs to conveniently record memories, consumers compare similar products to satisfy their image needs.

Broaden market definitions to find opportunities

Broader market definitions—including both generic market definitions and product-market definitions—can help firms find opportunities. But deciding *how* broad to go isn't easy. Too narrow a definition limits a firm's opportunities—but too broad a definition makes the company's efforts and resources seem insignificant. Consider, for example, the mighty Coca-Cola Company. It has great success and a huge market share in the U.S. cola-drinkers' market. On the other hand, its share of all beverage drinking worldwide is very small.

Here we try to match opportunities to a firm's resources and objectives. So the *relevant market for finding opportunities* should be bigger than the firm's present product-market—but not so big that the firm couldn't expand and be an important competitor. A small manufacturer of screwdrivers in Mexico, for example, shouldn't define its market as broadly as "the worldwide tool users market" or as narrowly as "our present screwdriver customers." But it may have the production and/or marketing potential to consider "the handyman's hand-tool market in North America." Carefully naming your product-market can help you see possible opportunities.

Understanding the geographic boundaries of a market can suggest new opportunities.



Naming Product-Markets and Generic Markets

Some managers think about markets just in terms of the product they already produce and sell. But this approach can lead to missed opportunities. For example, think about all of the minivans and SUVs that you see and how many cars they've replaced on the road. If Chrysler had been thinking only about the "car" market, the minivan opportunity might have been missed altogether. And as we've already highlighted with other examples in this chapter, instant film is being replaced with digital pictures, satellite TV is replacing cable, MP3 players are replacing portable CD players, and cell phones are replacing phone booths.

As this suggests, when evaluating opportunities, product-related terms do not—by themselves—adequately describe a market. A complete product-market definition includes a four-part description.

What:	**1. Product type (type of good and type of service)**
To meet what:	**2. Customer (user) needs**
For whom:	**3. Customer types**
Where:	**4. Geographic area**

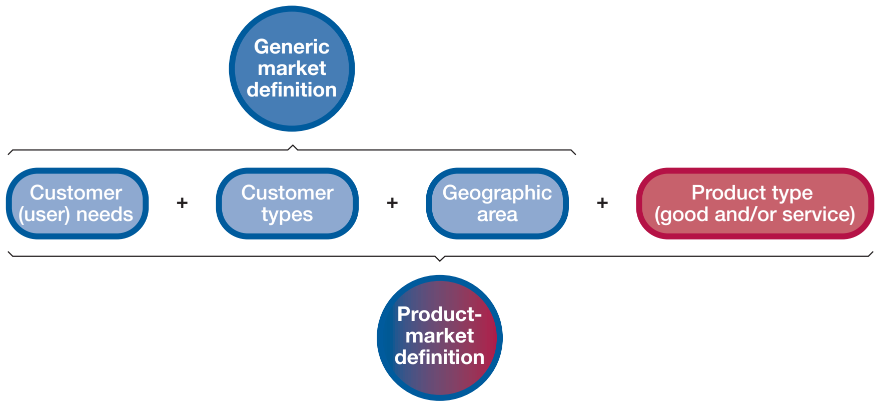
We refer to these four-part descriptions as product-market "names" because most managers label their markets when they think, write, or talk about them. Such a four-part definition can be clumsy, however, so we often use a nickname. And the nickname should refer to people—not products—because, as we emphasize, people make markets!

Product type should meet customer needs

Product type describes the goods and/or services that customers want. Sometimes the product type is strictly a physical good or strictly a service. But marketing managers who ignore the possibility that *both* are important can miss opportunities.

Customer (user) needs refer to the needs the product type satisfies for the customer. At a very basic level, product types usually provide functional benefits such as nourishing, protecting, warming, cooling, transporting, cleaning, holding,

Exhibit 3-4
Relationship between Generic and Product-Market Definitions



saving time, and so forth. Although we need to identify such "basic" needs first, in advanced economies, we usually go on to emotional needs—such as needs for fun, excitement, pleasing appearance, or status. Correctly defining the need(s) relevant to a market is crucial and requires a good understanding of customers. We discuss these topics more fully in Chapters 6 and 7. As a brief example, however, a buyer might want a small van to handle various cargo- and people-moving needs. The marketer would need to consider related needs such as economy in use, flexibility and convenience in changing the seat arrangement, and comfort for the driver and passengers.

Customer type refers to the final consumer or user of a product type. Here we want to choose a name that describes all present (possible) types of customers. To define customer type, marketers should identify the final consumer or user of the product type, rather than the buyer—if they are different. For instance, producers should avoid treating middlemen as a customer type—unless middlemen actually use the product in their own business.

The *geographic area* is where a firm competes—or plans to compete—for customers. Naming the geographic area may seem trivial, but understanding geographic boundaries of a market can suggest new opportunities. A firm aiming only at the domestic market, for example, may want to expand into world markets.

No product type in generic market names

A generic market description *doesn't include any product-type terms*. It consists of only three parts of the product-market definition—without the product type. This emphasizes that any product type that satisfies the customer's needs can compete in a generic market. Exhibit 3-4 shows the relationship between generic market and product-market definitions.

Later we'll study the many possible dimensions for segmenting markets. But for now you should see that defining markets only in terms of current products is not the best way to find new opportunities.

Market Segmentation Defines Possible Target Markets

Market segmentation is a two-step process

Market segmentation is a two-step process of: (1) *naming* broad product-markets and (2) *segmenting* these broad product-markets in order to select target markets and develop suitable marketing mixes.

This two-step process isn't well understood. First-time market segmentation efforts often fail because beginners start with the whole mass market and try to find

Opel's seven-seat compact van features the "Flex-7" seating system that allows one person to easily change the interior space to meet various cargo and people-moving needs.

one or two demographic characteristics to segment this market. Customer behavior is usually too complex to be explained in terms of just one or two demographic characteristics. For example, not all elderly men buy the same products or brands. Other dimensions usually must be considered—starting with customer needs.

Naming broad product-markets is disaggregating

The first step in effective market segmentation involves naming a broad product-market of interest to the firm. Marketers must break apart—disaggregate—all possible needs into some generic markets and broad product-markets in which the firm may be able to operate profitably. See Exhibit 3-3. No one firm can satisfy everyone's needs. So the naming—disaggregating—step involves brainstorming about very different solutions to various generic needs and selecting some broad areas—broad product-markets—where the firm has some resources and experience. This means that a car manufacturer would probably ignore all the possible opportunities in food and clothing markets and focus on the generic market, "transporting people in the world," and probably on the broad product-market, "cars, trucks, and utility vehicles for transporting people in the world."

Disaggregating, a practical rough-and-ready approach, tries to narrow down the marketing focus to product-market areas where the firm is more likely to have a competitive advantage or even to find breakthrough opportunities.

Market grid is a visual aid to market segmentation

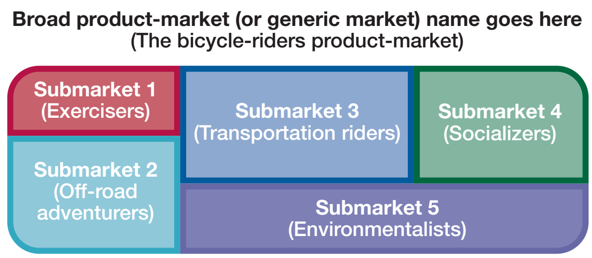
Assuming that any broad product-market (or generic market) may consist of submarkets, picture a market as a rectangle with boxes that represent the smaller, more homogeneous product-markets.

Exhibit 3-5, for example, represents the broad product-market of bicycle riders. The boxes show different submarkets. One submarket might focus on people who want basic transportation, another on people who want exercise, and so on. Alternatively, in the generic "transporting market" discussed above, we might see different product-markets of customers for bicycles, motorcycles, cars, airplanes, ships, buses, and "others."

Segmenting is an aggregating process

Marketing-oriented managers think of **segmenting** as an aggregating process—clustering people with similar needs into a "market segment." A **market segment** is a (relatively) homogeneous group of customers who will respond to a marketing mix in a similar way.

Exhibit 3-5
A Market Grid Diagram with Submarkets



This part of the market segmentation process (see Exhibit 3-3) takes a different approach from the naming part. Here we look for similarities rather than basic differences in needs. Segmenters start with the idea that each person is one of a kind but that it may be possible to aggregate some similar people into a product-market.

Segmenters see each of these one-of-a-kind people as having a unique set of dimensions. Consider a product-market in which customers' needs differ on two important segmenting dimensions: need for status and need for dependability. In Exhibit 3-6A, each dot shows a person's position on the two dimensions. While each person's position is unique, many of these people are similar in terms of how much status and dependability they want. So a segmenter may aggregate them into three (an arbitrary number) relatively homogeneous submarkets—A, B, and C. Group A might be called "status-oriented" and Group C "dependability-oriented." Members of Group B want both and might be called the "demanders."

How far should the aggregating go?

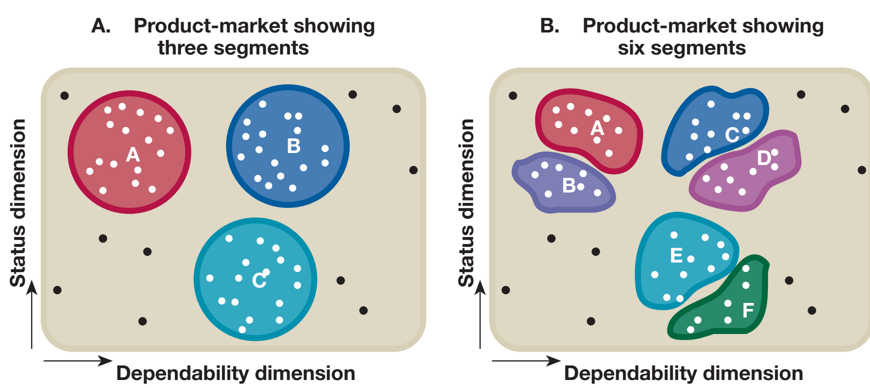
The segmenter wants to aggregate individual customers into some workable number of relatively homogeneous target markets and then treat each target market differently.

Look again at Exhibit 3-6A. Remember we talked about three segments. But this was an arbitrary number. As Exhibit 3-6B shows, there may really be six segments. What do you think—does this broad product-market consist of three segments or six?

Another difficulty with segmenting is that some potential customers just don't fit neatly into market segments. For example, not everyone in Exhibit 3-6B was put into one of the groups. Forcing them into one of the groups would have made these segments more heterogeneous and harder to please. Further, forming additional segments for them probably wouldn't be profitable. They are too few and not very similar in terms of the two dimensions. These people are simply too unique to be catered to and may have to be ignored—unless they are willing to pay a high price for special treatment.

The number of segments that should be formed depends more on judgment than on some scientific rule. But the following guidelines can help.

Exhibit 3-6
Every Individual Has His or Her Own Unique Position in a Market—Those with Similar Positions Can Be Aggregated into Potential Target Markets



Heinz Introduced "talking labels" on the bottles of its popular ketchup—and featured the change in print ads—as part of a global campaign to give the brand an edgy attitude and increase consumption among Heinz's teen target market.

Criteria for segmenting a broad product-market

Ideally, "good" market segments meet the following criteria:

1. *Homogeneous (similar) within*—the customers in a market segment should be as similar as possible with respect to their likely responses to marketing mix variables *and* their segmenting dimensions.
2. *Heterogeneous (different) between*—the customers in different segments should be as different as possible with respect to their likely responses to marketing mix variables *and* their segmenting dimensions.
3. *Substantial*—the segment should be big enough to be profitable.
4. *Operational*—the segmenting dimensions should be useful for identifying customers and deciding on marketing mix variables.

It is especially important that segments be *operational.* This leads marketers to include demographic dimensions such as age, sex, income, location, and family size. In fact, it is difficult to make some Place and Promotion decisions without such information.

Avoid segmenting dimensions that have no practical operational use. For example, you may find a personality trait such as moodiness among the traits of heavy buyers of a product, but how could you use this fact? Salespeople can't give a personality test to each buyer. Similarly, advertising couldn't make much use of this information. So although moodiness might be related in some way to previous purchases, it would not be a useful dimension for segmenting.

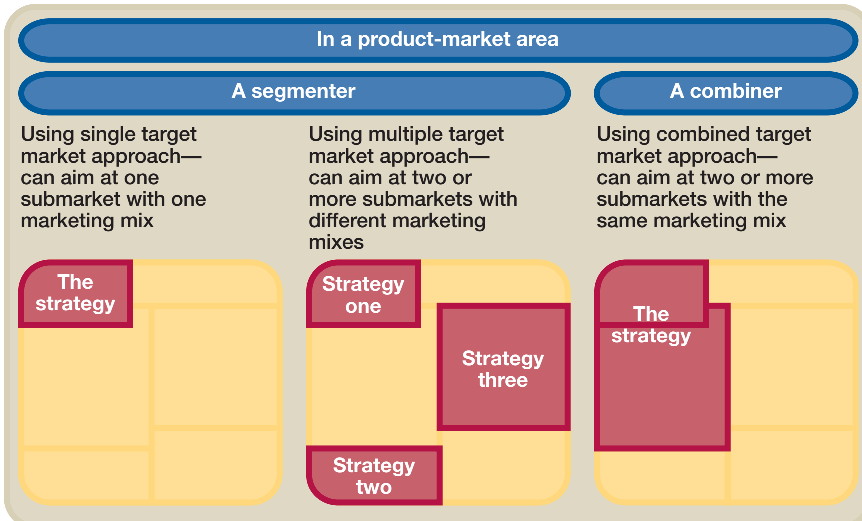
Target marketers aim at specific targets

Once you accept the idea that broad product-markets may have submarkets, you can see that target marketers usually have a choice among many possible target markets.

There are three basic ways to develop market-oriented strategies in a broad product-market.

1. The **single target market approach**—segmenting the market and picking one of the homogeneous segments as the firm's target market.
2. The **multiple target market approach**—segmenting the market and choosing two or more segments, then treating each as a separate target market needing a different marketing mix.
3. The **combined target market approach**—combining two or more submarkets into one larger target market as a basis for one strategy.

Exhibit 3-7
Target Marketers Have Specific Aims



Note that all three approaches involve target marketing. They all aim at specific, clearly defined target markets. See Exhibit 3-7. For convenience, we call people who follow the first two approaches the "segmenters" and people who use the third approach the "combiners."

Combiners try to satisfy "pretty well"

Combiners try to increase the size of their target markets by combining two or more segments. Combiners look at various submarkets for similarities rather than differences. Then they try to extend or modify their basic offering to appeal to these "combined" customers with just one marketing mix. See Exhibit 3-7. For example, combiners may try a new package, more service, a new brand, or new flavors. But even if they make product or other marketing mix changes, they don't try to satisfy unique smaller submarkets. Instead, combiners try to improve the general appeal of their marketing mix to appeal to a bigger "combined" target market.

A combined target market approach may help achieve some economies of scale. It may also require less investment than developing different marketing mixes for different segments—making it especially attractive for firms with limited resources.

Too much combining is risky

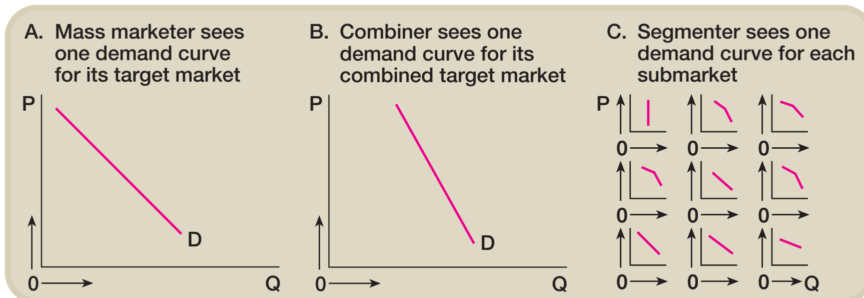
It is tempting to aim at larger combined markets instead of using different marketing mixes for smaller segmented markets. But combiners must be careful not to aggregate too far. As they enlarge the target market, individual differences within each submarket may begin to outweigh the similarities. This makes it harder to develop marketing mixes that can satisfy potential customers.

A combiner faces the continual risk of innovative segmenters chipping away at the various segments of the combined target market—by offering more attractive marketing mixes to more homogeneous submarkets. ATI Technologies, a firm that is a leader in making graphics chips for PCs, saw this happen. It produces high-quality products with features desired by a very wide variety of computer users. But ATI has lost business to more specialized competitors like Nvidia Corp. By focusing on the needs of video-game lovers who don't want to compromise when it comes to realistic special effects, Nvidia has developed chips that do fewer things. Still, Nvidia's chips do those fewer specialized things really well.

Segmenters try to satisfy "very well"

Segmenters aim at one or more homogeneous segments and try to develop a different marketing mix for each segment. Segmenters usually adjust their marketing

Exhibit 3-8
There May Be Different Demand Curves in Different Market Segments



mixes for each target market—perhaps making basic changes in the product itself—because they want to satisfy each segment very well.

Instead of assuming that the whole market consists of a fairly similar set of customers (like the mass marketer does) or merging various submarkets together (like the combiner), a segmenter sees submarkets with their own demand curves—as shown in Exhibit 3-8. Segmenters believe that aiming at one—or some—of these smaller markets makes it possible to provide superior value and satisfy them better. This then provides greater profit potential for the firm.

Segmenting may produce bigger sales

Note that segmenters are not settling for a smaller sales potential or lower profits. Instead, they hope to increase sales by getting a much larger share of the business in the market(s) they target. A segmenter who really satisfies the target market can often build such a close relationship with customers that it faces no real competition. A segmenter that offers a marketing mix precisely matched to the needs of the target market can often charge a higher price that produces higher profits.

Check Point Software Technologies, a company that makes firewall software to protect websites from hackers, is a good example. Microsoft, Cisco Systems, and most other firms that compete in Check Point's "computer security needs" market create sweeping sets of products to cover a host of corporate computing needs. But by focusing on a particular set of needs Check Point has become the leader in its market. The payoff is that its profit margins are even higher than those earned by Microsoft.[15]

Should you segment or combine?

Which approach should a firm use? This depends on the firm's resources, the nature of competition, and—most important—the similarity of customer needs, attitudes, and buying behavior.

In general, it's usually safer to be a segmenter—that is, to try to satisfy some customers *very* well instead of many just *fairly* well. That's why many firms use the single or multiple target market approach instead of the combined target market approach. Procter & Gamble, for example, offers many products that seem to compete directly with each other (e.g., Tide versus Cheer or Crest versus Gleem). However, P&G offers tailor-made marketing mixes to each submarket large—and profitable—enough to deserve a separate marketing mix. Though extremely effective, this approach may not be possible for a smaller firm with more limited resources. A smaller firm may have to use the single target market approach—focusing all its efforts at the one submarket niche where it sees the best opportunity.[16]

Kaepa, Inc., is a good example. Sales of its all-purpose sneakers plummeted as larger firms like Nike and Reebok stole customers with a multiple target market approach. They developed innovative products and aimed their promotion at specific needs—like jogging, aerobics, cross-training, and walking. Kaepa turned things around by catering to the needs of cheerleaders. Cheerleading squads can order

Ivillage.com's website focuses on women to do a better job in meeting their specific needs.

Kaepa shoes with custom team logos and colors. The soles of the shoes feature finger grooves that make it easier for cheerleaders to build human pyramids. The Kaepa website (www.kaepa.com) attracts the cheerleader target market with links to a host of other cheering sites. Kaepa also carefully targets its market research and promotion. Kaepa salespeople attend the cheerleading camps that each summer draw 40,000 enthusiasts. Kaepa even arranges for the cheering teams it sponsors to do demos at retail stores. This generates publicity and pulls in buyers, so retailers put more emphasis on the Kaepa line.[17]

Profit is the balancing point

In practice, cost considerations probably encourage more aggregating—to obtain economies of scale—while demand considerations suggest less aggregating—to satisfy needs more exactly.

Profit is the balancing point. It determines how unique a marketing mix the firm can afford to offer to a particular group.

What Dimensions Are Used to Segment Markets?

Segmenting dimensions guide marketing mix planning

Market segmentation forces a marketing manager to decide which product-market dimensions might be useful for planning marketing strategies. The dimensions should help guide marketing mix planning. Exhibit 3-9 shows the basic kinds of dimensions we'll be talking about in Chapters 5 and 6—and their probable effect on the four Ps. Ideally, we want to describe any potential product-market in terms of all three types of customer-related dimensions—plus a product type description—because these dimensions help us develop better marketing mixes.

Many segmenting dimensions may be considered

Customers can be described by many specific dimensions. Exhibit 3-10 shows some dimensions useful for segmenting consumer markets. A few are behavioral dimensions, others are geographic and demographic. Exhibit 3-11 shows some additional dimensions for segmenting markets when the customers are businesses, government agencies, or other types of organizations. Regardless of whether

Exhibit 3-9 Relation of Potential Target Market Dimensions to Marketing Strategy Decision Areas

Potential Target Market Dimensions	Effects on Strategy Decision Areas
1. Behavioral needs, attitudes and how present and potential goods and services fit into customers' consumption patterns.	Affects *Product* (features, packaging, product line assortment, branding) and *Promotion* (what potential customers need and want to know about the firm's offering, and what appeals should be used).
2. Urgency to get need satisfied and desire and willingness to seek information, compare, and shop.	Affects *Place* (how directly products are distributed from producer to customer, how extensively they are made available, and the level of service needed) and *Price* (how much potential customers are willing to pay).
3. Geographic location and other demographic characteristics of potential customers.	Affects size of *Target Markets* (economic potential), *Place* (where products should be made available), and *Promotion* (where and to whom to target advertising and personal selling).

customers are final consumers or organizations, segmenting a broad product-market may require using several different dimensions at the same time.[18]

What are the qualifying and determining dimensions?

To select the important segmenting dimensions, think about two different types of dimensions. **Qualifying dimensions** are those relevant to including a customer type in a product-market. **Determining dimensions** are those that actually affect the customer's purchase of a specific product or brand in a product-market.

A prospective car buyer, for example, has to have enough money—or credit—to buy a car and insure it. Our buyer also needs a driver's license. This still doesn't guarantee a purchase. He or she must have a real need—like a job that requires "wheels" or kids who have to be carpooled. This need may motivate the purchase of *some* car. But these qualifying dimensions don't determine what specific brand or model car the person might buy. That depends on more specific interests—such as the kind of safety, performance, or appearance the customer wants. Determining dimensions related to these needs affect the specific car the customer purchases. If safety is a determining dimension for a customer, a Volvo wagon that offers side impact protection, airbags, and all-wheel drive might be the customer's first choice.

Any hiking boot should repel water, and a product that doesn't meet that "qualifying need" probably wouldn't appeal to many hikers. Sorel wants its target customers to know that its boots go further in keeping feet dry because that difference may determine which brand of boot they buy.

Exhibit 3-10 Possible Segmenting Dimensions and Typical Breakdowns for Consumer Markets

Behavioral	
Needs	Economic, functional, physiological, psychological, social, and more detailed needs.
Benefits sought	Situation specific, but to satisfy specific or general needs.
Thoughts	Favorable or unfavorable attitudes, interests, opinions, beliefs.
Rate of use	Heavy, medium, light, nonusers.
Purchase relationship	Positive and ongoing, intermittent, no relationship, bad relationship.
Brand familiarity	Insistence, preference, recognition, nonrecognition, rejection.
Kind of shopping	Convenience, comparison shopping, specialty, none (unsought product).
Type of problem-solving	Routinized response, limited, extensive.
Information required	Low, medium, high.
Geographic	
Region of world, country	North America (United States, Canada), Europe (France, Italy, Germany), and so on.
Region in country	(Examples in United States): Pacific, Mountain, West North Central, West South Central, East North Central, East South Central, South Atlantic, Middle Atlantic, New England.
Size of city	No city; population under 5,000; 5,000–19,999; 20,000–49,999; 50,000–99,999; 100,000–249,999; 250,000–499,999; 500,000–999,999; 1,000,000–3,999,999; 4,000,000 or over.
Demographic	
Income	Under $5,000; $5,000–9,999; $10,000–14,999; $15,000–19,999; $20,000–29,999; $30,000–39,999; $40,000–59,999; $60,000 and over.
Sex	Male, female.
Age	Infant; under 6; 6–11; 12–17; 18–24; 25–34; 35–49; 50–64; 65 or over.
Family size	1, 2, 3–4, 5 or more.
Family life cycle	Young, single; young, married, no children; young, married, youngest child under 6; young, married, youngest child over 6; older, married, with children; older, married, no children under 18; older, single; other variations for single parents, divorced, etc.
Occupation	Professional and technical; managers, officials, and proprietors; clerical sales; craftspeople, foremen; operatives; farmers; retired; students; housewives; unemployed.
Education	Grade school or less; some high school; high school graduate; some college; college graduate.
Ethnicity	Asian, Black, Hispanic, Native American, White, Multiracial.
Social class	Lower-lower, upper-lower, lower-middle, upper-middle, lower-upper, upper-upper.

Note: Terms used in this table are explained in detail later in the text.

Determining dimensions may be very specific

How specific the determining dimensions are depends on whether you are concerned with a general product type or a specific brand. See Exhibit 3-12. The more specific you want to be, the more particular the determining dimensions may be. In a particular case, the determining dimensions may seem minor. But they are important because they *are* the determining dimensions.

Marketers at General Mills know this. Lots of people try to check e-mail or drive a car while eating breakfast or lunch. General Mills has figured out that for many of these target customers the real determining dimension in picking a snack is whether it can be eaten "one-handed."[19]

Determining dimensions may change

A marketing manager should seek new ways to serve existing customers and strengthen the relationship with them. Too often firms let their strategies get stagnant after they've established a base of customers and a set of marketing mix decisions. For example, special business services—like voice mail—related to the determining needs of upscale executives might initially help a motel win this business. However, the motel will lose its competitive edge if other motels start to offer the same benefits. Then, the determining dimensions change. To retain its

Exhibit 3-11 Possible Segmenting Dimensions for Business/Organizational Markets

Kind of relationship	Weak loyalty → strong loyalty to vendor Single source → multiple vendors “Arm’s length” dealings → close partnership No reciprocity → complete reciprocity
Type of customer	Manufacturer, service producer, government agency, military, nonprofit, wholesaler or retailer (when end user), and so on.
Demographics	Geographic location (region of world, country, region within country, urban → rural) Size (number of employees, sales volume) Primary business or industry (North American Industry Classification System) Number of facilities
How customer will use product	Installations, components, accessories, raw materials, supplies, professional services
Type of buying situation	Decentralized → centralized Buyer → multiple buying influence Straight rebuy → modified rebuy → new-task buying
Purchasing methods	Vendor analysis, purchasing specifications, Internet bids, negotiated contracts, long-term contracts, e-commerce websites

Note: Terms used in this table are explained in detail later in the text.

customers, the motel needs to find new and better ways to meet needs. For example, the motel might make it easier for traveling executives by providing high-speed Internet access for their use during a stay.[20]

Qualifying dimensions are important too

The qualifying dimensions help identify the “core features” that must be offered to everyone in a product-market. Qualifying and determining dimensions work together in marketing strategy planning.

Different dimensions needed for different submarkets

Note that each different submarket within a broad product-market may be motivated by a different set of dimensions. In the snack food market, for example, health food enthusiasts are interested in nutrition, dieters worry about calories, and economical shoppers with lots of kids may want volume to “fill them up.”

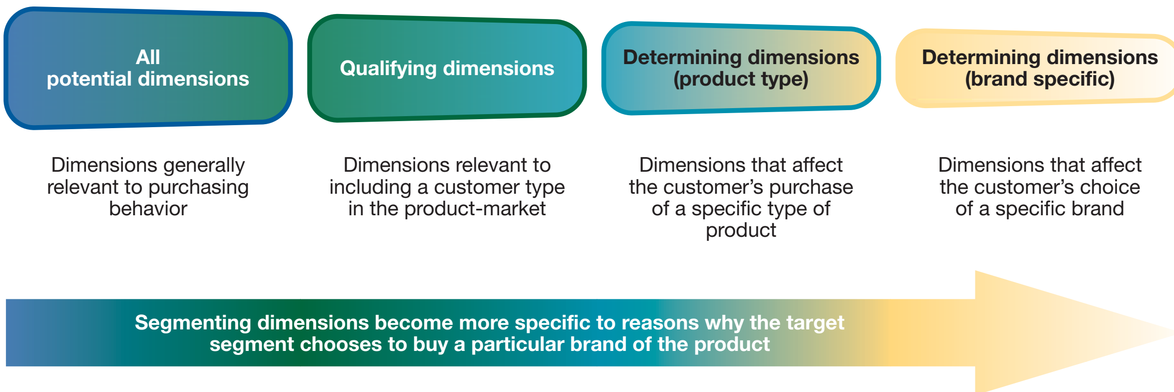
Ethical issues in selecting segmenting dimensions

Marketing managers sometimes face ethical decisions when selecting segmenting dimensions. Problems may arise if a firm targets customers who are somehow at a disadvantage in dealing with the firm or who are unlikely to see the negative effects of their own choices. For example, some people criticize shoe companies for targeting poor, inner-city kids who see expensive athletic shoes as an important status symbol. Many firms, including producers of infant formula, have been criticized for targeting consumers in less-developed nations. Encyclopedia publishers have been criticized for aggressive selling to less-educated parents who don’t realize that the “pennies a day” credit terms are more than they can afford. Some nutritionists criticize firms that market soft drinks, candy, and snack foods to children.

Sometimes a marketing manager must decide whether a firm should serve customers it really doesn’t want to serve. For example, banks sometimes offer marketing mixes that are attractive to wealthy customers but that basically drive off low-income consumers.

People often disagree about what segmenting dimensions are ethical in a given situation. A marketing manager needs to consider not only his or her own views

Exhibit 3-12 Finding the Relevant Segmenting Dimensions



but also the views of other groups in society. Even when there is no clear "right" answer, negative publicity may be very damaging. This is what Amazon.com encountered when it was revealed that it was charging some regular customers higher prices than new customers at its site.[21]

International marketing requires even more segmenting

Success in international marketing requires even more attention to segmenting. There are over 228 nations with their own unique cultures! And they differ greatly in language, customs (including business ethics), beliefs, religions, race, and income distribution patterns. (We'll discuss some of these differences in Chapters 5 and 6.) These additional differences can complicate the segmenting process. Even worse, critical data is often less available—and less dependable—as firms move into international markets. This is one reason why some firms insist that local operations and decisions be handled by natives. They, at least, have a feel for their markets.

There are more dimensions—but there is a way

Segmenting international markets may require more dimensions. But one practical method adds just one step to the approach discussed above. First, marketers segment by country or region—looking at demographic, cultural, and other characteristics, including stage of economic development. This may help them find regional or national submarkets that are fairly similar. Then—depending on whether the firm is aiming at final consumers or business markets—they apply the same basic approaches discussed earlier.

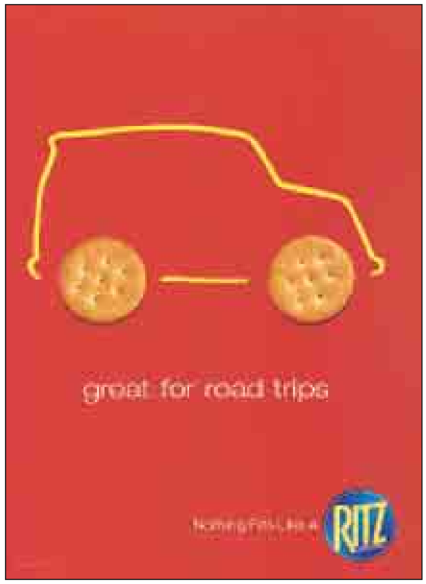
More Sophisticated Techniques May Help in Segmenting

Marketing researchers and managers often turn to computer-aided methods for help with the segmenting job. A detailed review of the possibilities is beyond the scope of this book. But a brief discussion will give you a flavor of how computer-aided methods work.

Clustering usually requires a computer

Clustering techniques try to find similar patterns within sets of data. Clustering groups customers who are similar on their segmenting dimensions into homogeneous segments. Clustering approaches use computers to do what previously was done with much intuition and judgment.

It is usually better to focus on the needs satisfied by products rather than on the product characteristics themselves.



The data to be clustered might include such dimensions as demographic characteristics, the importance of different needs, attitudes toward the product, and past buying behavior. The computer searches all the data for homogeneous groups of people. When it finds them, marketers study the dimensions of the people in the groups to see why the computer clustered them together. The results sometimes suggest new, or at least better, marketing strategies.[22]

A cluster analysis of the toothpaste market, for example, might show that some people buy toothpaste because it tastes good (the sensory segment), while others are concerned with the effect of clean teeth and fresh breath on their social image (the sociables). Still others worry about decay or tartar (the worriers), and some are just interested in the best value for their money (the value seekers). Each of these market segments calls for a different marketing mix—although some of the four Ps may be similar.

Customer database can focus the effort

A variation of the clustering approach is based on customer relationship management methods. With **customer relationship management (CRM),** the seller fine-tunes the marketing effort with information from a detailed customer database. This usually includes data on a customer's past purchases as well as other segmenting information. For example, an auto-repair garage that keeps a database of customer oil changes can send a reminder postcard when it's time for the next oil change. Similarly, a florist that keeps a database of customers who have ordered flowers for Mother's Day or Valentine's Day can call them in advance with a special offer. Firms that operate over the Internet may have a special advantage with these database-focused approaches. They are able to communicate with customers via a website or e-mail, which means that the whole effort is not only targeted but also very inexpensive. Further, it's fast and easy for a customer to reply.[23]

Amazon.com takes this even further. When a customer orders a book, the Amazon CRM system at the website recommends other related books that have been purchased by other customers who bought that book.

Herman Miller Takes a Back Seat to No One

Herman Miller (HM) is a 75-year-old company that makes office furniture. Boring stuff? Marketing managers at HM know that some office furniture customers feel that way. So, they decided to do something about it. Consider the success of the company's Aeron desk chair. In an e-commerce world even top executives sit at computers and need a desk chair created for both work and looks. To satisfy this upscale segment, HM designed a new type of chair from scratch. There's no fabric or padding, but everything about it adjusts to your body. It's so comfortable that HM positioned it as "the chair you can wear." With a price tag close to $1,000, it became a status symbol for high-tech managers and was as profitable as it was popular. But with the cooling off of the economy, collapse of the dot-coms, and cutbacks by big firms, HM is looking for other new opportunities for growth. It's finding them with a new line, called Red, that targets new firms and small businesses. HM created a new division, SQA (which stands for Simple, Quick, Affordable), to serve this segment. The SQA factory does not offer the thousands of choices in fabrics and styles that were popular with HM's traditional, big corporate buyers. Nor do customers get extensive help from sales reps and dealers. However, the new product line, called Red, does offer bold colors and chic styles that give HM an advantage over suppliers like OfficeMax. Buyers place orders at a slick website (www.hermanmillerred.com) that displays a 3-D drawing of the buyer's office space and furniture choices. The orders are immediately linked into the factory production schedule, so delivery times are very fast. The efficiency of this system also reduces selling costs. That means that the line is still profitable even at Red's affordable price point. Competing firms are now chasing this same market segment, but with HM's head start a lot of them are just taking a back seat.[24]

www.mhhe.com/fourps

Differentiation and Positioning Take the Customer Point of View

Differentiate the marketing mix—to serve customers better

As we've emphasized throughout, the reason for focusing on a specific target market—by using marketing segmentation approaches or tools such as cluster analysis or CRM—is so that you can fine-tune the whole marketing mix to provide some group of potential customers with superior value. By *differentiating* the marketing mix to do a better job meeting customers' needs, the firm builds a competitive advantage. When this happens, target customers view the firm's position in the market as uniquely suited to their preferences and needs. Further, because everyone in the firm is clear about what position it wants to achieve with customers, the Product, Promotion, and other marketing mix decisions can be blended better to achieve the desired objectives.

Although the marketing manager may want customers to see the firm's offering as unique, that is not always possible. Me-too imitators may come along and copy the firm's strategy. Further, even if a firm's marketing mix is different, consumers may not know or care. They're busy and, simply put, the firm's product may not be that important in their lives. Even so, in looking for opportunities it's important for the marketing manager to know how customers *do* view the firm's offering. It's also important for the marketing manager to have a clear idea about how he or she would like for customers to view the firm's offering. This is where another important concept, *positioning,* comes in.

Positioning is based on customers' views

Positioning refers to how customers think about proposed and/or present brands in a market. A marketing manager needs a realistic view of how customers think about offerings in the market. Without that, it's hard to differentiate. At the same time, the manager should know how he or she *wants* target customers to think about the firm's marketing mix. Positioning issues are especially important when competitors in a market appear to be very similar. For example, many people think that there isn't much difference between one brand of TV and another. But Sony wants TV buyers to see its Wega flat-screen as offering the very best picture.

Firms often use promotion to help "position" how a marketing mix meets target customers' specific needs. For example, Bic ads along the roadside in Thailand highlight an ultra-close shave. In the U.S., Target wants consumers to remember not only its soft goods but also its houseware lines.

Once you know what customers think, then you can decide whether to leave the product (and marketing mix) alone or reposition it. This may mean *physical changes* in the product or simply *image changes based on promotion*. For example, most cola drinkers can't pick out their favorite brand in a blind test—so physical changes might not be necessary (and might not even work) to reposition a cola. Yet, ads that portray Pepsi drinkers in funny situations help position "the Joy of Pepsi." Conversely, 7-Up reminds us that it is the uncola with no caffeine, "never had it and never will."

Internet

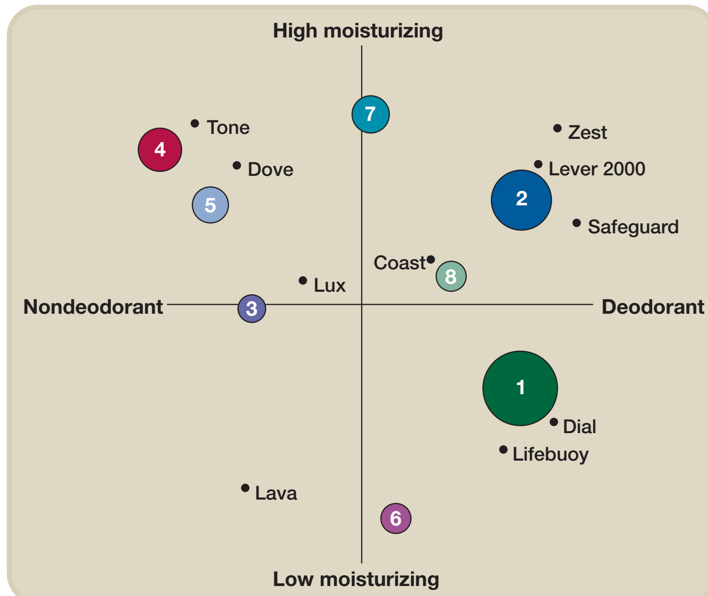
Internet Exercise For years, Volvo has had a reputation as a particularly safe car and much of its advertising has reinforced that positioning. Go to the website for Volvo cars (www.volvocars.com) and select the link for the U.S. website. Consider whether the U.S. website successfully reinforces a positioning of Volvo as a "safe" alternative. Why or why not?

Figuring out what customers really think about competing products isn't easy, but there are approaches that help. Most of them require some formal marketing research. The results are usually plotted on graphs to help show how consumers view the competing products. Usually, the products' positions are related to two or three product features that are important to the target customers.

Managers make the graphs for positioning decisions by asking consumers to make judgments about different brands—including their "ideal" brand—and then use computer programs to summarize the ratings and plot the results. The details of positioning techniques—sometimes called "perceptual mapping"—are beyond the scope of this text. But Exhibit 3-13 shows the possibilities.[25]

Exhibit 3-13 shows the "product space" for different brands of bar soap using two dimensions—the extent to which consumers think the soaps moisturize and deodorize their skin. For example, consumers see Dial as quite low on moisturizing but high on deodorizing. Lifebuoy and Dial are close together—implying that consumers think of them as similar on these characteristics. Dove is viewed as

Exhibit 3-13
"Product Space" Representing Consumers' Perceptions for Different Brands of Bar Soap



different and is further away on the graph. Remember that positioning maps are based on *customers' perceptions*—the actual characteristics of the products (as determined by a chemical test) might be different!

Each segment may have its own preferences

The circles in Exhibit 3-13 show different sets (submarkets) of consumers clustered near their ideal soap preferences. Groups of respondents with a similar ideal product are circled to show apparent customer concentrations. In this graph, the size of the circles suggests the size of the segments for the different ideals.

Ideal clusters 1 and 2 are the largest and are close to two popular brands—Dial and Lever 2000. It appears that customers in cluster 1 want more moisturizing than they see in Dial and Lifebuoy. However, exactly what these brands should do about this isn't clear. Perhaps both of these brands should leave their physical products alone—but emphasize moisturizing more in their promotion to make a stronger appeal to those who want moisturizers. A marketing manager talking about this approach might simply refer to it as "positioning the brand as a good moisturizer." Of course, whether the effort is successful depends on whether the whole marketing mix delivers on the promise of the positioning communication.

Note that ideal cluster 7 is not near any of the present brands. This may suggest an opportunity for introducing a new product—a strong moisturizer with some deodorizers. A firm that chooses to follow this approach would be making a segmenting effort.

Combining versus segmenting

Positioning analysis may lead a firm to combining—rather than segmenting—if managers think they can make several general appeals to different parts of a "combined" market. For example, by varying its promotion, Coast might try to appeal to segments 8, 1, and 2 with one product. These segments are all quite similar (close together) in what they want in an ideal brand. On the other hand, there may be clearly defined submarkets—and some parts of the market may be "owned" by one product or brand. In this case, segmenting efforts may be practical—moving the firm's own product into another segment of the general market area where competition is weaker.

Positioning as part of broader analysis

A positioning analysis helps managers understand how customers see their market. It is a visual aid to understanding a product-market. The first time such an analysis is done, managers may be shocked to see how much customers' perceptions of a market differ from their own. For this reason alone, positioning analysis may be crucial. But, a positioning analysis usually focuses on specific product features and brands that are close competitors in the product-market. Thus, it is a product-oriented approach. Important *customer*-related dimensions—including needs and attitudes—may be overlooked.

Premature emphasis on product features is dangerous in other ways as well. As our bar soap example shows, starting with a product-oriented definition of a market and how bar soaps compete against other bar soaps can make a firm miss more basic shifts in markets. For example, bars might be losing popularity to liquid soaps. Or other products, like bath oils or body shampoos for use in the shower, may be part of the relevant competition. Managers wouldn't see these shifts if they looked only at alternative bar soap brands—the focus is just too narrow.

It's also important to realize that the way consumers look at a product isn't just a matter of chance. Let's return to our bar soap example. While many consumers do think about soap in terms of moisturizing and deodorizing, other needs shouldn't be overlooked. For example, some consumers are especially concerned about wiping out germs. Marketers for Dial soap recognized this need and developed ads that positioned Dial as "the choice" for these target customers.

As we emphasize throughout the text, you must understand potential needs and attitudes when planning marketing strategies. If customers treat different products as substitutes, then a firm has to position itself against those products too. Customers won't always be conscious of all of the detailed ways that a firm's marketing mix might be different, but careful positioning can help highlight a unifying theme or benefits that relate to the determining dimensions of the target market. Thus, it's useful to think of positioning as part of the broader strategy planning process—because the purpose is to ensure that the whole marketing mix is positioned for competitive advantage.

Conclusion

Firms need creative strategy planning to survive in our increasingly competitive markets. In this chapter, we discussed how to find attractive target market opportunities. We started by considering four basic types of opportunities—market penetration, market development, product development, and diversification—with special emphasis on opportunities in international markets. We also saw that carefully defining generic markets and product-markets can help find new opportunities. We stressed the shortcomings of a too narrow, product-oriented view of markets.

We also discussed market segmentation—the process of naming and then segmenting broad product-markets to find potentially attractive target markets. Some people try to segment markets by starting with the mass market and then dividing it into smaller submarkets based on a few dimensions. But this can lead to poor results. Instead, market segmentation should first focus on a broad product-market and then group similar customers into homogeneous submarkets. The more similar the potential customers are, the larger the submarkets can be. Four criteria for evaluating possible product-market segments were presented.

Once a broad product-market is segmented, marketing managers can use one of three approaches to market-oriented strategy planning: (1) the single target market approach, (2) the multiple target market approach, and (3) the combined target market approach. In general, we encouraged marketers to be segmenters rather than combiners.

We also discussed some computer-aided approaches—clustering techniques, CRM, and positioning.

In summary, good marketers should be experts on markets and likely segmenting dimensions. By creatively segmenting markets, they may spot opportunities—even breakthrough opportunities—and help their firms succeed against aggressive competitors offering similar products. Segmenting is basic to target marketing. And the more you practice segmenting, the more meaningful market segments you will see.

Questions and Problems

1. Distinguish between an attractive opportunity and a breakthrough opportunity. Give an example.
2. Explain how new opportunities may be seen by defining a firm's markets more precisely. Illustrate for a situation where you feel there is an opportunity—namely, an unsatisfied market segment—even if it is not very large.
3. In your own words, explain why the book suggests that you should think of marketing strategy planning as a narrowing down process.
4. Distinguish between a generic market and a product-market. Illustrate your answer.
5. Explain the major differences among the four basic types of opportunities discussed in the text and cite examples for two of these types of opportunities.
6. Explain why a firm may want to pursue a market penetration opportunity before pursuing one involving product development or diversification.
7. In your own words, explain several reasons why marketing managers should consider international markets when evaluating possible opportunities.
8. Give an example of a foreign-made product (other than an automobile) that you personally have purchased. Give some reasons why you purchased that product. Do you think that there was a good opportunity for a domestic firm to get your business? Explain why or why not.
9. Explain what market segmentation is.
10. List the types of potential segmenting dimensions and explain which you would try to apply first, second, and third in a particular situation. If the nature of the situation would affect your answer, explain how.
11. Explain why segmentation efforts based on attempts to divide the mass market using a few demographic dimensions may be very disappointing.
12. Illustrate the concept that segmenting is an aggregating process by referring to the admissions policies of your own college and a nearby college or university.
13. Review the types of segmenting dimensions listed in Exhibits 3-10 and 3-11, and select the ones you think should be combined to fully explain the market segment you personally would be in if you were planning to buy a new watch today. List several dimensions and try to develop a shorthand name, like "fashion-oriented," to describe your own personal market segment. Then try to estimate what proportion of the total watch market would be accounted for by your market segment. Next, explain if there are any offerings that come close to meeting the needs of your market. If not, what sort of a marketing mix is needed? Would it be economically attractive for anyone to try to satisfy your market segment? Why or why not?
14. Identify the determining dimension or dimensions that explain why you bought the specific brand you did in your most recent purchase of a *(a)* soft drink, *(b)* shampoo, *(c)* shirt or blouse, and *(d)* larger, more expensive item, such as a bicycle, camera, or boat. Try to express the determining dimension(s) in terms of your own personal characteristics rather than the product's characteristics. Estimate what share of the market would probably be motivated by the same determining dimension(s).
15. Consider the market for off-campus apartments in your city. Identify some submarkets that have different needs and determining dimensions. Then evaluate how well the needs in these market segments are being met in your geographic area. Is there an obvious breakthrough opportunity waiting for someone?
16. Explain how positioning analysis can help a marketing manager identify target market opportunities.

Suggested Cases

7. Lilybank Lodge
29. Metal Works, Inc.
30. Deluxe Foods, Ltd.

Computer-Aided Problem

3. **Segmenting Customers**

The marketing manager for Audiotronics Software Company is seeking new market opportunities. He is focusing on the voice recognition market and has narrowed down to three segments: the Fearful Typists, the Power Users, and the Professional Specialists. The Fearful Typists don't know much about computers—they just want a fast way to create e-mail messages, letters, and simple reports without errors. They don't need a lot of special features. They want simple instructions and a program that's easy to learn. The Power Users know a lot about computers, use them often, and want a voice recognition program with many special features. All computer programs seem easy to them—so they aren't worried about learning to use the various features. The Professional Specialists have jobs that require a lot of writing. They don't know much about computers but are willing to learn. They want special features needed for their work—but only if they aren't too hard to learn and use.

The marketing manager prepared a table summarizing the importance of each of three key needs in the three segments (see table below).

Market Segment	Importance of Need (1 = Not Important; 10 = Very Important)		
	Features	Easy to Use	Easy to Learn
Fearful Typists	3	8	9
Power Users	9	2	2
Professional Specialists	7	5	6

Audiotronics' sales staff conducted interviews with seven potential customers who were asked to rate how important each of these three needs were in their work. The manager prepared a spreadsheet to help him cluster (aggregate) each person into one of the segments—along with other similar people. Each person's ratings are entered in the spreadsheet, and the clustering procedure computes a similarity score that indicates how similar (a low score) or dissimilar (a high score) the person is to the typical person in each of the segments. The manager can then "aggregate" potential customers into the segment that is most similar (that is, the one with the *lowest* similarity score).

a. *The ratings for a potential customer appear on the first spreadsheet. Into which segment would you aggregate this person?*
b. *The responses for seven potential customers who were interviewed are listed in the table below. Enter the ratings for a customer in the spreadsheet and then write down the similarity score for each segment. Repeat the process for each customer. Based on your analysis, indicate the segment into which you would aggregate each customer. Indicate the size (number of customers) of each segment.*
c. *In the interview, each potential customer was also asked what type of computer he or she would be using. The responses are shown in the table along with the ratings. Group the responses based on the customer's segment. If you were targeting the Fearful Typists segment, what type of computer would you focus on when developing your software?*
d. *Based on your analysis, which customer would you say is least like any of the segments? Briefly explain the reason for your choice.*

For additional questions related to this problem, see Exercise 3-4 in the *Learning Aid for Use with Basic Marketing*, 14th edition.

	Importance of Need (1 = Not Important; 10 = Very Important)			
Potential Customer	Features	Easy to Use	Easy to Learn	Type of Computer
A.	8	1	2	Dell laptop
B.	6	6	5	IBM desktop
C.	4	9	8	Apple
D.	2	6	7	Apple
E.	5	6	5	IBM desktop
F.	8	3	1	Dell laptop
G.	4	6	8	Apple

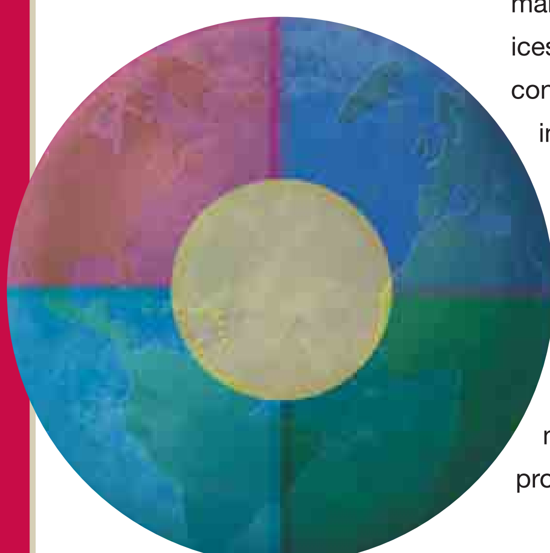
When You Finish This Chapter, You Should

1. Know the variables that shape the environment of marketing strategy planning.
2. Understand why company objectives are important in guiding marketing strategy planning.
3. See how the resources of a firm affect the search for opportunities.
4. Know how the different kinds of competitive situations affect strategy planning.
5. Understand how the economic and technological environment can affect strategy planning.
6. Know why you might be sent to prison if you ignore the political and legal environment.
7. Understand how to screen and evaluate marketing strategy opportunities.
8. Understand the important new terms (shown in red).

Chapter Four

Evaluating Opportunities in the Changing Marketing Environment

UPS is on a roll. But if you think it's just those clean brown trucks that are moving, think again. Top management's objective isn't just to be the leader in delivering packages, but also to be the world leader in delivering services and information to corporate clients to help them pare shipping, inventory, and handling costs, manage relationships with suppliers, and even bill their customers. To achieve these objectives, marketing managers at UPS are developing completely new marketing strategies for new services and markets, like logistics consulting and handling of digital invoices and payments.



These initiatives mean that UPS is no longer competing with just package delivery rivals like FedEx and DHL, but with a host of other firms that market information technology solutions for business problems. But UPS has resources

place

price

promotion

produc

and strengths that help in this competition. It has already earned the trust of many business customers with whom it has close working relationships. Its experience and expertise are a competitive advantage also. A decade ago, UPS began to make huge investments in information systems, mainly to make its own operations more efficient. However, when the Internet came along UPS quickly took advantage of the technology to make its package tracking databases available to customers (www.ups.com). For final consumers, this was just a nice benefit of using UPS. But for many business customers, knowing precisely where stuff was meant saving millions of dollars in inventory costs. That opened customers' eyes to the possibilities. Then UPS set up a special sales force to help firms link their e-commerce websites directly to UPS shipping data. That gave it more opportunities to see ways that UPS could improve a customer's distribution system. Now, for example, if you order a pair of Air Jordans at Nike.com, the order is instantly filled by UPS from Nike inventory maintained at a UPS warehouse in Kentucky—and UPS delivers the sneakers directly to you the next day. In fact, if there is any problem and you call the toll-free number on Nike's website, it's a UPS employee at a call center in San Antonio who answers your call.

Sometimes UPS logistics solutions don't even rely on UPS trucks. For example, Ford Motor Company has given UPS a contract to manage the transportation and distribution of over four million cars and trucks a year—from 21 different factories to 6,000 dealers across North America. Now a Ford dealer who wants to find a metallic blue Mustang convertible can instantly do it online. The UPS system also reduces transit time for a new Mustang from 16 days to 12. That frees up $1 billion worth of inventory and saves Ford $125 million a year in inventory carrying costs.

These successes are earning profits for UPS, but it still must cope with the challenges of a weakened economy. However, even when demand for package deliveries is low UPS has a profit advantage over competitors who are less efficient. A weak economy may even help the UPS strategic business unit that offers logistics consulting services because customer firms have an even greater need to pare costs. That is one reason the market for logistics consulting services is expected to grow threefold by 2005. Moreover, the trend toward free trade is helping UPS expand revenue from both international airfreight and the broker services it now offers to help firms cope with local customs laws.[1]

The Marketing Environment

You saw in the last chapter that using segmenting and positioning to narrow down to a specific marketing strategy takes a real understanding of what makes customers tick. You also saw that developing a competitive advantage and a strategy that offers customers superior value takes an understanding of the capabilities of your own company and of competitors. This chapter takes this thinking further. As the UPS case shows, a marketing manager must analyze customer needs and choose marketing strategy variables within the framework of the marketing environment and how it is changing.

A large number of forces shape the marketing environment. To help organize your thinking, it's useful to classify the various forces as falling into either (1) the direct market environment or (2) the external market environment. The direct environment of any generic market or product-market includes customers, the company, and competitors. The external market environment is broader. The variables of the external market environment fall into four major areas:

1. Economic environment.
2. Technological environment.
3. Political and legal environment.
4. Cultural and social environment.

In the short run, the marketing manager doesn't control the variables of the marketing environment. That's why it's sometimes useful to think of them as uncontrollable variables. On the other hand, the marketing manager can and should carefully consider the environmental variables when making decisions that can be controlled. For example, a manager may not be able to do anything to offset the strengths of a specific competitor, but the manager can select strategies that lead the firm into a new product-market where that firm does not compete, or where competition in general is not as strong. In this chapter, we'll look at these marketing environment variables in more detail. We'll see how they shape opportunities—limiting some possibilities and making others more attractive.

In creating its new website, Gap's objective was to complement and support its bricks and mortar stores rather than just cannibalize in-store sales. So, Gap Online features sizes and styles, like maternity clothes, that are not in stock in regular stores.

Objectives Should Set Firm's Course

A company must decide where it's going, or it may fall into the trap expressed so well by the quotation: "Having lost sight of our objective, we redoubled our efforts." Company objectives should shape the direction and operation of the whole business.

It is difficult to set objectives that really guide the present and future development of a company. The process forces top management to look at the whole business, relate its present objectives and resources to the external environment, and then decide what the firm wants to accomplish in the future.

The marketing manager should be heard when the company is setting objectives. But setting whole-company objectives—within resource limits—is ultimately the responsibility of top management. In this sense, whole-company objectives are usually outside the marketing manager's "control."

It would be convenient if a company could set one objective—such as making a profit—and let that serve as the guide. Actually, however, setting objectives is much more complicated, which helps explain why it's often done poorly—or not done at all.

Three basic objectives provide guidelines

The following three objectives provide a useful starting point for setting a firm's objectives. They should be sought *together* because in the long run a failure in even one of the three areas can lead to total failure of the business. A business should:

1. Engage in specific activities that will perform a socially and economically useful function.
2. Develop an organization to carry on the business and implement its strategies.
3. Earn enough profit to survive.[2]

Should be socially useful

The first objective isn't just a "do-gooder" objective. Businesses can't exist without the approval of consumers. If a firm's activities appear to be contrary to the consumer "good," the firm can be wiped out almost overnight by political or legal action—or consumers' own negative responses.

A firm should set need-satisfying objectives rather than production-oriented objectives. Because customer needs change, too narrow a view may lead the company into a product-market in which the product itself will soon be obsolete.[3]

Should earn some profit

A firm must make a profit to survive. But just saying that a firm should try to make a profit isn't enough. Management must specify the time period involved since many plans that maximize profit in the long run lose money during the first few years. Thousands of new dot.com firms went belly-up after a year or two of losses because they could not even cover their expenses in the short run.

On the other hand, seeking only short-term profits may steer the firm from opportunities that would offer larger long-run profits. For example, Fruit of the Loom struggled to maximize profits with its men's underwear and other clothing lines, but in those intensely competitive markets the maximum possible profit margins were so thin that it ultimately had to reorganize under the bankruptcy law. In a situation like this, it might be better to set a *target* rate of profit that will lead the firm into areas with more promising possibilities.

A mission statement helps set the course

Our three general objectives provide guidelines, but a firm should develop its own objectives. This is important, but top executives often don't state their objectives clearly. Too often, they say what their objectives were after the fact. If objectives aren't clear from the start, different managers may hold unspoken and conflicting objectives—a common problem in large companies and in nonprofit organizations.

Many firms try to avoid this problem by developing a **mission statement,** which sets out the organization's basic purpose for being. For example, the mission of the Fort Smith Public Library (www.fspl.lib.ar.us) is "to serve the minds of the citizens in our community by providing easy access to resources that meet their informational and recreational needs." As illustrated by this example, a good mission statement should focus on a few key goals rather than embracing everything. It should also supply guidelines when managers face difficult decisions. For example, if an employee of the library is trying to decide whether or not to write a proposal for the funding of a Spanish language story time or new computers that provide Internet access, it should be clear that these services are within the scope of the library's stated mission. On the other hand, if another possible opportunity was to use extra space in the library for exercise equipment, it would appear to be beyond the stated mission. Of course, a mission statement may need to be revised as new market needs arise or as the marketing environment changes, but this would be a fundamental change and not one that is made casually.[4]

The whole firm must work toward the same objectives

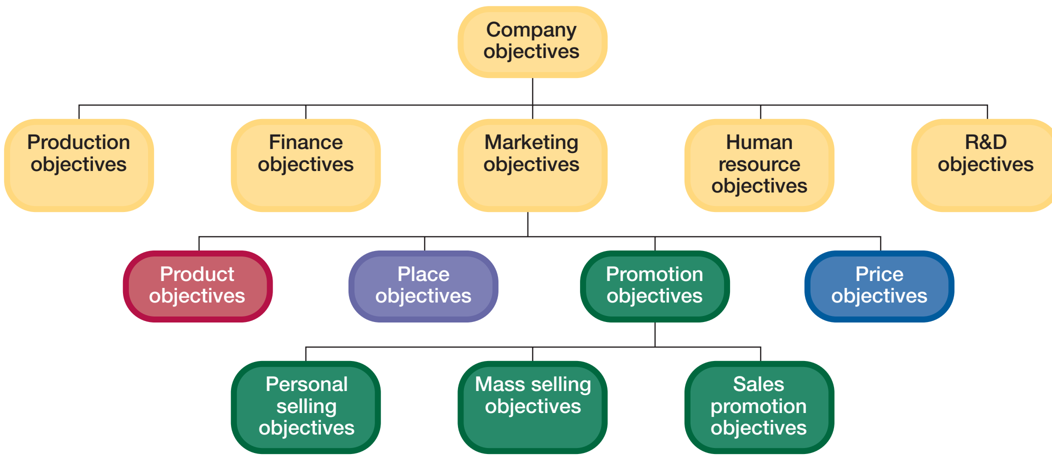
A mission statement is important, but it is not a substitute for more specific objectives that provide guidance in screening possible opportunities. For example, top management might set objectives such as "earn 25 percent annual return on investment," "become the market-share leader in each of our product-markets," and "introduce at least three innovative and successful products in the next two years."

Of course, when there are a number of specific objectives stated by top management, it is critical that they be compatible. If they're not, frustration and even failure may result. For example, a top-management objective of 25 percent annual return on investment may seem reasonable taken by itself. And the objective of introducing new products is reasonable. However, if the costs of developing and introducing the new products cannot be recouped within one year, the return on investment objective is impossible.[5]

Top-management myopia may straitjacket marketing

We are assuming that it is the marketing manager's job to work within the framework of objectives provided by top management. But some of these objectives may limit marketing strategies and perhaps damage the whole business. This is another reason why it is desirable for the marketing manager to help shape the company's objectives.

Exhibit 4-1 A Hierarchy of Objectives



Some top managements want a large market share because they feel this ensures greater profitability. But many large firms with big market shares, like Eastern Airlines, have gone bankrupt. These firms sought large market shares—but earned little profit. Increasingly, managers are shifting their objectives toward *profitable* sales growth rather than just larger market share—as they realize that the two don't necessarily go together.[6]

Company objectives should lead to marketing objectives

You can see why the marketing manager should be involved in setting company objectives. Company objectives guide managers as they search for and evaluate opportunities—and later plan marketing strategies. Particular *marketing* objectives should be set within the framework of larger company objectives. As shown in Exhibit 4-1, firms need a hierarchy of objectives—moving from company objectives to marketing department objectives. For each marketing strategy, firms also need objectives for each of the four Ps—as well as more detailed objectives. For example, in the Promotion area, we need objectives for advertising, sales promotion, *and* personal selling.

Toyota provides a good example. One of its company objectives is to achieve high customer satisfaction. So, the R&D people design vehicles to meet specific reliability objectives. Similarly, the production people work to cut manufacturing defects. The marketing department, in turn, sets specific customer satisfaction objectives for every product. That leads to specific promotion objectives to ensure that the sales and advertising people don't promise more than the company can deliver. Dealers' service people, in turn, work to fix any problem the first time it's reported.

Both company objectives and marketing objectives should be realistic and achievable. Overly ambitious objectives are useless if the firm lacks the resources to achieve them.

Company Resources May Limit Search for Opportunities

Every firm has some resources—hopefully some unique ones—that set it apart. Breakthrough opportunities—or at least some competitive advantage—come from making use of these strengths while avoiding direct competition with firms having similar strengths.

To find its strengths, a firm must evaluate its functional areas (production, research and engineering, marketing, general management, and finance) as well as its present products and markets. The expertise and knowledge of people at the firm can also be a unique resource. By analyzing successes or failures in relation to the firm's resources, management can discover why the firm was successful—or why it failed—in the past.

Harley-Davidson's motorcycle business was on the ropes, and it was losing customers to Japanese competitors. Studying the Japanese firms helped Harley identify ways to produce higher quality motorcycles at lower cost. With these resource-use problems resolved, Harley was again on the road to achieving its objectives. As its sales and reputation grew, its close relationship with Harley owners became a resource that helped Harley introduce a profitable line of accessories. The Harley case highlights both manufacturing quality and relationships with existing customers as resources. Other resources that should be considered as part of an evaluation of strengths and weaknesses are discussed in the following sections.[7]

Financial strength

Some opportunities require large amounts of capital just to get started. Money may be required for R&D, production facilities, marketing research, or advertising before a firm makes its first sale. And even a really good opportunity may not be profitable for years. So lack of financial strength is often a barrier to entry into an otherwise attractive market.

Producing capability and flexibility

In many businesses, the cost of producing and selling each unit decreases as the quantity increases. Therefore, smaller firms can be at a great cost disadvantage if they try to win business from larger competitors.

On the other hand, new—or smaller—firms sometimes have the advantage of flexibility. They are not handicapped with large, special-purpose facilities that are obsolete or poorly located. Large steel producers once enjoyed economies of scale. But today they have trouble competing with producers using smaller, more flexible plants.

Some firms are finding that they have the greatest flexibility by not having any "in house" manufacturing at all. Sara Lee, the company that markets brands like Hanes and L'Eggs, is a good example. Sara Lee sold its manufacturing facilities for many of these textile-related markets. Sara Lee says it doesn't have a competitive advantage in manufacturing. Further, as its needs change in various markets around the world it will buy products from whatever suppliers are best able to meet its specifications. Of course, this could be risky if some other firm can develop a competitive advantage—because it can provide retailers with faster or more reliable response when they place orders.

Marketing strengths

Our marketing strategy planning framework (Exhibit 3-1) helps in analyzing current marketing resources. In the product area, for example, a familiar brand can be a big strength. Starbucks is famous for its coffee beverages. Starbucks Coffee Ice Cream was also a leader within a year of its introduction. People tried it because they knew what Starbucks flavor meant.[8] A new idea or process may be protected by a *patent*. A patent owner has a 20-year monopoly to develop and use its new product, process, or material. If one firm has a strong patent, competitors may be limited to second-rate offerings—and their efforts may be doomed to failure.[9]

Good relations with established middlemen—or control of good locations—can be important resources in reaching some target markets. When marketing managers at Microsoft decided to introduce the Xbox game console, Microsoft software and

A familiar brand name—and other marketing strengths—can be an advantage in seeking new opportunities.

computer accessories had already proved profitable for retailers like Best Buy and Wal-Mart that could reach the target market. So these retailers were willing to give the new product shelf space even if they were already carrying competing products from Nintendo or Sony.[10]

Similarly, existing computer systems that effectively share information in the channel, speed delivery of orders, and control inventory can be a big advantage. When P&G adds a new type of detergent, the systems to manage distribution are already in place.

Promotion and price resources must be considered too. Fidelity Investments already has a skilled sales force. Marketing managers know these sales reps can handle new products and customers. And expertise to create an Internet website for online orders may enable a firm to expand its market and undercut competitors' prices.

Finally, thorough understanding of a target market can give a company an edge. Many companies fail in new product-markets because they don't really understand the needs of the new customers or the new competitive environment.

Analyzing Competitors and the Competitive Environment

Choose opportunities that avoid head-on competition

The **competitive environment** affects the number and types of competitors the marketing manager must face and how they may behave. Although marketing managers usually can't control these factors, they can choose strategies that avoid head-on competition. And where competition is inevitable, they can plan for it.

Economists describe four basic kinds of market (competitive) situations: pure competition, oligopoly, monopolistic competition, and monopoly. Understanding the differences among these market situations is helpful in analyzing the competitive environment, and our discussion assumes some familiarity with these concepts. (For a review, see Exhibit A-11 and the related discussion in Appendix A, which follows Chapter 22.)

Most product-markets head toward pure competition—or oligopoly—over the long run. In these situations, competitors offer very similar products. Because customers see the different available products (marketing mixes) as close substitutes, managers just compete with lower and lower prices, and profit margins shrink. Sometimes managers do this much too quickly, without really thinking through the question of how they might add more value to the marketing mix. It's crucial to remember that the marketing mix that offers customers the best value is not necessarily the one with the lowest price.

Dodge would like to avoid head-on competition with other auto producers, but that is difficult if potential customers view competing autos as very similar.

Avoiding pure competition is sensible and certainly fits with our emphasis on target marketing and the need to find a competitive advantage on which to differentiate the firm's marketing mix. This is why effective target marketing is fundamentally different from effective decision making in other areas of business. Accounting, production, and financial managers for competing firms can learn about and use the same standardized approaches—and they will work well in each case. By contrast, marketing managers can't just adopt the same "good" marketing strategy being used by other firms. That just leads to head-on competition and a downward spiral in prices and profits. So target marketers try to offer a marketing mix better suited to customers' needs than competitors' offerings.

Competitor-free environments are rare

Most marketing managers would like to have such a strong marketing mix that customers see it as uniquely able to meet their needs. This competitor-free ideal guides the search for breakthrough opportunities. Yet monopoly situations, in which one firm completely controls a broad product-market, are rare in market-directed economies. Further, governments commonly regulate monopolies. For example, in many parts of the world prices set by utility companies must be approved by a government agency. Although most marketing managers can't expect to operate with complete control in an unregulated monopoly, they can move away from head-on competition.

Monopolistic competition is typical—and a challenge

In monopolistic competition, a number of different firms offer marketing mixes that at least some customers see as different. Each competitor tries to get control (a monopoly) in its "own" target market. But competition still exists because some customers see the various alternatives as substitutes. Most marketing managers in developed economies face monopolistic competition.

In monopolistic competition, marketing managers sometimes try to differentiate very similar products by relying on other elements of the marketing mix. For example, Clorox Bleach uses the same basic chemicals as other bleaches. But marketing managers for Clorox may help to set it apart from other bleaches by offering an improved pouring spout, by producing ads that demonstrate its stain-killing power, or by getting it better shelf positions in supermarkets. Yet such approaches may not work, especially if competitors can easily imitate each new idea. Efforts to promote real, but subtle,

When AOL got started in the U.S., it faced relatively little competition in the new market for online services. However, in entering the European market, it has faced more competition from subscription-free Internet service providers; so promotion focused on AOL's superior support.

differences may not do any good either. If potential customers view the different offerings as essentially similar, the market will become more and more competitive—and firms will have to rely on lower costs to obtain a competitive advantage.

Analyze competitors to find a competitive advantage

The best way for a marketing manager to avoid head-on competition is to find new or better ways to satisfy customers' needs and provide value. The search for a breakthrough opportunity—or some sort of competitive advantage—requires an understanding not only of customers but also of competitors. That's why marketing managers turn to **competitor analysis**—an organized approach for evaluating the strengths and weaknesses of current or potential competitors' marketing strategies. A complete discussion of the possible approaches for competitor analysis is beyond the scope of the first marketing course. But we will briefly cover an approach that works well in many different market situations.

The basic approach to competitor analysis is simple. You compare the strengths and weaknesses of your current (or planned) target market and marketing mix with what competitors are currently doing or are likely to do in response to your strategy.

The initial step in competitor analysis is to identify potential competitors. It's useful to start broadly and from the viewpoint of target customers. Companies may offer quite different products to meet the same needs, but they are competitors if customers see them as offering close substitutes. For example, disposable diapers, cloth diapers, and diaper rental services all compete in the same generic market concerned with baby care. Identifying a broad set of potential competitors helps marketing managers understand the different ways customers are currently meeting needs and sometimes points to new opportunities. For example, even parents who usually prefer the economy of cloth diapers may be interested in the convenience of disposables when they travel.

Usually, however, marketing managers quickly narrow the focus of their analysis to the set of **competitive rivals**—firms that will be the closest competitors. Rivals offering similar products are usually easy to identify. However, with a really new and different product concept, there may not be a current competitor with a similar product. In that case, the closest competitor may be a firm that is currently serving similar needs with a different type of product. Although such firms may not appear to be close competitors, they are likely to fight back—perhaps with a directly competitive product—if another firm starts to take away customers.

Anticipate competition that will come

Marketing managers must consider how long it might take for competitors to appear. It's easy to make the mistake of assuming that there won't be competitors—or of discounting how aggressive competition may become. But a successful strategy attracts copycats who jump in for a share of the profit. Sometimes a creative imitator

Exhibit 4-2 Competitor Analysis (summary): Disposable Diaper Competition in Japan

	P&G's Current and Planned Strategy	Kao's Strengths (+) and Weaknesses (−)	Uni-Charm's Strengths (+) and Weaknesses (−)
Target Market(s)	Upscale, modern parents who can afford disposable diapers	Same as for P&G	Same as for P&G, but also budget-conscious segment that includes cloth diaper users (+)
Product	Improved fit and absorbency (+); brand name imagery weak in Japan (−)	Brand familiarity (+), but no longer the best performance (−)	Two brands—for different market segments—and more convenient package with handles (+)
Place	Distribution through independent wholesalers to both food stores and drugstores (+), but handled by fewer retailers (−)	Close relations with and control over wholesalers who carry only Kao products (+); computerized inventory reorder system (+)	Distribution through 80% of food stores in best locations (+); shelf space for two brands (+)
Promotion	Heaviest spending on daytime TV, heavy sales promotion, including free samples (+); small sales force (−)	Large efficient sales force (+); lowest advertising spending (−) and out-of-date ad claims (−)	Advertising spending high (+); effective ads that appeal to Japanese mothers (+)
Price	High retail price (−), but lower unit price for larger quantities (+)	Highest retail price (−), but also best margins for wholesalers and retailers (+)	Lowest available retail price (+); price of premium brand comparable to P&G (−)
(Potential) Competitive Barriers	Patent protection (+), limits in access to retail shelf space (−)	Inferior product (−), excellent logistics support system (+)	Economies of scale and lower costs (+); loyal customers (+)
Likely Response(s)	Improve wholesaler and retailer margins; faster deliveries in channel; change package to require less shelf space	Press retailers to increase in-store promotion; change advertising and/or improve product	Increase short-term sales promotions; but if P&G takes customers, cut price on premium brand

figures out a way to provide customers with superior value. Then, sales may disappear before the pioneer even knows what's happened.

Finding a sustainable competitive advantage requires special attention to competitor strengths and weaknesses. For example, it is very difficult to dislodge a firm that is already a market leader simply by attacking with a similar strategy. The leader can usually defend its position by quickly copying the best parts of what a new competitor is trying to do. On the other hand, an established competitor may not be able to defend quickly if it is attacked where it is weak. For example, Right Guard deodorant built its strong position with an aerosol spray dispenser. But many consumers don't like the messy aerosol cloud; that weakness provided Old Spice with an opportunity for a deodorant in a pump dispenser. Right Guard did not quickly fight back with its own pump because that could have hurt sales of its established product.[11]

Watch for competitive barriers

In a competitor analysis, you also consider **competitive barriers**—the conditions that may make it difficult, or even impossible, for a firm to compete in a market. Such barriers may limit your own plans or, alternatively, block competitors' responses to an innovative strategy.

For example, Exhibit 4-2 summarizes a competitor analysis in the Japanese market for disposable diapers. P&G was about to replace its original Pampers, which were selling poorly, with a new version that offered improved fit and better absorbency. Kao and Uni-Charm, the two leading Japanese producers, both had better distribution networks. Kao also had a better computer system to handle reorders. This was crucial because most Japanese grocery stores and drugstores are very small—about 150 square feet. Shelf space is limited and frequent restocking by wholesalers is critical. So getting cooperation in the channel was a potential competitive barrier for P&G. Uni-Charm further reduced P&G's access to customers when it took advantage of its relationship with retailers to introduce a second, lower-priced brand. To help overcome resistance in the channel, P&G improved the product, changed the packaging to take up less space, and offered wholesalers and retailers better markups.[12]

Seek information about competitors

A marketing manager should actively seek information about current or potential competitors. Although most firms try to keep the specifics of their plans secret, much public information may be available. For example, many firms routinely monitor competitors' local newspapers. In one such case, an article discussed a change in the competitor's sales organization. An alert marketing manager realized that the change was made to strengthen the competitor's ability to take business from one of her firm's key target markets. This early warning provided time to make adjustments.

Other sources of competitor information include trade publications, alert sales reps, middlemen, and other industry experts. In business markets, customers may be quick to explain what competing suppliers are offering.

The Internet is a powerful way to get information about competitors. A firm that puts all of its marketing information on a website for customers also makes it readily available to competitors. Similarly, computer programs make it easy to search through thousands of online publications and databases for any mention of a competitor. It's also increasingly common to specify what you want and instruct a software "robot" to send you a copy as soon as it's available. This is an incredibly powerful source of information that didn't even exist a few years ago. For more information about this type of Internet news service, check out www.infogate.com. Similarly, websites that provide investors with up-to-date information about companies can also be very useful for competitor analysis; for an example, see www.companysleuth.com.

Internet

Internet Exercise If you were a new marketing manager at Rubbermaid, you might be interested in finding out more about Tupperware, an important competitor in some markets. What type of relevant information could you get by going to the Tupperware website (www.tupperware.com)?

Ethical issues may arise

The search for information about competitors sometimes raises ethical issues. For example, it's not unusual for people to change jobs and move to a competing firm in the same industry. Such people may have a great deal of information about the competitor, but is it ethical for them to use it? Similarly, some firms have been criticized for going too far—like waiting at a landfill for competitors' trash to find copies of confidential company reports. And the high-tech version of that occurs when computer "hackers" use the Internet to break into a competitor's computer network. In minutes, hackers can steal information that has taken years to collect.

Beyond the moral issues, spying on competitors to obtain trade secrets is illegal. Damage awards can be huge. The courts ordered competing firms to pay Procter & Gamble about $125 million in damages for stealing secrets about its Duncan Hines soft cookies. For example, a Frito-Lay employee posed as a potential customer to attend a confidential sales presentation.[13]

Competition may vary from country to country

A firm that faces very stiff competition may find that the competitive environment—and the opportunities—are much better in another region or country. For instance, eight years of slow growth and deregulation made the Japanese market extremely competitive. So, the Iris Ohyama Company, a maker of plastic flower pots and storage containers, started exporting to North America. Within three years, its sales to U.S. retailers like Staples were $60 million—10 percent of total revenue.[14]

Direct competition cannot always be avoided

Despite the desire to avoid highly competitive situations, a firm may find that it can't. Some firms are already in an industry before it becomes intensely competitive. For example, Rubbermaid was one of the first firms to introduce sturdy, low-cost plastic housewares. Now it is a respected brand name but faces competition from hundreds of other firms. As competitors fail, new firms enter the market, possibly because they don't see more attractive alternatives. This is a common pattern with small retailers and wholesalers in less-developed economies. New entrants may not even know how competitive the market is—but they stick it out until they run out of money.

The Economic Environment

The **economic and technological environment** affects the way firms—and the whole economy—use resources. We will treat the economic and technological environments separately to emphasize that the technological environment provides a *base* for the economic environment. Technical skills and equipment affect the way companies convert an economy's resources into output. The economic environment, on the other hand, is affected by the way all of the parts of a macro-economic system interact. This then affects such things as national income, economic growth, and inflation. The economic environment may vary from one country to another, but economies around the world are linked.

Economic conditions change rapidly

The economic environment can, and does, change quite rapidly. The effects can be far-reaching and require changes in marketing strategy.

Even a well-planned marketing strategy may fail if a country or region goes through a rapid business decline. As consumers' incomes drop, they must shift their spending patterns. They may simply have to do without some products. In the late 1990s this happened across countries in Asia, and many businesses collapsed. Those that did not had big losses. You can see how quickly this happens by considering Thailand. In a few months, the buying power of Thai money (the bhat) was cut by half. Imagine how *your* life would change if you suddenly had half as much money. If this happened to you and most of the people you know, what would its effect be on businesses where you buy?

Of course, economic changes are not always this dramatic. Consider the cooling off of the U.S. economy in 2000. The growth of the economy leading up to that time created a strong job market, increased incomes, and focused attention on the rising value of investments. Many consumers felt like they were well off. Purchases of pricey items and luxuries trended up because of this "wealth effect." This behavior quickly disappeared when the economy turned, but for most products demand declined more gradually and overall consumer income and spending did not fall dramatically. Even so, a weak economy undermines consumer confidence, even among families whose income is not affected. When consumer confidence is low, people delay purchasing—especially big ticket items. Similarly, firms cut back on their own purchases. Many companies aren't strong enough to survive such downturns.

Interest rates and inflation affect buying

Changes in the economy are often accompanied by changes in the interest rate—the charge for borrowing money. Interest rates directly affect the total price borrowers must pay for products. So the interest rate affects when, and if, they will buy. This is an especially important factor in some business markets. But it also affects consumer purchases of homes, cars, furniture, computers, and other items usually bought on credit.

Interest rates usually increase during periods of inflation, and inflation is a fact of life in many economies. In some Latin American countries, inflation has

Managers who compete in global markets need to be aware of how changes in the global economy will impact their strategies and opportunities.

exceeded 400 percent a year in recent years. In contrast, recent U.S. levels—3 to 20 percent—seem low. Still, inflation must be considered in strategy planning. When costs are rising rapidly and there are no more cost-cutting measures to take, a marketing manager may have to increase prices. But the decisions of individual marketing managers to raise prices add to macro-level inflation. That can lead to government policies that reduce income, employment, *and* consumer spending.

The global economy is connected

In the past, marketing managers often focused their attention on the economy of their home country. It's no longer that simple. The economies of the world are connected—and changes in one economy quickly affect others. One reason for this is that the amount of international trade is increasing—and it is affected by changes in and between economies. For example, International Harvester (IH) was very successful selling its earth-moving equipment in Asia when construction was booming. However, when the "Asian flu" hit, many customers could no longer make payments. IH faced big losses—and the cost of retrieving equipment that was 13,000 miles away!

Changes in the *exchange rate*—how much one country's money is worth in another country's money—have an important effect on international trade. When the dollar is strong, it's worth more in foreign countries. This sounds good—but it makes U.S. products more expensive overseas and foreign products cheaper in the United States. Then, firms like Compaq lose foreign customers to producers from other countries.

A marketing manager isn't safe from the forces of changing exchange rates just because his or her firm is not involved in foreign trade. New competition arises in domestic markets as foreign products gain a competitive edge with lower prices. Many companies find themselves helpless during such economic change. In fact, a country's whole economic system can change as the balance of imports and exports shifts—affecting jobs, consumer income, and national productivity.

You can see that the marketing manager must watch the economic environment carefully. In contrast to the cultural and social environment, economic conditions change continuously. And they can move rapidly—up or down—requiring immediate strategy changes.[15]

The Technological Environment

Technology affects opportunities

Technology is the application of science to convert an economy's resources to output. Technology affects marketing in two basic ways: with new products and with new processes (ways of doing things). For example, we are moving from an industrial society to an information society. Advances in information technology make it possible for people in different parts of the world to communicate face-to-face with satellite video-conferencing and to transmit complex design drawings over the Internet. Websites enable sophisticated e-commerce exchanges between remote firms. These process changes are accompanied by an exciting explosion of high-tech products—from genome-based medicines to micro-lasers in factories to cars that contact the police if they are stolen.

Technology transfer is rapid

New technologies have created important industries that didn't even exist a few years ago. Fifteen years ago AOL didn't exist. Now it's one of the best known brands in the world. With such big opportunities at stake, you can also see why there is such rapid transfer of technology from one part of the world to another. But technology transfer is not automatic. Someone—perhaps you—has to see the opportunity.

Internet technologies are reshaping marketing

Many of the big advances in business have come from early recognition of new ways to do things. There is perhaps no better example of this than the World Wide Web and the Internet. The **Internet** is a system for linking computers around the world. The idea of linking computers in a network is not new. It's been around for years. Further, when we say that the Internet is a system it might be more accurate to just think of it as a collection of consistent hardware and software standards. Even so, the Internet expands the network concept to include any computer anywhere. Further, the World Wide Web makes the exchange of information on the Internet easy. As a result, this new technology is radically changing just about every aspect of marketing. We'll be discussing these changes in more detail throughout the text, so for now we'll just illustrate the impact.

Consider the arena of promotion. The invention of TV changed marketing because it suddenly made it possible for a sponsor to broadcast a vivid message to millions of people at the same time. Now, the Internet makes it possible for that sponsor to select any of millions of messages and to simultaneously narrowcast any of them to millions of different individuals. It is just as easy for customers to request the information in the first place, or to respond electronically once they have it. Thus, the Internet's capability radically changes our ideas about how firms communicate with customers, and vice versa. Similarly, the Internet is creating totally different approaches to pricing. Airlines are now running online auctions of seats that might otherwise go unsold. If you sell every seat to the highest bidder, you are really pricing precisely to match supply and demand. To check out an online auction, go to www.ebay.com.

In hindsight, new approaches such as these seem obvious—given that the technology is available. But they are not obvious up front—unless you're really looking for them. Marketers should help their firms see such opportunities by trying to understand the "why" of present markets—and what is keeping their firms from being more successful. Then, as new technological developments come along, the marketers will be alert to possible uses of those technologies and see how opportunities can be turned into profits.[16]

Technology also poses challenges

The rapid pace of technological change opens up new opportunities, but it also poses challenges for marketers. For some firms, success hinges on how quickly new ideas can be brought to market. But it's easy for a firm to slip into a production orientation

RealMedia promotes the multimedia capabilities of its website products to marketing managers because it knows that its technological innovations will result in new market opportunities for other firms only if marketing managers see the possibilities.

in the flush of excitement that comes from a new idea or R&D discovery. That makes it more important than ever for marketing thinking to guide the production process—starting at the beginning with decisions about what customers will really value and where development efforts should be focused.

Technology and ethical issues

Marketers must also help their firms decide what technological developments are ethically acceptable. For example, many firms use a system to identify incoming callers. Before the phone is even answered the computer shows who is calling and detailed information—ranging from what purchases the customer has made in the past to the income level of people who live in the caller's zip code area. This can be a powerful marketing tool, but many people feel that it's an invasion of privacy. Similarly, many firms track information about who "hits" the company web page and what website they came from. The firm can then sell this information to whoever wants to use it to send promotional e-mail. Yet uninvited e-mail is just another form of invasion of privacy.

With the growing concern about environmental pollution and the quality of life, some attractive technological developments may be rejected because of their long-run effects on the environment. Aseptic drink boxes, for example, are convenient but difficult to recycle. In a case like this, what's good for the firm and some customers may not be good for the cultural and social environment or acceptable in the political and legal environment. Being close to the market should give marketers a better feel for current trends and help firms avoid serious mistakes.[17]

The Political Environment

The attitudes and reactions of people, social critics, and governments all affect the political environment. Consumers in the same country usually share a common political environment, but the political environment can also have a dramatic effect on opportunities at a local or international level. Some business managers have become very successful by studying the political environment and developing strategies that take advantage of opportunities related to changing political dimensions.

Nationalism can be limiting in international markets

Strong sentiments of **nationalism**—an emphasis on a country's interests before everything else—affect how macro-marketing systems work. They can affect how marketing managers work as well. Nationalistic feelings can reduce sales—or even block all marketing activity—in some international markets. For many years, Japan has made it difficult for outside firms to do business there—in spite of the fact that Japanese producers of cars, TVs, digital cameras, and other products have established profitable markets in the United States, Europe, and other parts of the world. Japan is under pressure to change, but the changes are coming slowly.

The "Buy American" policy in many government contracts and business purchases reflects this same attitude in the U.S. There is broad support for protecting U.S. producers—and jobs—from foreign competition.[18]

Nationalistic feelings can determine whether a firm can enter markets because businesses often must get permission to operate. In some political environments, this is only a routine formality. In others, a lot of red tape and personal influence are involved, and bribes are sometimes expected. This raises ethical issues for marketing managers—and legal issues too, since it's illegal for U.S. firms to offer such bribes. Clearly, that can make it difficult for a U.S. firm to compete with a company from a country that doesn't have similar laws.

Regional groupings are becoming more important

Important dimensions of the political environment are likely to be similar among nations that have banded together to have common regional economic boundaries. The move toward economic unification of Europe and free trade among the nations of North America are outstanding examples of this sort of regional grouping.

The unification of European markets

In the past, each country in Europe had its own unique trade rules and regulations. These differences—and nationalistic squabbles—made it difficult and expensive to move products from one country to the others. Now, the member countries of the European Union (EU) are trying to reduce conflicting laws, taxes, and other obstacles to trade within Europe. Trucks loaded with products now spill across borders of the European continent and Britain. The increased efficiency is reducing costs and the prices European consumers pay and creating new jobs. Even bigger changes may come if Britain decides to join other key member countries that have moved to the euro, a new unified money system for the EU. With the currencies of countries in the euro-zone phased out, transactions no longer involve the extra uncertainty and cost of converting payments from one currency to another.

Step-by-step Europe is becoming the largest unified market in the world, but marketers should still expect to encounter some differences among European countries. What happened to Lands' End, the Wisconsin-based Internet and mail-order retailer, illustrates the issues. To better reach pan-European consumers, Lands' End set up shop in England and Germany. As in the U.S., its promotion and website touted the unconditional lifetime guarantee that is a key part of its strategy. However, German consumer protection rules prohibited promotion of the lifetime guarantee; the Germans argued that promoting the guarantee was a misleading gimmick (on the logic that the cost of the guarantee was "hidden" in higher prices that consumers would pay). German officials wanted this ban to apply even if the German consumer purchased the product from a Lands' End website in England or the U.S. This obviously made things difficult for Lands' End, but there is also an important broader concern. If quirky local rules like this are allowed to prevail in the future, small companies that want to use e-commerce to efficiently reach the whole European market will have to comply not only with the laws of the

Adero wants marketers to keep in mind that a website that can attract prospects from all over the world won't be successful in turning them into customers if it ignores nationalism and cultural differences.

country in which they operate but also with all of the different laws in every country. This would certainly hinder the advantages that should come from more European unification.[19]

NAFTA is building trade cooperation

The international competition fostered by the moves to unify Europe provided impetus for the U.S., Mexico, and Canada to develop more cooperative trade agreements. **The North American Free Trade Agreement (NAFTA)** lays out a plan to reshape the rules of trade among the U.S., Canada, and Mexico. NAFTA basically enlarges the free-trade pact that had already knocked down most barriers to U.S.–Canada trade, and over a 15-year period it will eliminate most such barriers with Mexico. It also establishes a forum for resolving future trade disputes.

NAFTA is a long-term proposition, and its overall economic impact is yet to be seen. However, tariffs that have already dropped are having a significant impact on specific businesses. For example, Raychem Corp., a small producer of telecommunications equipment, no longer faces a 25 percent tariff on exports to Mexico. That is leveling its competitive playing field and creating new opportunities. More generally, NAFTA is creating a free-trade region that encompasses over 400 million people and three economies that produce over $9 trillion worth of goods and services annually. Thus, the changes that result from NAFTA may ultimately be as significant as those in Europe. Talks are underway to explore the concept of expanding NAFTA to create a free-trade zone for 34 countries across North, South, and Central America.

Of course, removal of some economic and political barriers—whether across all of the Americas or Europe—will not eliminate the need to adjust strategies to reach submarkets of consumers. Centuries of political and cultural differences will not disappear overnight. Some may never disappear.[20]

Some dramatic changes in the political environment—like the fall of communism in Eastern Europe—happen fast and are hard to predict. Yet many important political changes—both within and across nations—evolve more gradually. The development of consumerism is a good example.

Consumerism is here—and basic

Consumerism is a social movement that seeks to increase the rights and powers of consumers. In the last 40 years, consumerism has emerged as a major political force. Although the consumer movement has spread to many different countries, it was born in America.

The basic goals of modern consumerism haven't changed much since 1962, when President Kennedy's "Consumer Bill of Rights" affirmed consumers' rights to safety, to be informed, to choose, and to be heard.

Thirty-five years ago, U.S. consumerism was much more visible. Consumers staged frequent boycotts and protest marches and attracted much media attention. Today, consumer groups provide information and work on special projects like product safety standards. Publications like *Consumer Reports* provide product comparisons and information on other consumer concerns.

Clearly, top management—and marketing managers—must continue to pay attention to consumer concerns. The old, production-oriented ways of doing things are no longer acceptable.[21]

The Legal Environment

Changes in the political environment often lead to changes in the legal environment and in the way existing laws are enforced. The legal environment sets the basic rules for how a business can operate in society. The legal environment may severely limit some choices, but changes in laws and how they are interpreted also create new opportunities. To illustrate the effects of the legal environment, we will discuss how it has evolved in the United States. However, keep in mind that laws often vary from one geographic market to another—especially when different countries are involved.

Trying to encourage competition

American economic and legislative thinking is based on the idea that competition among many small firms helps the economy. Therefore, attempts by business to limit competition are considered contrary to the public interest.

As industries grew larger after the Civil War, some became monopolies controlled by wealthy businessmen—the robber barons. Smaller producers had trouble surviving. A movement grew—especially among Midwestern farmers—to control monopolists.

Starting in 1890, Congress passed a series of antimonopoly laws. Exhibit 4-3 shows the names and dates of these laws. Although the specific focus of each law is different, in general they are all intended to encourage competition.

Antimonopoly law and marketing mix planning

In later chapters, we will specifically apply antimonopoly law to the four Ps. For now you should know what kind of proof the government must have to get a conviction under each of the major laws. You should also know which of the four Ps are most affected by each law. Exhibit 4-3 provides such a summary—with a phrase following each law to show what the government must prove to get a conviction.

Prosecution is serious—you can go to jail

Businesses and *individual managers* are subject to both criminal and civil laws. Penalties for breaking civil laws are limited to blocking or forcing certain actions—along with fines. Where criminal law applies, jail sentences can be imposed. For example, several managers at Beech-Nut Nutrition Company were fined $100,000 each and sentenced to a year in jail. In spite of ads claiming that Beech-Nut's apple juice was 100 percent natural, they tried to bolster profits by secretly using low-cost artificial ingredients.[22]

Consumer protection laws are not new

Although antimonopoly laws focus on protecting competition, the wording of the laws in Exhibit 4-3 has, over time, moved toward protecting consumers. Some

Exhibit 4-3 Focus (mostly prohibitions) of Federal Antimonopoly Laws on the Four Ps

Law	Product	Place	Promotion	Price
Sherman Act (1890) Monopoly or conspiracy in restraint of trade	Monopoly or conspiracy to control a product	Monopoly or conspiracy to control distribution channels		Monopoly or conspiracy to fix or control prices
Clayton Act (1914) Substantially lessens competition	Forcing sale of some products with others—tying contracts	Exclusive dealing contracts (limiting buyers' sources of supply)		Price discrimination by manufacturers
Federal Trade Commission Act (1914) Unfair methods of competition		Unfair policies	Deceptive ads or selling practices	Deceptive pricing
Robinson-Patman Act (1936) Tends to injure competition		Prohibits paying allowances to "direct" buyers in lieu of middlemen costs (brokerage charges)	Prohibits "fake" advertising allowances or discrimination in help offered	Prohibits price discrimination on goods of "like grade and quality" without cost justification, and limits quantity discounts
Wheeler-Lea Amendment (1938) Unfair or deceptive practices	Deceptive packaging or branding		Deceptive ads or selling claims	Deceptive pricing
Antimerger Act (1950) Lessens competition	Buying competitors	Buying producers or distributors		
Magnuson-Moss Act (1975) Unreasonable practices	Product warranties			

consumer protections are also built into the English and U.S. common law systems. A seller has to tell the truth (if asked a direct question), meet contracts, and stand behind the firm's product (to some reasonable extent). Beyond this, it is expected that vigorous competition in the marketplace will protect consumers—*so long as they are careful*.

Yet focusing only on competition didn't protect consumers very well in some areas. So the government found it necessary to pass other laws. For example, various laws regulate packaging and labels, credit practices, and environmental issues. Usually, however, the laws focus on specific types of products.

Foods and drugs are controlled

Consumer protection laws in the United States go back to 1906 when Congress passed the Pure Food and Drug Act. Unsanitary meat-packing practices in the Chicago stockyards stirred consumer support for this act. This was a major victory for consumer protection. Before the law, it was assumed that common law and the old warning "let the buyer beware" would take care of consumers.

Later acts corrected some loopholes in the law. The law now bans the shipment of unsanitary and poisonous products and requires much testing of drugs. The Food and Drug Administration (FDA) attempts to control manufacturers of these products. It can seize products that violate its rules—including regulations on branding and labeling.

Product safety is controlled

The Consumer Product Safety Act (of 1972), another important consumer protection law, set up the Consumer Product Safety Commission. This group has broad power to set safety standards and can impose penalties for failure to meet these standards. There is some question as to how much safety consumers really want—the commission found the bicycle the most hazardous product under its control!

But given that the commission has the power to *force* a product off the market—or require expensive recalls to correct problems—it is obvious that safety must be considered in product design. And safety must be treated seriously by marketing managers. There is no more tragic example of this than the recent recalls of Firestone tires used as original equipment on Ford's Explorer SUV. Hundreds of consumers were killed or seriously injured in accidents. Consumer faith in the Firestone brand is so low that it may not survive—even if the company isn't bankrupted by the costs of the recalls and lawsuit damages.[23]

Internet

Internet Exercise The Consumer Product Safety Commission sometimes requires auto makers to issue recalls. However, not all consumers learn about the recalls. Go to the *Consumer Reports* website (www.consumerreports.org) and select the link for recalls. Then check to see if there has been a recall on a year and model of car or truck that is of interest to you (say, one owned by your family).

State and local laws vary

Besides federal legislation—which affects interstate commerce—marketers must be aware of state and local laws. There are state and city laws regulating minimum prices and the setting of prices, regulations for starting up a business (licenses, examinations, and even tax payments), and in some communities, regulations prohibiting certain activities—such as telephone selling or selling on Sundays or during evenings.

Know the laws—follow the courts and federal agencies

Often laws are vaguely phrased—to convey intent but not specific detail. Then it's up to the courts and government agencies to spell out the details. As a result, a law may be interpreted and enforced differently over time. For example, during the late 1970s and 1980s, many U.S. government agencies regulated businesses less zealously and instead focused more on encouraging competition. Attention to regulation was swinging the other way in the 1990s—in part to correct abuses such as those that occurred in the savings and loan industry.

It was in this sort of political environment that the U.S. Justice Department, and the attorney generals in a number of states, brought charges against Microsoft. Many government officials, competitors, and consumer interest groups felt that Microsoft violated the antimonopoly laws, and at one point a judge declared that Microsoft would be broken up into two or more competing companies. However, the court case dragged out for over five years, and by the time of the national elections in 2000 the political climate was swinging toward less aggressive enforcement of the laws. As this very visible and important case shows, how the laws are interpreted and enforced can be even more important than the wording of the law when it was originally written.[24]

Because legislation must be interpreted by federal agencies and the courts, marketing managers need to study both legislative developments and the thinking of the courts and agencies. See Exhibit 4-4 for a description of some important federal regulatory agencies that should be considered in marketing strategy planning.

Exhibit 4-4 Some Important U.S. Federal Regulatory Agencies

Agencies	Responsibilities
Federal Trade Commission (FTC)	Enforces laws and develops guidelines regarding unfair business practices
Food and Drug Administration (FDA)	Enforces laws and develops regulations to prevent distribution and sale of adulterated or misbranded foods, drugs, cosmetics, and hazardous consumer products
Consumer Product Safety Commission (CPSC)	Enforces the Consumer Product Safety Act—which covers any consumer product not assigned to other regulatory agencies
Federal Communications Commission (FCC)	Regulates interstate wire, radio, television, and telephone
Environmental Protection Agency (EPA)	Develops and enforces environmental protection standards
Office of Consumer Affairs (OCA)	Handles consumers' complaints

Consumerists and the law say "Let the seller beware"

The old rule about buyer–seller relations—*let the buyer beware*—has changed to *let the seller beware*. The current shift to proconsumer laws and court decisions suggests that lawmakers are more interested in protecting consumers. This may upset production-oriented managers. But times have changed—and managers must adapt to this new political and legal environment. After all, it is the consumers—through their government representatives—who determine the kind of economic system they want.[25]

The Cultural and Social Environment

The **cultural and social environment** affects how and why people live and behave as they do—which affects customer buying behavior and eventually the economic, political, and legal environment. Many variables make up the cultural and social environment. Some examples are the languages people speak, the type of education they have, their religious beliefs, what type of food they eat, the style of clothing and housing they have, and how they view work, marriage, and family. Because the cultural and social environment has such broad effects, most people don't stop to think about it, or how it may be changing, or how it may differ for other people.

A marketing manager can't afford to take the cultural and social environment for granted. Although changes tend to come slowly, they can have far-reaching effects. A marketing manager who sees the changes early may be able to identify big opportunities. Further, within any broad society, different subgroups of people may be affected by the cultural and social environment in different ways. In most countries, the trend toward multiculturalism is making such differences even more important to marketers. They require special attention when segmenting markets. In fact, dealing with these differences is often one of the greatest challenges managers face when planning strategies, especially for international markets.

Since we will discuss details of how the cultural and social environment relates to buying behavior in Chapters 5 through 7, here we will just use an example to illustrate its impact on marketing strategy planning.

Changing women's roles

The shifting roles of women in society illustrate the importance of the cultural and social environment on marketing strategy planning. Forty years ago, most people in the United States felt that a woman's role was in the home—first and foremost as a wife and mother. Women had less opportunity for higher education and were completely shut out of many of the most interesting jobs. Obviously,

Kellogg realizes that more and more consumers are feeling a "poverty of time," so it uses humor to focus on the time-saving benefits of its Nutri-Grain bar as an on-the-go breakfast.

there have been big changes in that stereotyped thinking. With better job opportunities, more women are delaying marriage, and once married they are likely to stay in the workforce and have fewer children. For example, in 1950, only 24 percent of wives worked outside the home. Now that figure is over 60 percent. Among women in the 35–44 age group, the percentage is already over 70. Not everything has changed, though. The median income for women lags and is only 73 percent of men's.

Still, the flood of women into the job market boosted economic growth and changed U.S. society in many other ways. Many in-home jobs that used to be done primarily by women—ranging from family shopping to preparing meals to doing volunteer work—still need to be done by someone. Husbands and children now do some of these jobs, a situation that has changed the target market for many products. Or a working woman may face a crushing "poverty of time" and look for help elsewhere, creating opportunities for producers of frozen meals, child care centers, dry cleaners, financial services, and the like.

Although there is still a big wage gap between men and women, the income working women generate gives them new independence and purchasing power. For example, women now purchase about half of all cars. Not long ago, many car dealers insulted a woman shopper by ignoring her or suggesting that she come back with her husband. Now car companies have realized that women are important customers. It's interesting that Japanese car dealers, especially Mazda and Toyota, were the first to really pay attention to women customers. In Japan, fewer women have jobs or buy cars—the Japanese society is still very much male-oriented. Perhaps it was the extreme contrast with Japanese society that prompted these firms to pay more attention to women buyers in the United States.[26]

Women's changing role has created opportunities for marketing but also complications. A marketing mix targeted at women, for example, may require a real balancing act. Advertising showing a woman at the office may attract some customers but alienate housewives who feel that their job doesn't command as much status as it should. Conversely, an ad that shows a woman doing housework might be criticized for encouraging stereotypes.

Changes come slowly

Most changes in basic cultural values and social attitudes come slowly. An individual firm can't hope to encourage big changes in the short run. Instead, it should identify current attitudes and work within these constraints—as it seeks new and better opportunities.[27]

Using Screening Criteria to Narrow Down to Strategies

A progressive firm constantly looks for new opportunities. Once the opportunities are identified, the firm must screen and evaluate them. Usually, a firm can't pursue all available opportunities, so it must try to match its opportunities to its resources and

Enron Trades on Success

Managers at Enron take pride in their ability to spot market changes and then quickly develop profitable new strategies. Enron started in the natural gas pipeline business. When natural gas distribution was deregulated in the late 1980s, Enron increased the use of its pipeline by finding producers with excess supply and selling the excess to firms in other areas where demand was high. In the 1990s, it used its expertise in matching supply and demand to become a wholesaler for other commodities—ranging from electricity to steel—often for the same customers. Originally this buying and selling was handled by fax and phone, but now it's a natural fit for the Web (www.enrononline.com). For example, Enron posts prices for an array of energy contracts. Utilities caught short on supply can make a purchase with a click of the mouse. Producers with excess capacity can check the price Enron is willing to pay. Then Enron's staff does credit checks, handles billing, and schedules transmission capacity to actually deliver the electricity. Enron has become so good with this approach that it now uses it to "make markets" for hundreds of other products—ranging from capacity on telecommunications lines to pollution emissions credits. It handles thousands of transactions each day. As a result, Enron has quickly become the largest business-to-business e-commerce operator. However, dealing with so many buyers and sellers from different economies around the globe increases the risk that Enron will face more losses from credit defaults. So one of its criteria for screening new opportunities is that the expected profits be large relative to the credit risks.[28]

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objectives. First, management must quickly screen out obvious mismatches so other opportunities can be analyzed more carefully. Let's look at some approaches for screening and evaluating opportunities.

Developing and applying screening criteria

After you analyze the firm's resources (for strengths and weaknesses), the environmental trends the firm faces, and the objectives of top management, you merge them all into a set of product-market screening criteria. These criteria should include both quantitative and qualitative components. The quantitative components summarize the firm's objectives: sales, profit, and return on investment (ROI) targets. (Note: ROI analysis is discussed briefly in Appendix B, which comes after Chapter 22.) The qualitative components summarize what kinds of businesses the firm wants to be in, what businesses it wants to exclude, what weaknesses it should avoid, and what resources (strengths) and trends it should build on.[29]

Developing screening criteria is difficult but worth the effort. They summarize in one place what the firm wants to accomplish—in quantitative terms—as well as roughly how and where it wants to accomplish it. When a manager can explain the specific criteria that are relevant to selecting (or screening out) an opportunity, others can understand the manager's logic. Thus, marketing decisions are not just made or accepted based on intuition and gut feel. On the other hand, if the criteria are constantly changing when the focus moves from one opportunity to another, then the decision making is not consistent.

The criteria should be realistic—that is, they should be achievable. Opportunities that pass the screen should be able to be turned into strategies that the firm can implement with the resources it has.

Exhibit 4-5 illustrates some product-market screening criteria for a small retail and wholesale distributor. These criteria help the firm's managers eliminate unsuitable opportunities and find attractive ones to turn into strategies and plans.

Whole plans should be evaluated

You need to forecast the probable results of implementing a marketing strategy to apply the quantitative part of the screening criteria because only implemented plans generate sales, profits, and return on investment (ROI). For a rough screening, you only need to estimate the likely results of implementing each opportunity over a logical planning period. If a product's life is likely to be three years, for example, a good strategy may not produce profitable results for 6 to 12 months. But evaluated over the projected three-year life, the product may look like a winner. When evaluating the potential of possible opportunities (product-market strategies), it is important to evaluate similar things—that is, *whole* plans.

Exhibit 4-5 An Example of Product-Market Screening Criteria for a Small Retail and Wholesale Distributor ($10 million annual sales)

1. Quantitative criteria

a. Increase sales by $1,500,000 per year for the next five years.
b. Earn ROI of at least 25 percent before taxes on new ventures.
c. Break even within one year on new ventures.
d. Opportunity must be large enough to justify interest (to help meet objectives) but small enough so company can handle with the resources available.
e. Several opportunities should be pursued to reach the objectives—to spread the risks.

2. Qualitative criteria

a. Nature of business preferred.
   (1) Should take advantage of our online Internet order system and website promotion.
   (2) New goods and services for present customers to strengthen relationships and revenue.
   (3) "Quality" products that do not cannibalize sales of current products.
   (4) Competition should be weak and opportunity should be hard to copy for several years.
   (5) There should be strongly felt (even unsatisfied) needs—to reduce promotion costs and permit "high" prices.
b. Constraints.
   (1) Nature of businesses to exclude.
      (a) Manufacturing.
      (b) Any requiring large fixed capital investments.
      (c) Any requiring many support people who must be "good" all the time and would require much supervision.
   (2) Geographic.
      (a) United States, Mexico, and Canada only.
   (3) General.
      (a) Make use of current strengths.
      (b) Attractiveness of market should be reinforced by more than one of the following basic trends: technological, demographic, social, economic, political.
      (c) Market should not be bucking any basic trends.

Opportunities that pass the screening criteria should be evaluated in more detail before being accepted as *the* product-market strategic plans for implementation. Usually, a firm has more opportunities than resources and has to choose among them—to match its opportunities to its resources and objectives. The following approaches help firms select among possible plans.

Total profit approach can help evaluate possible plans

In the total profit approach, management forecasts potential sales and costs during the life of the plan to estimate likely profitability.

Managers may evaluate the prospects for each plan over a five-year planning period, using monthly and/or annual sales and cost estimates. This is shown graphically in Exhibit 4-6.

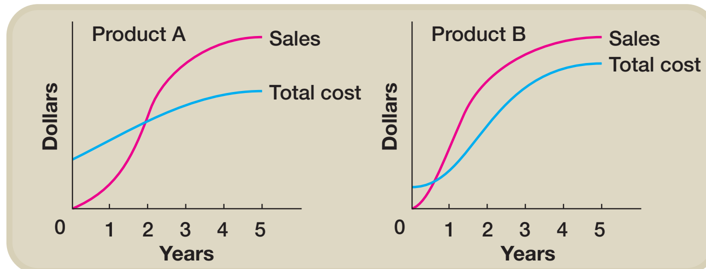
Note that managers can evaluate different marketing plans at the same time. Exhibit 4-6 compares a much improved product and product concept (Product A) with a "me-too" product (Product B) for the same target market. In the short run, the me-too product will make a profit sooner and might look like the better choice—if managers consider only one year's results. The improved product, on the other hand, will take a good deal of pioneering—but over its five-year life will be much more profitable.

Return-on-investment (ROI) approach can help evaluate possible plans too

Besides evaluating the profit potential of possible plans, firms may also calculate the return on investment (ROI) of resources needed to implement plans. One plan may require a heavy investment in advertising and channel development, for example, while another relies primarily on lower price.

ROI analyses can be useful for selecting among possible plans because equally profitable plans may require vastly different resources and offer different rates of return on investment. Some firms are very concerned with ROI, especially those that borrow money for working capital. There is little point in borrowing to implement strategies that won't return enough to meet the cost of borrowing.

Exhibit 4-6
Expected Sales and Cost Curves of Two Strategies over Five-Year Planning Periods



Planning Grids Help Evaluate a Portfolio of Opportunities

When a firm has many possibilities to evaluate, it usually has to compare quite different ones. This problem is easier to handle with graphical approaches—such as the nine-box strategic planning grid developed by General Electric and used by many other companies. Such grids can help evaluate a firm's whole portfolio of strategic plans or businesses.

General Electric looks for green positions

General Electric's strategic planning grid—see Exhibit 4-7—forces company managers to make three-part judgments (high, medium, and low) about the business strengths and industry attractiveness of all proposed or existing product-market plans. As you can see from Exhibit 4-7, this approach helps a manager organize information about the company's marketing environments (discussed earlier in this chapter) along with information about its strategy and translate it into relevant screening criteria.

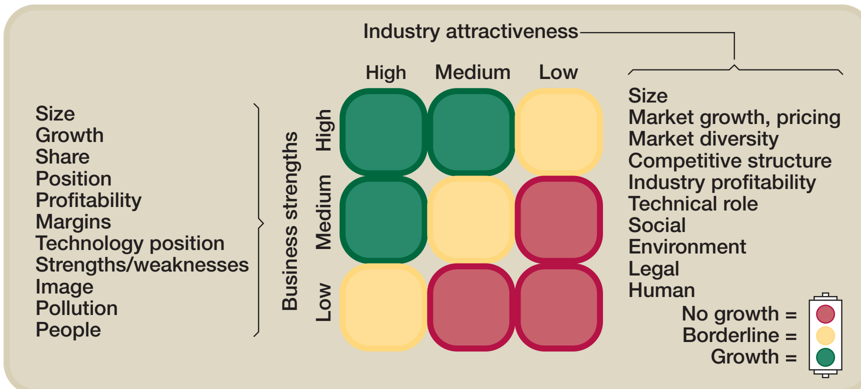
The industry attractiveness dimension helps managers answer the question: Does this product-market plan look like a good idea? To answer that question, managers have to judge such factors (screening criteria) as the size of the market and its growth rate, the nature of competition, the plan's potential environmental or social impact, and how laws might affect it. Note that an opportunity may be attractive for *some* company—but not well suited to the strengths (and weaknesses) of a particular firm. That is why the GE grid also considers the business strengths dimension.

The business strengths dimension focuses on the ability of the company to pursue a product-market plan effectively. To make judgments along this dimension, a manager evaluates whether the firm has people with the right talents and skills to implement the plan, whether the plan is consistent with the firm's image and profit objectives, and whether the firm could establish a profitable market share given its technical capability, costs, and size. Here again, these factors suggest screening criteria specific to this firm and market situation.

GE feels opportunities that fall into the green boxes in the upper left-hand corner of the grid are its best growth opportunities. Managers give these opportunities high marks on both industry attractiveness and business strengths. The red boxes in the lower right-hand corner of the grid, on the other hand, suggest a no-growth policy. Existing red businesses may continue to generate earnings, but they no longer deserve much investment. Yellow businesses are borderline cases—they can go either way. GE may continue to support an existing yellow business but will probably reject a proposal for a new one. It simply wouldn't look good enough on the relevant screening criteria.

GE's "stoplight" evaluation method is a subjective, multiple-factor approach. It avoids the traps and possible errors of trying to use oversimplified, single-number criteria—like ROI or market share. Instead, top managers review detailed written

Exhibit 4-7
General Electric's Strategic Planning Grid



summaries of many different screening criteria that help them make summary judgments. Then they can make a collective judgment. This approach generally leads to agreement. It also helps everyone understand why the company supports some new opportunities and not others.[30]

General Electric considers factors that reflect its objectives. Another firm might modify the evaluation to emphasize other factors—depending on its objectives and the type of product-market plans it is considering. While different firms focus on different screening criteria, using many factors helps ensure that managers consider all the company's concerns when evaluating alternative opportunities.

Multiproduct Firms Have a Difficult Strategy Planning Job

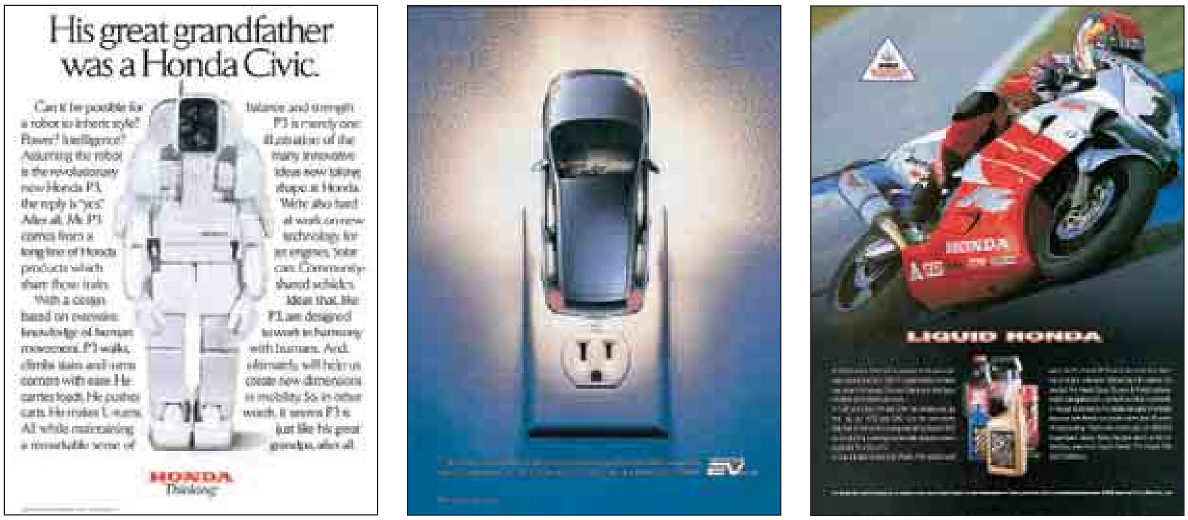
Multiproduct firms, like General Electric, obviously have a more difficult strategic planning job than firms with only a few products or product lines aimed at the same or similar target markets. Multiproduct firms have to develop strategic plans for very different businesses. And they have to balance plans and resources so the whole company reaches its objectives. This means they must analyze alternatives using approaches similar to the General Electric strategic planning grid and only approve plans that make sense for the whole company—even if it means getting needed resources by milking some businesses and eliminating others.

Details on how to manage a complicated multiproduct firm are beyond our scope. But you should be aware (1) that there are such firms and (2) that the principles in this text are applicable—they just have to be extended. For example, some firms use strategic business units (SBUs), and some use portfolio management.

Strategic business units may help

Some multiproduct firms try to improve their operations by forming strategic business units. A **strategic business unit (SBU)** is an organizational unit (within a larger company) that focuses on some product-markets and is treated as a separate profit center. By forming SBUs, a company formally acknowledges its very different activities. One SBU of Sara Lee, for example, produces baked goods for consumers and restaurants—another produces and markets Hanes brand T-shirts and underwear.

Some SBUs grow rapidly and require a great deal of attention and resources. Others produce only average profits and should be *milked*—that is, allowed to generate cash for the businesses with more potential. Product lines with poor market position, low profits, and poor growth prospects should be dropped or sold.



Large multiproduct firms, like Honda, evaluate and pursue a varied portfolio of strategic opportunities all around the world.

Some firms use portfolio management

Some top managements handle strategic planning for a multiproduct firm with an approach called **portfolio management**—which treats alternative products, divisions, or strategic business units (SBUs) as though they were stock investments, to be bought and sold using financial criteria. Such managers make trade-offs among very different opportunities. They treat the various alternatives as investments that should be supported, milked, or sold off—depending on profitability and return on investment (ROI). In effect, they evaluate each alternative just like a stock market trader evaluates a stock.[31]

This approach makes some sense if alternatives are really quite different. Top managers feel they can't become very familiar with the prospects for all of their alternatives. So they fall back on the easy-to-compare quantitative criteria. And because the short run is much clearer than the long run, they place heavy emphasis on *current* profitability and return on investment. This puts great pressure on the operating managers to deliver *in the short run*—perhaps even neglecting the long run.

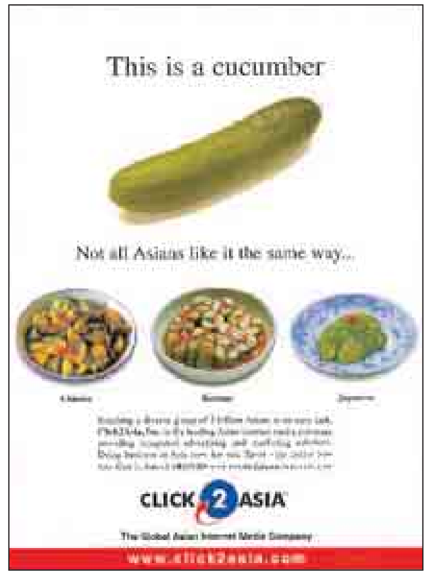
Neglecting the long run is risky—and this is the main weakness of the portfolio approach. This weakness can be overcome by enhancing the portfolio management approach with market-oriented strategic plans. They make it possible for managers to more accurately evaluate the alternatives' short-run and long-run prospects.

Evaluating Opportunities in International Markets

Evaluate the risks

The approaches we've discussed so far apply to international markets just as they do to domestic ones. But in international markets it is often harder to fully understand the marketing environment variables. This may make it harder to see the risks involved in particular opportunities. Some countries are politically unstable; their governments and constitutions come and go. An investment safe under one government might become a takeover target under another. Further, the possibility of foreign exchange controls—and tax rate changes—can reduce the chance of getting profits and capital back to the home country.

Some products, like industrial motors made by Baldor, are used the same way all over the world. Other products are much more sensitive to cultural differences.



To reduce the risk of missing some basic variable that may help screen out a risky opportunity, marketing managers sometimes need a detailed analysis of the market environment they are considering entering. Such an analysis can reveal facts about an unfamiliar market that a manager in a distant country might otherwise overlook. Further, a local citizen who knows the marketing environment may be able to identify an "obvious" problem ignored even in a careful analysis. Thus, it is very useful for the analysis to include inputs from locals—perhaps cooperative middlemen.[32]

Risks vary with environmental sensitivity

The farther you go from familiar territory, the greater the risk of making big mistakes. But not all products, or marketing mixes, involve the same risk. Think of the risks as running along a "continuum of environmental sensitivity." See Exhibit 4-8.

Some products are relatively insensitive to the economic and cultural environment they're placed in. These products may be accepted as is—or they may require just a little adaptation to make them suitable for local use. Most industrial products are near the insensitive end of this continuum.

At the other end of the continuum, we find highly sensitive products that may be difficult or impossible to adapt to all international situations. Consumer products closely linked to other social or cultural variables are at this end. For example, some of the scanty women's clothing popular in Western countries would be totally inappropriate in Arab countries where women are expected to cover even their faces. Similarly, some cultures view dieting as unhealthy; that explains why products like Diet Pepsi that are popular in the United States have done poorly there. "Faddy" type consumer products are also at this end of the continuum. It's sometimes difficult to understand why such products are well accepted in a home market. This, in turn, makes it even more difficult to predict how they might be received in a different environment.

This continuum helps explain why many of the early successes in international marketing were basic commodities such as gasoline, soap, transportation vehicles, mining equipment, and agricultural machinery. It also helps explain why some consumer products firms have been successful with basically the same promotion and products in different parts of the globe.

Yet some managers don't understand the reason for these successes. They think they can develop a global marketing mix for just about *any* product. They fail to

Exhibit 4-8
Continuum of Environmental Sensitivity

see that firms producing and/or selling products near the sensitive end of the continuum should carefully analyze how their products will be seen and used in new environments—and plan their strategies accordingly.[33]

What if risks are still hard to judge?

If the risks of an international opportunity are hard to judge, it may be wise to look first for opportunities that involve exporting. This gives managers a chance to build experience, know-how, and confidence over time. Then the firm will be in a better position to judge the prospects and risks of taking further steps.

Conclusion

Businesses need innovative strategy planning to survive in our increasingly competitive markets. In this chapter, we discussed the variables that shape the environment of marketing strategy planning and how they may affect opportunities. First we looked at how the firm's own resources and objectives may help guide or limit the search for opportunities. Then, we went on to look at the need to understand competition and how to do a competitive analysis. Then, we shifted our focus to the external market environments. They are important because changes in these environments present new opportunities, as well as problems, that a marketing manager must deal with in marketing strategy planning.

The economic environment—including chances of recessions or inflation—also affects the choice of strategies. And the marketer must try to anticipate, understand, and deal with these changes—as well as changes in the technology underlying the economic environment.

The marketing manager must also be aware of legal restrictions and be sensitive to changing political climates. The acceptance of consumerism has already forced many changes.

The cultural and social environment affects how people behave and what marketing strategies will be successful.

Developing good marketing strategies within all these environments isn't easy. You can see that marketing management is a challenging job that requires integration of information from many disciplines.

Eventually, managers need procedures for screening and evaluating opportunities. We explained an approach for developing qualitative and quantitative screening criteria—from an analysis of the strengths and weaknesses of the company's resources, the environmental trends it faces, and top management's objectives. We also discussed ways for evaluating and managing quite different opportunities—using the GE strategic planning grid, SBUs, and portfolio management.

Now we can go on in the rest of the book to discuss how to turn opportunities into profitable marketing plans and programs.

Questions and Problems

1. Do you think it makes sense for a firm to base its mission statement on the type of product it produces? For example, would it be good for a division that produces electric motors to have as its mission: "We want to make the best (from our customers' point of view) electric motors available anywhere in the world"?
2. Explain how a firm's objectives may affect its search for opportunities.
3. Specifically, how would various company objectives affect the development of a marketing mix for a new type of Internet browser software? If this company were just being formed by a former programmer with limited financial resources, list the objectives the programmer might have. Then discuss how they would affect the development of the programmer's marketing strategy.

4. Explain how a firm's resources may limit its search for opportunities. Cite a specific example for a specific resource.
5. Discuss how a company's financial strength may have a bearing on the kinds of products it produces. Will it have an impact on the other three Ps as well? If so, how? Use an example in your answer.
6. In your own words, explain how a marketing manager might use a competitor analysis to avoid situations that involve head-on competition.
7. The owner of a small hardware store—the only one in a medium-sized town in the mountains—has just learned that a large home improvement chain plans to open a new store nearby. How difficult will it be for the owner to plan for this new competitive threat? Explain your answer.
8. Discuss the probable impact on your hometown if a major breakthrough in air transportation allowed foreign producers to ship into any U.S. market for about the same transportation cost that domestic producers incur.
9. Will the elimination of trade barriers between countries in Europe eliminate the need to consider submarkets of European consumers? Why or why not?
10. Which way does the U.S. political and legal environment seem to be moving (with respect to business-related affairs)?
11. Why is it necessary to have so many laws regulating business? Why hasn't Congress just passed one set of laws to take care of business problems?
12. What and who is the U.S. government attempting to protect in its effort to preserve and regulate competition?
13. For each of the *major* laws discussed in the text, indicate whether in the long run the law will promote or restrict competition (see Exhibit 4-3). As a consumer without any financial interest in business, what is your reaction to each of these laws?
14. Are consumer protection laws really new? Discuss the evolution of consumer protection. Is more such legislation likely?
15. Explain the components of product-market screening criteria that can be used to evaluate opportunities.
16. Explain the differences between the total profit approach and the return-on-investment approach to evaluating alternative plans.
17. Explain General Electric's strategic planning grid approach to evaluating opportunities.
18. Distinguish between the operation of a strategic business unit and a firm that only pays lip service to adopting the marketing concept.

Suggested Cases

2. Healthy Foods, Inc.
6. Three Rivers Steel Company

Computer-Aided Problem

4. **Competitor Analysis**

Mediquip, Inc., produces medical equipment and uses its own sales force to sell the equipment to hospitals. Recently, several hospitals have asked Mediquip to develop a laser-beam "scalpel" for eye surgery. Mediquip has the needed resources, and 200 hospitals will probably buy the equipment. But Mediquip managers have heard that Laser Technologies—another quality producer—is thinking of competing for the same business. Mediquip has other good opportunities it could pursue—so it wants to see if it would have a competitive advantage over Laser Tech.

Mediquip and Laser Tech are similar in many ways, but there are important differences. Laser Technologies already produces key parts that are needed for the new laser product—so its production costs would be lower. It would cost Mediquip more to design the product—and getting parts from outside suppliers would result in higher production costs.

On the other hand, Mediquip has marketing strengths. It already has a good reputation with hospitals—and its sales force calls on only hospitals. Mediquip thinks that each of its current sales reps could spend some time selling the new product and that it could adjust sales territories so only four more sales reps would be needed for good coverage in the market. In contrast, Laser Tech's sales reps call on only industrial customers, so it would have to add 14 reps to cover the hospitals.

Hospitals have budget pressures—so the supplier with the lowest price is likely to get a larger share of the business. But Mediquip knows that either supplier's price will be set high enough to cover the added costs of designing, producing, and selling the new product—and leave something for profit.

Mediquip gathers information about its own likely costs and can estimate Laser Tech's costs from industry studies and Laser Tech's annual report. Mediquip has set up a spreadsheet to evaluate the proposed new product.

a. *The initial spreadsheet results are based on the assumption that Mediquip and Laser Tech will split the business 50/50. If Mediquip can win at least 50 percent of the market, does Mediquip have a competitive advantage over Laser Tech? Explain.*

b. *Because of economies of scale, both suppliers' average cost per machine will vary depending on the quantity sold. If Mediquip had only 45 percent of the market and Laser Tech 55 percent, how would their costs (average total cost per machine) compare? What if Mediquip had 55 percent of the market and Laser Tech only 45 percent? What conclusion do you draw from these analyses?*

c. *It is possible that Laser Tech may not enter the market. If Mediquip has 100 percent of the market, and quantity purchases from its suppliers will reduce the cost of producing one unit to $6,500, what price would cover all its costs and contribute $1,125 to profit for every machine sold? What does this suggest about the desirability of finding your own unsatisfied target markets? Explain.*

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

When You Finish This Chapter, You Should

1. Know about population and income trends in global markets—and how they affect marketers.

2. Understand how population growth is shifting in different areas and for different age groups.

3. Know about the distribution of income in the United States.

4. Know how consumer spending is related to family life cycle and other demographic dimensions.

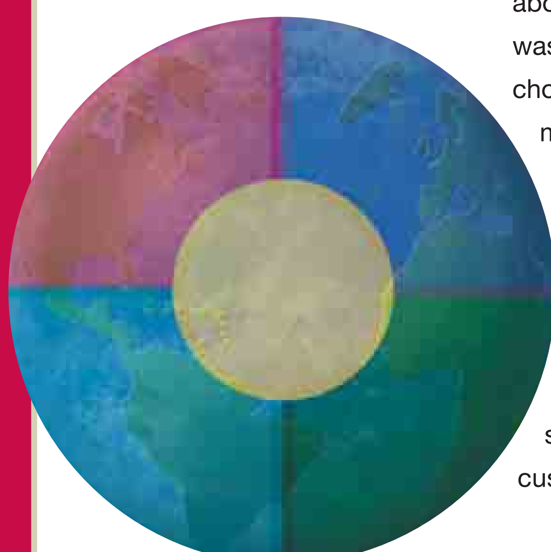
5. Know why ethnic markets are important—and why increasingly they are the focus of multicultural marketing strategies.

6. Understand the important new terms (shown in red).

Chapter Five

Demographic Dimensions of Global Consumer Markets

Charles Schwab has been developing marketing strategies for the financial services company that bears his name for nearly three decades. When he started, investors who wanted to direct their own investments—without a lot of advice or pressure from a broker—didn't have many alternatives. Schwab filled that need with no-frills service and a discount price. In the 1980s, just as the large group of middle-age baby boomers were beginning to worry about investing for retirement, he was the first to give them a lot of choices in a big "supermarket" of mutual funds. Then in the 1990s Schwab pioneered low-cost website-based trading and quickly became the top online broker (www.schwab.com).



Schwab has found ways to satisfy many different types of customers, but he doesn't just

place price promotion produc

see all investors as one big market. Rather, he develops different marketing mixes to meet different needs. Consider, for example, the senior citizen group. Americans over 65 control about 70 percent of the country's investment assets, but Internet use among this group is low compared to younger people. To better meet the needs of the over-65 group, Schwab recently supplemented his online services by adding 3,500 new call-in advisors as well as new branch offices in high-growth areas. He has also added a new division that specializes in estate planning.

Similarly, Schwab has distinct strategies to reach fast-growing ethnic markets. It's no accident that branch offices in cities like San Francisco and New York have service reps who speak Chinese. Schwab has found that many Chinese Americans, even long-term residents of the U.S., like to converse with an advisor in their native language—and these customers are a key target market. While there are only 2.6 million Chinese Americans, the median income of their households is about $65,000, compared to about $40,000 for the typical American household. They also tend to trade stocks two or three times more often than the average investor, and that boosts commission income. To attract Chinese Americans who prefer online trading, Schwab has also set up a special website that offers Chinese language news services (www.schwab.com/chinese). A year after its creation this site had attracted five million hits.

Recently, Schwab's daughter, who was an assistant manager at the Atlanta office, saw a need for the firm to sharpen its focus on women investors. In the past, it appeared that it was enough to just be "gender neutral." However, with changing demographic patterns there has been significant growth in the number of women who manage their own investments. There are now more than 220,000 women who head households with incomes of more than $100,000—and by 2010 that group will double and will control more than a trillion dollars in investments. Importantly, their needs and interests are sometimes different. To better reach this group, Schwab is designing investment seminars specifically for, and taught by, women (www.schwab.com/women). These seminars avoid jargon and include topics on special concerns faced by women, such as how to handle finances after a divorce. Schwab also developed new promotion targeted at women. For example, one clever TV commercial featured Sarah Ferguson, the Duchess of York and a divorced mom, telling a little girl a bedtime tale about a young woman who is whisked away by a knight to a castle, married, and given her every wish "forever and ever." But the ad ends with a shot of Ms. Ferguson saying, "Of course, if it doesn't work out you'll need to understand the difference between a P/E ratio and a dividend yield."

Schwab's strategies and success have not gone unnoticed by competitors. For example, E*Trade, which started on the Web, is opening branches in Super Target stores. And firms like Fidelity Investments are putting multilingual brokers in many offices. So, Schwab will need to continue seeking markets with new growth opportunities.[1]

Target Marketers Focus on the Customer

Target marketers believe that the *customer* should be the focus of all business and marketing activity. These marketers hope to develop unique marketing strategies by finding unsatisfied customers and offering them superior value with more attractive marketing mixes. They want to work in less-competitive markets with more inelastic demand curves. Finding these attractive opportunities takes real knowledge of potential customers and what they want. This means finding those market dimensions that make a difference—in terms of population, income, needs, attitudes, and buying behavior.

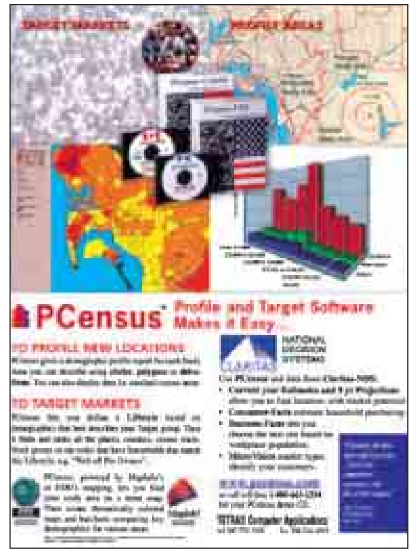
Marketers need to answer three important questions about any potential market:

1. What are its relevant segmenting dimensions?
2. How big is it?
3. Where is it?

The first question is basic. Management judgment—perhaps aided by analysis of existing data and new findings from marketing research—is needed to pick the right dimensions.

To help build your judgment regarding buying behavior, this chapter and the next two will discuss what we know about various kinds of customers and their buying behavior. Keep in mind that we aren't trying to make generalizations about average customers or how the mass market behaves—but rather how *some* people in *some* markets behave. You should expect to find differences.

In this chapter we focus on demographic dimensions. Demographic dimensions provide marketing managers with critical information about the size, location, and characteristics of target markets. Marketing managers must also be alert to



Information about demographic characteristics of consumer markets is readily available and can help marketing managers plan more successful strategies.

demographic trends. They often provide an early warning about new opportunities—or the need to adjust existing strategies.

Get the facts straight—for good marketing decisions

Everybody "knows" that there is a vast and largely untapped market in China and that many people in Somalia live in desperate poverty. It's also clear that demographic dimensions vary within countries: Lots of retired people live in Florida, many Californians speak Spanish, and the population in the Sun Belt states is growing fast. Generalities like these may be partly true—but "partly true" isn't good enough when it comes to making marketing strategy decisions.

Fortunately, much useful information is available on the demographic dimensions of consumer markets around the world. Most of it is free because it has been collected by government agencies. With valid data available, managers have no excuse for basing their decisions on guesses. Look at the data in the next few chapters in terms of selecting relevant market dimensions—and estimating the potential in different market segments. Also, check your own assumptions against this data. Now is a good time to get your facts straight!

People with Money Make Markets

Markets consist of people with money to spend. So it makes sense to start with a broad view of how population, income, and other key demographic dimensions vary for different countries around the world. This will help you to see why so many firms pursue opportunities in international markets. And our examples will illustrate why companies can't depend on half-truths in increasingly competitive international markets.

Marketers search for growing markets

Some marketing managers never consider opportunities outside of their own country. That may make sense in some cases, but it may also lead to missed opportunities. For example, crowded cities in the U.S. may seem to offer great potential, but the U.S. population makes up less than 5 percent of the total world population—which is now over 6 billion.

Marketers who are interested in the rapidly growing teen market often find that teens have many common interests, values, and needs—whether they are shopping online or in-store.

Although a country's current population is important, it provides only a snapshot of the market. The population trend is also important.

Thirty years ago, global population growth was over 2 percent per year. Now it's down to just 1.3 percent. Exhibit 5-1 shows where long-term world population growth will come from. Notice the expected growth of countries in the Middle and Far East. India (with a population of over 1 billion) and China (with a population of almost 1.3 billion) are getting even larger. You can see why so many firms from all over the world want to reach consumers in these countries now that trade barriers are relaxing. Although many of the countries in South America and Africa have much smaller populations, they too are growing at a rapid rate.[2]

Exhibit 5-1 shows that over the long term population growth is expected in most countries. But how rapidly? And will output increase faster than population? These are important questions for marketers. The answers affect how rapidly a country moves to higher stages of development—and becomes a new market for different kinds of products.

Population, income, and other demographic dimensions help to answer these questions. Exhibit 5-2 on pp. 132–133 summarizes current data for representative countries from different regions around the world. Note that population growth varies dramatically from country to country. In general, less-developed countries experience the fastest rate of growth. The populations of Pakistan, Nicaragua, Nigeria, and Saudi Arabia are expected to double in 25 years or less. It will take about five times as long for the population of the U.S. to double. Population growth is even slower in Canada, Japan, and the European countries.[3]

Population is becoming more concentrated

The population in some countries is spread over a very large area. Population density is important to marketers. If the population is very spread out, as it is in many of the African countries, it is difficult and expensive for marketers to adjust time and place discrepancies between producers and consumers. This is especially a problem in countries without efficient highway and rail systems. Similarly, a widely

In countries like the Philippines and Venezuela, where consumers have less purchasing power and shops are small, Colgate is gaining widespread acceptance by providing products in economical sizes.

spread population may make promotion more difficult, especially if there are language differences or communication systems are poor. Of course, even in countries with low population density, major cities may be packed with people.

The extent to which a country's population is clustered around urban areas varies a lot. In the United Kingdom, Argentina, Australia, Israel, and Singapore, for example, more than 85 percent of people live in urban areas. See Exhibit 5-2. By contrast, in Ethiopia, Nepal, and Uganda less than 17 percent of the people live in major urban areas.

People everywhere are moving off the farm and into industrial and urban areas. Shifts in population—combined with already dense populations—have led to extreme crowding in some parts of the world. And the crowding is likely to get worse.

The worldwide trend toward urbanization has prompted increased interest in international markets. For many firms, the concentration of people in major cities simplifies Place and Promotion strategy decisions—especially for major cities in the wealthiest nations. Affluent, big-city consumers often have similar lifestyles and needs. Thus, many of the products successful in Toronto, New York, or Paris are likely to be successful in Caracas and Tokyo. The spread of the Internet, satellite TV, and other communication technologies will accelerate this trend.

However, keep in mind that many of the world's consumers—whether crowded in cities or widely spread in rural areas—live in deplorable conditions. These people have little hope of escaping the crush of poverty. They certainly have needs—but they don't have the income to do anything about the needs.

There's no market when there's no income

Profitable markets require income—as well as people. The amount of money people can spend affects the products they are likely to buy. When considering international markets, income is often one of the most important demographic dimensions.

There are a variety of different measures of national income. One widely used measure is **gross national product (GNP)**—the total market value of goods and services produced by a country's economy in a year. Gross domestic product (GDP) is a similar measure that often is used to describe the U.S. economy. The difference between the two measures is that GNP for a nation does not include income earned by foreigners who own resources in that nation. By contrast, the

Exhibit 5-1 Projected Population Increase (millions) between 1994 and 2020

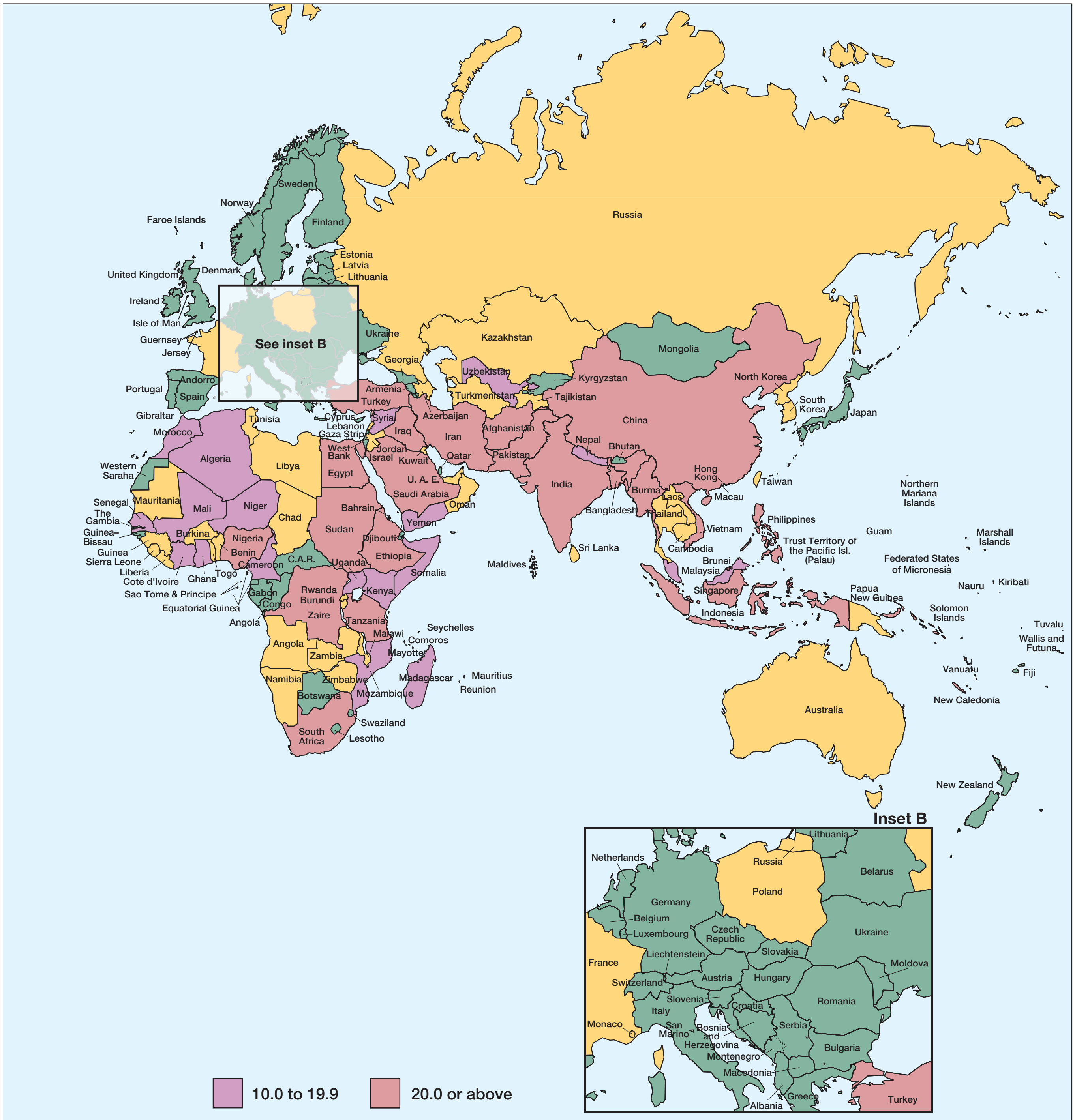

Russia
Sweden
Norway
Finland
Faroe Islands
Estonia
Latvia
Lithuania
United Kingdom
Denmark
Ireland
Isle of Man
Guernsey
Jersey
See inset B
Ukraine
Georgia
Kazakhstan
Mongolia
Uzbekistan
Kyrgyzstan
North Korea
South Korea
Japan
Portugal
Andorra
Spain
Gibraltar
Morocco
Tunisia
Armenia
Turkey
Turkmenistan
Tajikistan
China
Cyprus
Lebanon
Gaza Strip
Syria
Azerbaijan
Iraq
Iran
Afghanistan
Western Sahara
Algeria
Libya
West Bank
Israel
Jordan
Kuwait
Qatar
Pakistan
Nepal
Bhutan
Egypt
U. A. E.
Saudi Arabia
Oman
India
Hong Kong
Macau
Taiwan
Northern Mariana Islands
Senegal
The Gambia
Guinea-Bissau
Guinea
Sierra Leone
Liberia
Cote d'Ivoire
Ghana
Togo
Sao Tome & Principe
Equatorial Guinea
Mauritania
Mali
Niger
Chad
Bahrain
Sudan
Burkina
Nigeria
Benin
Cameroon
C.A.R.
Djibouti
Ethiopia
Yemen
Somalia
Uganda
Kenya
Rwanda
Burundi
Gabon
Congo
Zaire
Angola
Tanzania
Malawi
Seychelles
Comoros
Mayotte
Zambia
Namibia
Zimbabwe
Botswana
Mozambique
Madagascar
Mauritius
Reunion
South Africa
Swaziland
Lesotho
Bangladesh
Burma
Laos
Thailand
Vietnam
Cambodia
Sri Lanka
Maldives
Philippines
Trust Territory of the Pacific Isl. (Palau)
Guam
Marshall Islands
Federated States of Micronesia
Brunei
Malaysia
Singapore
Indonesia
Papua New Guinea
Nauru
Kiribati
Solomon Islands
Tuvalu
Wallis and Futuna
Vanuatu
Fiji
New Caledonia
Australia
New Zealand
Inset B
Netherlands
Lithuania
Russia
Belarus
Poland
Germany
Belgium
Luxembourg
Czech Republic
Ukraine
Liechtenstein
Slovakia
France
Moldova
Switzerland
Austria
Hungary
Slovenia
Croatia
Romania
Italy
Monaco
San Marino
Bosnia and Herzegovina
Serbia
Montenegro
Bulgaria
Macedonia
Greece
Albania
Turkey
10.0 to 19.9
20.0 or above

Exhibit 5-2 Demographic Dimensions for Representative Countries

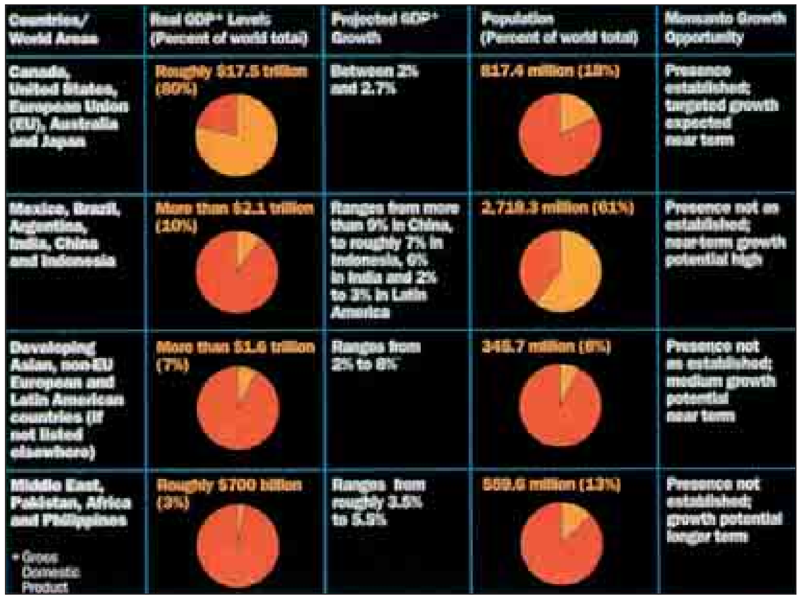
Country	2000 Population (000s)	1990–2000 Annual Percent Population Growth	2000 Years for Population to Double	2000 Population Density (people/ square mile)	1999 Percent of Population in Urban Areas	1999 GNP (millions of $U.S.)	1999 GNP per Capita	1999 GDP (millions of $U.S.)	1999 Illiteracy Percent
Algeria	31,194	2.1	29	34	60	46,455	1,550	47,015	33
Argentina	36,955	1.2	62	35	90	277,882	7,600	281,942	3
Australia	19,165	1.2	110	6	85	380,791	20,050	389,691	0
Bangladesh	129,194	1.6	38	2,305	24	46,960	370	45,779	59
Brazil	172,860	1.3	45	52	81	742,819	4,420	760,345	15
Cameroon	15,422	2.7	27	84	48	8,509	580	8,781	25
Canada	31,278	1.2	178	8	77	591,354	19,320	612,049	0
Chile	15,154	1.4	54	52	85	71,145	4,740	71,093	4
China	1,261,832	1.0	79	342	32	980,246	780	991,203	17
Colombia	39,686	1.9	34	91	73	93,558	2,250	88,596	9
Croatia	4,282	−0.5	no	211	57	20,932	4,650	21,752	2
Cuba	11,142	0.6	103	260	75	—	—	—	3
Ecuador	12,920	2.2	33	116	64	16,231	1,310	18,713	9
Egypt	68,360	2.0	35	177	45	87,530	1,400	92,413	45
Ethiopia	64,117	2.8	29	150	17	6,578	100	6,534	63
Finland	5,167	0.4	433	40	67	122,874	23,780	126,130	0
France	59,330	0.4	204	279	75	1,427,160	23,480	1,410,260	0
Germany	82,797	0.4	no	596	87	2,079,230	25,350	2,081,200	0
Ghana	19,534	2.4	29	212	38	7,396	390	7,606	30
Greece	10,602	0.4	no	208	60	124,010	11,770	123,934	3
Haiti	6,868	1.3	40	599	35	3,163	410	3,871	51
Hungary	10,139	−0.2	no	279	64	46,810	4,650	48,355	1
Iceland	276	0.8	81	7	92	8,109	29,280	8,483	0
India	1,014,004	1.8	39	789	28	442,233	450	459,765	44
Indonesia	224,784	1.8	44	289	40	119,544	580	140,964	14
Iran	65,620	1.6	48	107	61	110,535	1,760	101,073	24
Iraq	22,676	2.2	25	137	74	—	—	—	45
Ireland	3,797	0.8	116	140	59	71,405	19,160	84,861	0
Israel	5,842	2.6	45	766	91	104,081	17,450	125,031	4
Italy	57,634	0.2	no	497	67	1,135,990	19,710	1,149,960	2
Jamaica	2,653	0.7	45	615	56	6,042	2,330	6,134	14
Japan	126,550	0.2	462	870	79	4,078,920	32,230	4,395,080	0
Kenya	30,340	2.4	33	135	32	10,601	360	10,603	19
Kuwait	1,974	−0.8	32	318	97	32,270	19,020	29,572	18
Libya	5,115	2.1	28	8	87	—	—	—	21
Madagascar	15,506	3.0	24	66	29	3,716	250	3,733	34
Malaysia	21,793	2.2	34	183	57	77,278	3,400	74,634	13

GDP does include foreign income. The measure you use can make a difference, especially when comparing countries with different patterns of international investment. For example, Ford has a factory in Thailand. The GDP measure for Thailand would include the profits from that factory because they were earned in that country. However, Ford is not a Thai firm and most of its profit will ultimately flow out of Thailand. Thus, the Thai GNP would not include those profits. You should see that using GDP income measures can give the impression that people in less-developed

Country	2000 Population (000s)	1990–2000 Annual Percent Population Growth	2000 Years for Population to Double	2000 Population Density (people/ square mile)	1999 Percent of Population in Urban Areas	1999 GNP (millions of $U.S.)	1999 GNP per Capita	1999 GDP (millions of $U.S.)	1999 Illiteracy Percent
Mexico	100,350	1.7	36	132	74	428,794	4,400	474,951	9
Morocco	30,122	2.0	41	167	55	33,816	1,200	35,238	52
Mozambique	19,105	2.9	32	62	39	3,889	230	4,169	57
Nepal	24,702	2.5	28	421	12	5,091	220	4,904	60
Netherlands	15,892	0.6	193	1,010	89	384,325	24,320	384,766	0
Nicaragua	4,813	2.8	23	101	56	2,110	430	2,302	32
Nigeria	123,338	2.9	24	346	43	37,882	310	43,286	37
North Korea	21,688	0.8	48	466	60	—	—	—	1
Norway	4,481	0.5	217	36	75	146,430	32,880	145,449	0
Pakistan	141,554	2.2	25	490	36	63,971	470	59,880	55
Panama	2,808	1.6	41	98	56	8,624	3,070	9,606	8
Peru	27,013	2.1	32	55	72	60,319	2,390	57,318	10
Philippines	81,160	2.2	31	693	58	77,966	1,020	75,350	5
Poland	38,646	0.1	no	310	65	153,065	3,960	154,146	0
Romania	22,411	−0.2	no	244	56	34,188	1,520	33,750	2
Russia	146,001	−0.1	no	22	77	332,536	2,270	375,345	1
Saudi Arabia	22,024	3.3	23	26	85	143,361	6,910	128,892	24
Singapore	4,152	3.2	84	16,714	100	95,429	29,610	84,945	8
Somalia	7,253	0.8	24	29	27	—	—	—	—
South Africa	43,421	1.3	55	92	52	133,216	3,160	131,127	15
South Korea	47,471	1.0	82	1,234	81	397,910	8,490	406,940	2
Spain	39,997	0.2	6,931	202	77	551,560	14,000	562,245	2
Sri Lanka	19,239	1.1	60	757	23	15,176	810	15,707	9
Sudan	35,080	2.8	32	30	35	8,300	290	10,695	43
Sweden	8,873	0.4	no	51	83	221,764	25,040	226,388	0
Switzerland	7,262	0.6	315	448	68	273,061	38,350	260,299	0
Syria	16,306	2.7	25	231	54	15,172	970	19,380	26
Tanzania	35,306	3.0	24	97	32	8,027	240	8,777	25
Thailand	61,231	1.1	70	313	21	121,019	1,960	123,887	5
Turkey	65,667	1.6	46	218	74	186,289	2,900	188,374	15
Uganda	23,318	3.1	24	251	14	6,786	320	6,349	34
Ukraine	49,153	−0.5	no	212	68	42,713	850	42,415	0
United Kingdom	59,508	0.3	546	632	89	1,338,080	22,640	1,373,610	0
United States	281,422	1.0	120	77	77	8,350,960	30,600	8,708,870	0
Venezuela	23,543	2.0	34	69	87	86,963	3,670	103,918	8
Vietnam	78,774	1.7	48	615	20	28,157	370	28,567	7
Zimbabwe	11,343	1.2	69	75	35	6,131	520	5,716	12

countries have more income than they really do. For that reason, we'll focus on comparisons that are based on GNP.

Exhibit 5-2 gives an estimate of GNP and GDP for each country listed. You can see that the more developed industrial nations—including the U.S., Japan, and Germany—have the biggest share of the world's GNP. This is why so much trade takes place between these countries—and why many firms see them as the more important markets.[4]



This chart from Monsanto's annual report shows how the firm wants to build its presence in countries with large populations and projected strong economic growth. India is an example of a key target.

People can't spend what they don't have

GNP tells us about the income of a whole nation, but in a country with a large population that income must be spread over more people. GNP per person is a useful figure because it gives some idea of the income level of people in a country. Exhibit 5-2 shows, for example, that GNP per capita in the U.S. is quite high—about $30,600. Japan, Norway, Switzerland, and Singapore are among those with the highest GNP per capita. In general, markets like these offer the best potential for products that are targeted at consumers with higher income levels.

Many managers, however, see great potential—and less competition—where GNP per capita is low. For example, Mars is making a big push to promote its candy in the countries of Eastern Europe. As with many other firms, it hopes to establish a relationship with consumers now, and then turn strong brand loyalty into profitable growth as consumer incomes increase.

A business and a human opportunity

The large number of countries with low GNP per capita is a stark reminder that much of the world's population lives in extreme poverty. Even among countries with the largest overall GNPs, you see some sign of this. In India, for example, GNP per person is only $450 a year. Many countries are in the early stages of economic development. Most of their people work on farms—and live barely within the money economy. At the extreme, in Ethiopia GNP per person per year is only about $100 (in U.S. dollars). To put this in perspective, 60 percent of the world's population—in 61 countries—receive only 6 percent of the world's total income, or about $2 a day.

These people, however, have needs, and many are eager to improve themselves. But they may not be able to raise their living standards without outside help. This presents a challenge and an opportunity to the developed nations—and to their business firms.

Some companies are trying to help the people of less-developed countries. Corporations such as Pillsbury, Monsanto, and Coca-Cola have developed nutritious foods that can be sold cheaply—but still profitably—in poorer countries.[5]

Computer Company Creates Legendary Success in China

China is the home of almost 1.3 billion people and accounts for about 25 percent of the world's population. Its population would be even larger, but about 20 years ago the communist government set a rule that most families could have only one child. Although the Chinese economy is changing rapidly, the gross national product per capita in China is only about 2.5 percent what it is in the U.S. and Japan. To put that in perspective, the average per capita income in China is less than $70 per month. Yet, not everyone in China is on the low end of the income distribution, and with so many people the demand for some goods and services is huge. In fact, China is becoming the world's fastest growing market for personal computers and mobile phones. For example, by 2005 it is expected that one out of four mobile phones in the world will be in China—a total of 250 million units. Similarly, although only about 1 out of every 175 Chinese currently has a personal computer, sales in China are already over 1.5 million units a year. It's easy to see why firms like Compaq and Dell that are leaders in other parts of the world want to capture more of this market. But they are finding it difficult to compete with Legend, a Chinese computer maker. One reason is that managers at Legend understand their customers better. For example, unlike customers in more developed markets, most Chinese are first-time buyers who want a lot of hand-holding and service. So Legend developed easy-to-use software and Chinese language tutorials for its high-quality computers. Legend also installs speech recognition software; that helps because there are many more characters in the Chinese language than letters in the English alphabet (and keys on the typical keyboard). Legend also has a big advantage in reaching customers. It has over 1,800 local distributors and more than 50 of its own stores. They help overcome distribution problems caused by China's inefficient highway and rail system, and they support customers with good service and free training. When China enters the World Trade Organization, lower import tariffs on foreign made computers will probably increase competition. However, by then, market growth may be slower.[6]

www.mhhe.com/fourps

What do Third World consumers really need?

Marketing managers from developed nations sometimes face an ethical dilemma about whether their products help or hurt consumers in less-developed nations. For example, a United Nations report criticized Coke and Pepsi for expanding their soft-drink sales in the Philippines. The study concluded that consumers had shifted to soft drinks from local beverages—such as a mixture of lime juice and coconut water—that provided needed vitamins.

In another much publicized case, producers of infant formula were criticized for giving free samples to hospitals. Nestlé and other big suppliers in this market say that they only gave the free samples to children who were in need—and at the request of hospitals. But critics argued that the practice encouraged new mothers to give up breast feeding. Away from the hospital, mothers would rely on unsanitary water supplies. Such improper use of the formula could lead to malnutrition and other illnesses. So, Nestlé and the others pledged to stop giving away free samples. Although that step stopped some misuse, now the formula is not available to many people who really need it. For example, over a million babies have been infected with AIDS from breast feeding. To help fight this staggering epidemic, Nestlé is willing to donate formula, but not unless the World Health Organization agrees that it is not a violation of its pledge.

In cases like these, a marketing manager may need to weigh the benefits and risks of trying to serve Third World markets. For example, in the U.S. Quicksilver Enterprises sells its 250-pound aluminum and fiberglass "ultralight" airplanes—that look like go-carts with wings—to wealthy hobbyists. However, Quicksilver found a growing market for ultralights in developing nations, where farmers use them for crop dusting. They help farmers increase production of much needed foods. So what's the problem? In the U.S., the government bans ultralights as not being safe enough for crop dusting. Some critics argue that a firm shouldn't sell its products in foreign markets if they are illegal in the U.S. But ultimately, the marketing manager often must decide what to do.[7]

Reading, writing, and marketing problems

The ability of a country's people to read and write has a direct influence on the development of its economy—and on marketing strategy planning. The degree of literacy affects the way information is delivered—which in marketing means promotion. Unfortunately, only about three-fourths of the world's population can read and write. Data on illiteracy rates is inexact because different countries use different measures. Even so, you may be surprised by the high illiteracy rates for some of the countries in Exhibit 5-2.

Illiteracy sometimes causes difficulties with product labels and instructions—for which we normally use words. This was one issue in the infant formula conflict. In an even more extreme case, some producers of baby food found that consumers misinterpreted a baby's picture on their packages. Illiterate natives believed that the product was just that—a ground-up baby! Many companies meet this lack of literacy with instructions that use pictures instead of words. Singer used this approach with its sewing machines.

Even in Latin America—which has generally higher literacy rates than Africa or Asia—a large number of people cannot read and write. Marketers have to use symbols, colors, and other nonverbal means of communication if they want to reach the masses.[8]

Much segmenting may be required

Marketers can learn a great deal about possible opportunities in different countries by studying available demographic data and trends. The examples we considered here give you a feel, but much more useful data is available. For example, *The World Factbook* is prepared by the Central Intelligence Agency (CIA) for the use of U.S. government officials, but it is available to everyone. It gives facts and statistics on each country in the world. This book can be accessed at the CIA's website (www.odci.gov/cia/publications/factbook). The World Bank publishes *The World Development Indicators,* another excellent source for statistics on individual countries. It is available at the World Bank's website (www.worldbank.org/data/wdi). The International Programs Center of the U.S. Census Bureau also publishes an analysis on world population and related topics called *World Population Profile.* You can also access useful statistics for individual countries at the Census Bureau's website (www.census.gov/ipc).

Internet

Internet Exercise Visit the website for the CIA's *World Factbook* (www.odci.gov/cia/publications/factbook) and compare the profile data for Canada and Australia. How are they similar and how are they different?

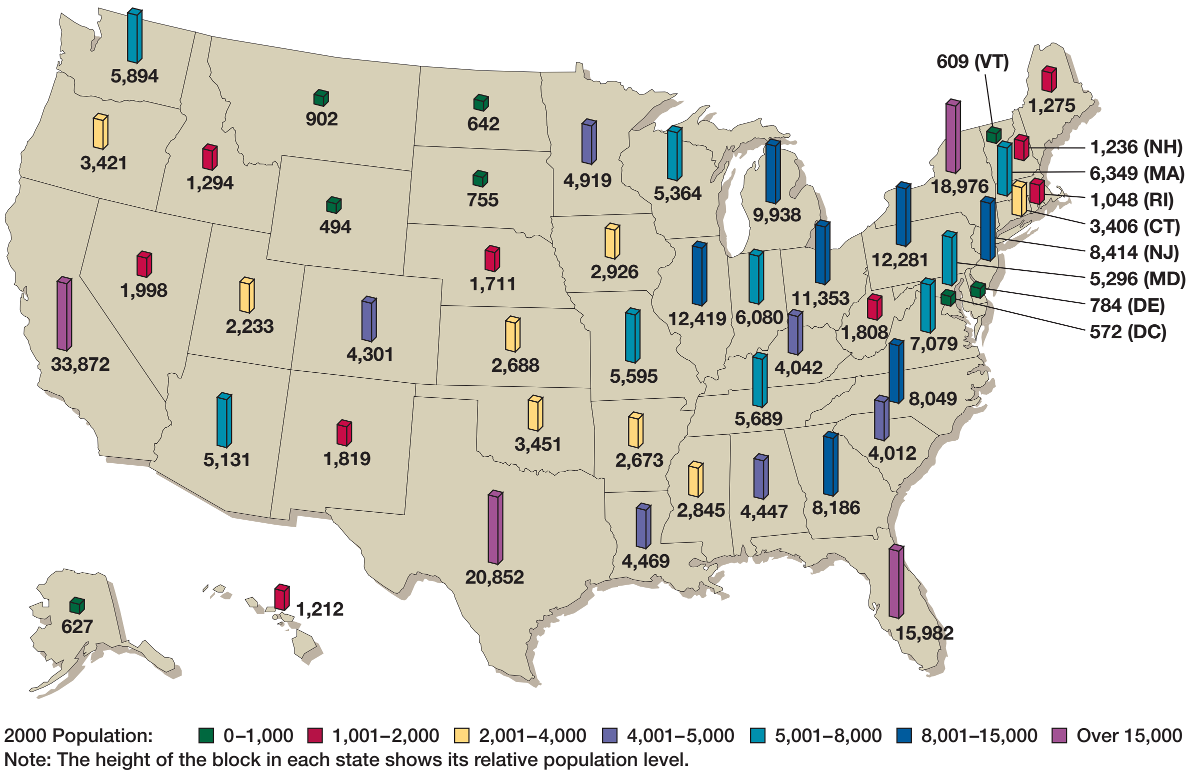
After finding some countries or regions of possible interest (and eliminating unattractive ones), much more segmenting may be required. To illustrate how useful demographic dimensions can be in this effort, we will consider specific characteristics of the U.S. market in some detail. For additional data on the U.S. market, you can go to the Census Bureau's website (www.census.gov). Similar ideas apply to other markets around the world.

Population Trends in the U.S. Consumer Market

Where does your state stand?

Exhibit 5-3 is a map of the U.S. showing the relative population for each state. The "high areas" on this map emphasize the concentration of population in different geographic regions. Note that California is the most populated state, with Texas a distant second. New York, in third place, still has almost as large a population as Texas, but Texas' population is more spread out. More generally, the heavy concentration of people in the Northeast makes this market larger than the whole West Coast.

Exhibit 5-3 Map of U.S. Showing Population by State (all figures in thousands)



As is the case in many countries, the most populated U.S. areas developed near inexpensive water transportation—on ocean harbors (East and West Coasts), along major rivers (like the Mississippi), or in the Great Lakes region. Obviously, these markets are attractive to many marketers. But this can also mean tough competition—as in the big urban East and West Coast markets.

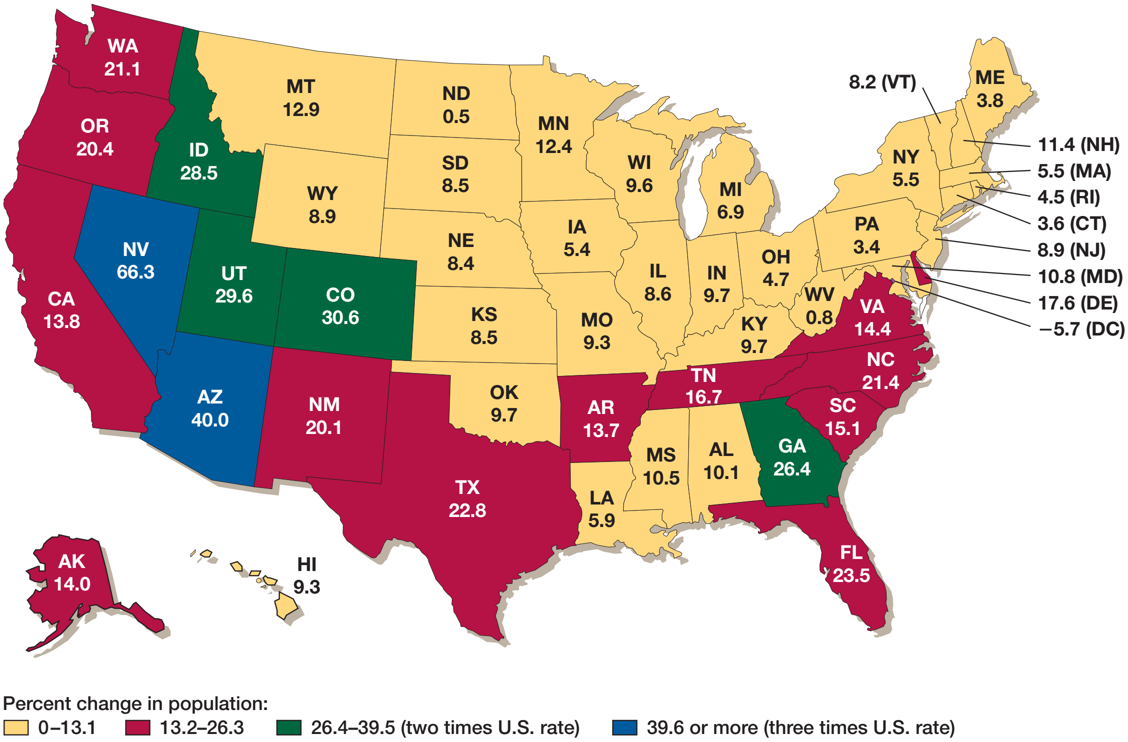
Marketers anxious to avoid the extremely competitive East and West Coast markets often view the midwestern and southern states as unique target markets. Note, too, the few people in the plains and mountain states, which explains why some national marketers pay less attention to these areas. Yet these states can provide an opportunity for an alert marketer looking for less competitive markets.

Where are the people today and tomorrow?

Population figures for a single year don't show the dynamic aspects of markets. Currently, U.S. population is about 281 million. By 2050, the U.S. population could rise to more than 400 million. But it is important to remember that the population has been growing continuously since the founding of the country. It almost doubled from 1950 to the present. But—and this is valuable to marketers—the population did *not* double everywhere. Marketers always look for fast-growing markets. They want to know where growth has occurred recently—and where growth is likely to occur in the future.

Exhibit 5-4 shows the percentage growth in population in different regions of the country. The states with the darkest shading are growing at the fastest rate. Note that the greatest growth is in the West—in states such as Nevada, Arizona, Idaho, Utah, and Colorado. Growth continued in the Sun Belt states of the South as well, with Georgia leading the way with 26 percent, and other Sun Belt states like Florida, Texas, North Carolina, and Tennessee growing rapidly.

Exhibit 5-4 Percent Change in Population by State, 1990–2000



Notice that some of the most populated areas in Exhibit 5-3 are not growing the fastest. The population of New York, for example, grew at less than 6 percent during the last decade. Other states like Connecticut and Pennsylvania grew less than 4 percent. In fact, the West is growing at almost four times the rate of the Northeast.

These different rates of growth are especially important to marketers. Sudden growth in one area may create a demand for many new shopping centers—while retailers in declining areas face tougher competition for a smaller number of customers. In growing areas, demand may increase so rapidly that profits may be good even in poorly planned facilities.

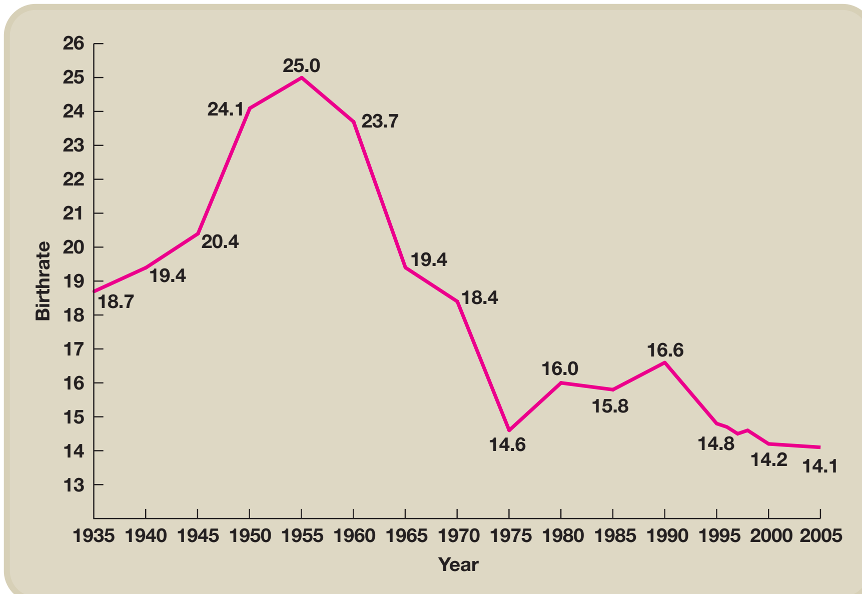
These maps summarize state-level data to give the big picture. However, much more detailed population data is available. You can obtain detailed census data—or updated estimates—for very small geographic areas. Just as we mapped population changes at the state level, a local marketer can divide a big metropolitan area into many smaller areas to see where the action is. As this decade continues, census data may become outdated—but by then local and state government planning groups may be able to provide updates.

Population will keep growing, but . . .

Despite the large increases, the *rate* of population growth in the U.S. has slowed dramatically—to about 1 percent a year during the last decade. In fact, many U.S. marketers who enjoyed rapid and profitable growth in the 1960s and 1970s know that the domestic picnic is over. They now turn to international markets where population—and sales revenues—continue to grow.

In the U.S., most of our future growth is expected to come from immigration. In fact, even now the total U.S. population would start to decline if immigration stopped. Let's look at some of these trends—and what they mean to marketing managers.[9]

Exhibit 5-5
Changes in the U.S. Birthrate, 1935–2005



Birthrate—boom or bust?

The U.S. **birthrate**—the number of babies born per 1,000 people—fluctuated greatly in the last 50 years. Exhibit 5-5 shows a clear pattern. A post–World War II baby boom began as returning soldiers started families, and it lasted about 15 years into the early 1960s. In the 1970s the situation changed to a "baby bust" as more women stayed in the workforce and couples waited longer to have children. When you see the dip in the birthrate—and think about the declining market for baby products—you can understand why Johnson & Johnson promotes its baby shampoo to adults who want a gentle product. You can also understand why Johnson & Johnson looks for opportunities in Asia and Latin America where the birthrate is higher.

The U.S. birthrate hit a low in 1976 and then rose again—but only slightly. From 1980 to 1990 the birthrate was between 15 and 17. It is starting to drop again now, and this trend should continue—with an estimated birthrate of about 14.1 around the year 2005. These shifts are easy to explain. As the baby boom generation entered its child-bearing years, there were more women to have babies. However, as the boomers aged this baby "boomlet" passed and turned to what some have called a "baby bust." In addition, American couples are having fewer children. There may be more demand for small apartments, in-home entertainment, travel, and smaller food packages.

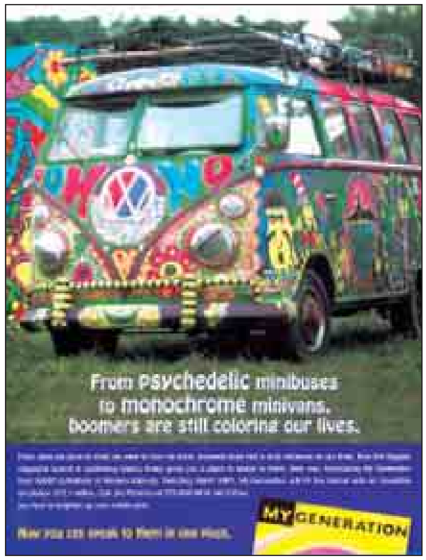
With fewer children, parents can spend more money on each child. For example, expensive bikes, video game consoles, MP3 players, and designer clothes for children have all sold well in recent years because parents can indulge one or two children more easily than a houseful.[10]

The graying of America

Because our population is growing slowly, the average age is rising. In 1970, the average age of the population was 28—but by the year 2000 the average age jumped to about 36.

Stated another way, the percentage of the population in different age groups is changing. Exhibit 5-6 shows the number of people in different age groups in 1990 and 2000—and how the size of these groups will look in 2010. Note the big increases in the 45–64 age group from 1990 to 2000 and also 2000 to 2010.

Highly targeted advertising media such as magazines and cable TV are proving especially effective at targeting messages to specific groups.



The major reason for the changing age distribution is that the post–World War II baby boom produced about one-fourth of the present U.S. population. This large group crowded into the schools in the 1950s and 60s—and then into the job market in the 1970s. In the 1980s, they swelled the middle-aged group. And early in the 21st century, they will reach retirement—still a dominant group in the total population. According to one population expert, "It's like a goat passing through a boa constrictor."

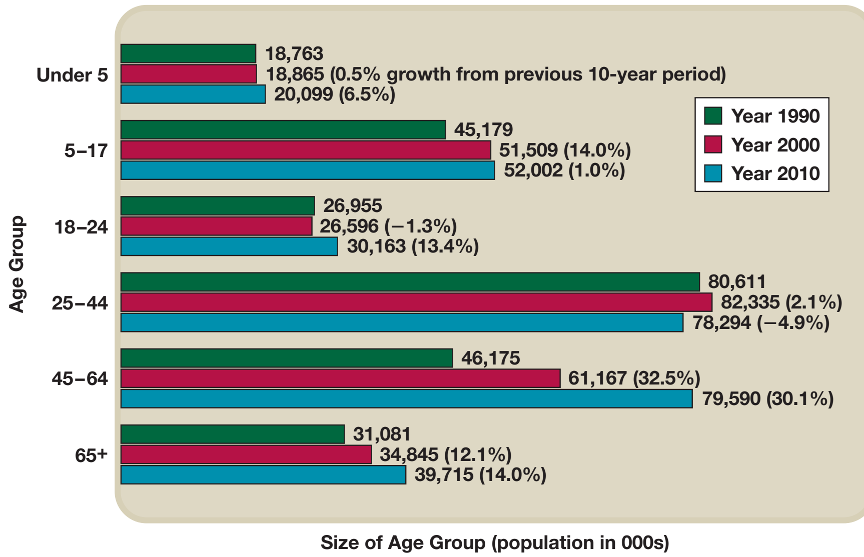
Some of the effects of this big market are very apparent. For example, recording industry sales exploded—to the beat of rock and roll music and the Beatles—as the baby boom group moved into their record-buying teens. Soon after, colleges added facilities and faculty to handle the surge—then had to cope with excess capacity and loss of revenue when the student-age population dwindled. To relieve financial strain many colleges now add special courses and programs for adults to attract the now-aging baby boom students. On the other hand, the fitness industry and food producers who offer low-calorie foods are reaping the benefit of a middle-aged "bulge" in the population.

Medical advances help people live longer and are also adding to the proportion of the population in the senior citizen group. Note from Exhibit 5-6 that the over-65 age group will grow another 14 percent by 2010. Even more dramatic, by 2030 the over-65 group will double in size and they will be almost 20 percent of the total U.S. population. This ongoing growth creates new opportunities for such industries as tourism, health care, and financial services.[11]

The teen cycle is starting again

While society—and many marketers—have been fixated on the aging baby boomers, the ranks of teenagers have started to grow again. This is in part reflected in the 14.0 percent growth of the 5–17 age group between 1990 and 2000 and the 13.4 percent growth rate of the 18–24 age group in this decade (see Exhibit 5-6). But the coming changes are even bigger than this suggests. For 15 years, there was a steady decline in the number of teenagers. Now that has reversed. Between 1995 and 2005, the teenage group will grow at close to twice the rate of the overall population. By the time the number of teens peaks in 2010, the size of this group will top the baby boom–fueled teen explosion of the 1970s. In 2010, there will be over

Exhibit 5-6
Population Distribution (and Percent Growth Rate) by Age Groups for Different 10-Year Periods



35 million U.S. teens—and along the way a new teen-oriented culture will reshape society and markets. However, marketers who simultaneously try to appeal to aging baby boomers and to teens may find themselves right in the middle of a real clash of cultures.[12]

Household composition is changing

Many people incorrectly think of the "typical" American household as a married couple with two children—living in the suburbs. This never was true and is even less true now. Less than 24 percent of households consist of a husband, wife, and children under 18. Another 28 percent of households involve married couples, but ones without children living at home.

Although almost all Americans marry, they are marrying later, delaying child bearing, and having fewer children. And couples don't stay together as long as they used to. The U.S. has the highest divorce rate in the world—about 50 percent of marriages end in divorce. That helps to explain why more than 12 percent of U.S. households are now families headed by a single woman. Yet, divorce does not seem to deter people from marrying again. Over 80 percent of divorced people remarry in what is described as "the triumph of hope over experience." Still, even with all this shifting around, at any given time only about 60 percent of all adults are married.

Nonfamily households are increasing

Many households are not families in the traditional sense. There are now about 5.5 million unmarried couples who live together. That's a whopping 70 percent increase during the last decade. Some of these arrangements are temporary—as in college towns or in large cities where recent graduates go for their first "real" job. But the majority are older couples who choose not to get married. The number of these nontraditional households is still relatively small. But marketers pay special attention to them because they are growing at a much higher rate than the traditional family households. And they have different needs and attitudes than the stereotypical American family. To reach this market, some banks changed their policies about loans to unmarried couples for homes, cars, and other major purchases. And some insurance companies designed coverage for unmarried couples.

Single-adult households are also on the rise and they account for over one-fourth of all households—almost 27 million people! These include young adults who leave home when they finish school, as well as separated, divorced, or widowed people who live alone. In some big cities, the percentage of single-person households is even higher—around 30 percent in New York and Washington, D.C. These people need smaller apartments, smaller cars, smaller food packages, and, in some cases, less-expensive household furnishings because many singles don't have much money. Other singles have ample discretionary income and are attractive markets for top-of-the-line clothing, expensive electronic gadgets, status cars, travel, nice restaurants, and trendy bars.[13]

The shift to urban and suburban areas

Migration from rural to urban areas has been continuous in the U.S. since 1800. In 1920, about half the population lived in rural areas. By 1950, the number living on farms dropped to 15 percent—and now it is less than 2 percent. We have become an urban and suburban society.[14]

Since World War II, there has been a continuous flight to the suburbs by middle-income consumers. By 1970, more people lived in the suburbs than in the central cities. Retailers moved too—following their customers. Lower-income consumers—often with varied ethnic backgrounds—moved in, changing the nature of markets in the center of the city.

Industries too have been fleeing the cities, moving many jobs closer to the suburbs. Today's urban economic system is not as dependent on central cities. A growing population must go somewhere—and the suburbs can combine pleasant neighborhoods with easy transportation to higher-paying jobs nearby or in the city.

Purchase patterns are different in the suburbs. For example, a big city resident may not need or own a car. But with no mass transportation, living carless in the suburbs is difficult. And in some areas, it almost seems that an SUV or a minivan—to carpool kids and haul lawn supplies or pets—is a necessity.

Local political boundaries don't define market areas

These continuing shifts—to and from urban and suburban areas—mean that the usual practice of reporting population by city and county boundaries can result in misleading descriptions of markets. Marketers are more interested in the size of homogeneous *marketing* areas than in the number of people within political boundaries. To meet this need, the U.S. Census Bureau has developed a separate population classification based on metropolitan statistical areas. Much data is reported on the characteristics of people in these areas. The technical definition of these areas has changed over time. But basically a **Metropolitan Statistical Area (MSA)** is an integrated economic and social unit with a large population nucleus. Generally, an MSA centers on one city or urbanized area of 50,000 or more inhabitants and includes bordering urban areas.

The largest MSAs—basically those with a population of more than a million—are called Consolidated Metropolitan Statistical Areas. Over three-fourths of all Americans live in MSAs and almost 40 percent live in the 18 largest CMSAs. More detailed data is available for areas within these sprawling, giant urban areas.

Big targets are attractive—but very competitive

Some national marketers sell only in these metro areas because of their large, concentrated populations. They know that having so many customers packed into a small area can simplify the marketing effort. They can use fewer middlemen and still offer products conveniently. One or two local advertising media—a city newspaper or TV station—can reach most residents. If a sales force is needed, it will incur less travel time and expense because people are closer together.

Metro areas are also attractive markets because they offer greater sales potential than their large population alone suggests. Consumers in these areas have more money to spend because wages tend to be higher. In addition, professionals—with higher salaries—are concentrated there. But, remember that competition for consumer dollars is usually stiff in an MSA.[15]

The mobile ones are an attractive market

Of course, none of these population shifts is necessarily permanent. People move, stay awhile, and then move again. In fact, about 16 percent of Americans move each year. Although about 6 out of 10 moves are within the same county, both the local and long-distance mobiles are important market segments.

Often people who move in the same city trade up to a bigger or better house or neighborhood. They tend to be younger and better educated people on the way up in their careers. Their income is rising—and they have money to spend. Buying a new house may spark many other purchases too. The old sofa may look shabby in the new house. And the bigger yard may require a new lawn mower—or even a yard service.

Many long-distance moves are prompted by the search for a better lifestyle. Many affluent retirees, for example, move to find a more comfortable life. Young people also hop from place to place—attracted by better job opportunities. This applies to graduates moving to high-paying, new-economy jobs as well as recent immigrants whose only choice may be a low-wage service job.

Regardless of why someone moves, many market-oriented decisions have to be made fairly quickly after a move. People must find new sources of food, clothing, medical and dental care, and household products. Once they make these basic buying decisions, they may not change for a long time. Alert marketers try to locate these potential customers early—to inform them of offerings before they make their purchase decisions. Retail chains, "national" brands, and franchised services available in different areas have a competitive advantage with mobiles. The customer who moves to a new town may find the familiar CVS sign down the street and never even try its local competitors.[16]

Income Dimensions of the U.S. Market

So far, we have been concerned mainly with the *number* of different types of people—and *where* they live.

More people are in middle and upper income levels

Earlier in this chapter you saw how GNP figures can be helpful in analyzing markets. But GNP figures are more meaningful to marketing managers when converted to family or household income—and its distribution. Family incomes in the U.S. generally increased with GNP. But even more important to marketers, the *distribution* of income changed drastically over time.

Fifty years ago, the U.S. income distribution looked something like a pyramid. Most families were bunched together at the low end of the income scale—just over a subsistence level—to form the base of the income pyramid. There were many fewer families in the middle range, and a relative handful formed an elite market at the top. This pattern still exists in many nations.

By the 1970s, real income (buying power) in the U.S. had risen so much that most families—even those near the bottom of the income distribution—could afford a comfortable standard of living. And the proportion of people with middle incomes was much larger. Such middle-income people enjoyed real choices in the marketplace.

This revolution broadened markets and drastically changed the U.S. marketing system. Products viewed as luxuries in most parts of the world sell to "mass" markets

Marketers are very aware that spending varies with income and other demographic dimensions.

in the U.S. And these large markets lead to economies of scale, which boost our standard of living even more. Similar situations exist in Canada, many Western European countries, Australia, New Zealand, and Japan.

Real income growth has slowed—but for how long?

Trends in median family income from 1960 to 1999 reflect this upward shift in the income distribution—and the increased number of families with more money to spend. See Exhibit 5-7. Note, though, that (real) median income stopped its continuous rise during the inflation-ridden 1970s. Since then it has gone through periods of both upswings and decreases, but the changes in recent years have not been as great as they were a few decades ago.

Exhibit 5-7
Median Family Income over Time (in 1999 dollars)

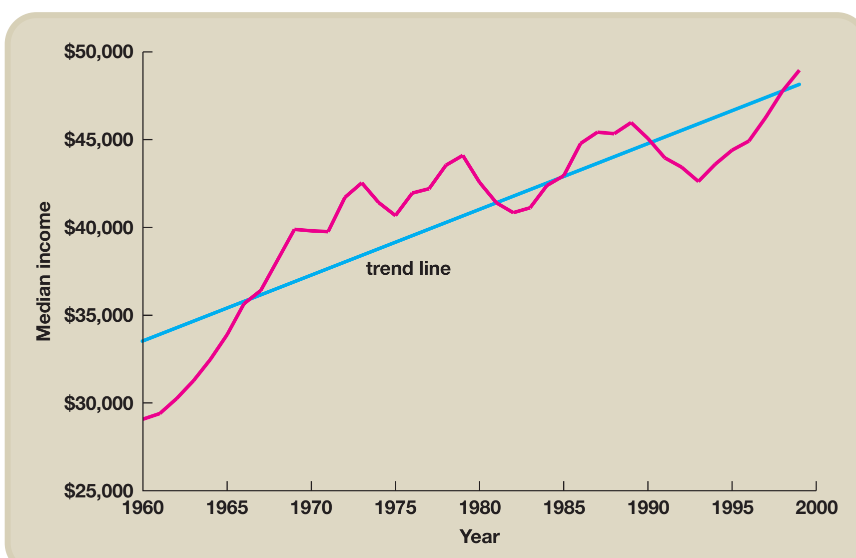
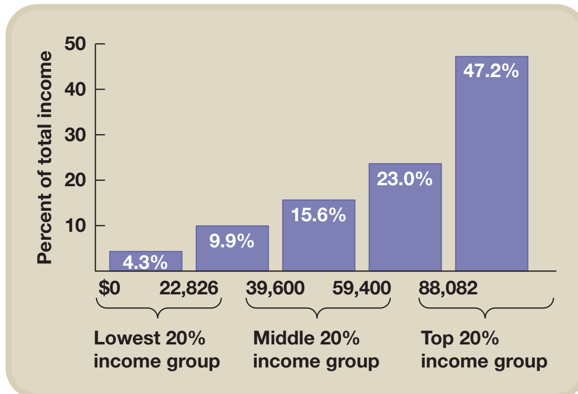


Exhibit 5-8
Percent of Total Income Going to Different Income Groups in 1999



There is heated debate about what will happen to consumer incomes—and income distribution—in the future. Some business analysts feel that the lack of significant income growth signals worse things to come. They think that a decline in the manufacturing sector of the economy threatens America's middle-class standard of living. These analysts argue that in industries with traditionally high wages, firms are replacing workers with technology—to be able to compete with low-cost foreign producers. At the same time, new jobs are coming from growth of the lower-paying service industries. But other analysts are not so pessimistic. They agree that the percentage of the workforce earning middle-income wages has declined recently—but they think this is a temporary shift, not a long-term trend, and that over time the efficiencies that come from new information technologies will "lift" the whole economy.

What happens to income levels will be critical to you—and to American consumers in general. It is easy for both consumers and marketing managers to be lulled by the promise of a constantly increasing standard of living. Both consumer thinking—and marketing strategy—will have to adjust if growth does not resume.

The higher-income groups receive a big share

Higher-income groups in the U.S. receive a very large share of total income, as you can see in Exhibit 5-8, which divides all families into five equal-sized groups—from lowest income to highest. Note that although the median income of U.S. families in 1999 was about $48,950, the top 20 percent of the families—those with incomes over $88,082—received over 47 percent of the total income. This gave them extra buying power, especially for luxury items like cellular phones, memberships in country clubs, and yachts. Well-to-do families with incomes over $155,040—the top 5 percent nationally—got more than 20 percent of the total income.

At the lower end of the scale, over 14 million families had less than $22,826 income. They account for 20 percent of all families but receive only 4.3 percent of total income. Even this low-income group is an attractive market for some basic commodities, especially food and clothing—even though almost half of them live below the poverty level of $17,029 for a family of four. These consumers may receive food stamps, medicare, and public housing, which increases their buying power. Some marketers target this group, usually with a lower-price marketing mix.

How much income is "enough?"

We can't stress the importance of income distribution too much. Many companies make serious marketing strategy errors by overestimating the amount of income in various target markets. Marketers can easily make such errors because of the natural tendency for people to associate with others like themselves—and to assume that almost everyone lives like they do. A marketing manager who earns $125,000 a year may have no clue what life is like for a family that lives on $25,000 a year.

The 1999 median family income of about $48,950 is a useful reference point because some college graduates start near this level. And a young working couple together can easily go way over this figure. This may seem like a lot of money at first—but it is surprising how soon needs and expenses rise and adjust to available income. America's middle-income consumers have been hit hard by the spiraling costs of health care, housing, energy, cars, taxes, and tuition bills. More than ever, these consumers look for purchases that offer good value for the money spent. Some high-living marketers may not understand that these consumers *need* to pinch their pennies, but that practical reality now explains much of the buying behavior of lower and middle-income markets in the U.S.[17]

Can low-income consumers protect themselves?

In market-directed economies, consumers are free to make choices in the marketplace. But with little income, education, or opportunity to become informed, many consumers in the lowest income groups have few real choices. Some marketing managers struggle over whether to serve these markets. A credit company, for example, may find customers willing to pay a high finance charge to borrow money. And the high rate may be needed to cover the risk of unpaid loans. But is it exploitation to charge a higher rate to those who can least afford it and who really have no other choice?[18]

Spending Varies with Income and Other Demographic Dimensions

We've been using the term *family income* because consumer budget studies show that most consumers spend their incomes as part of family or household units. They usually pool their incomes when planning major expenditures. So, most of our discussion will concern how families or households spend their income.

Disposable income is what you get to spend

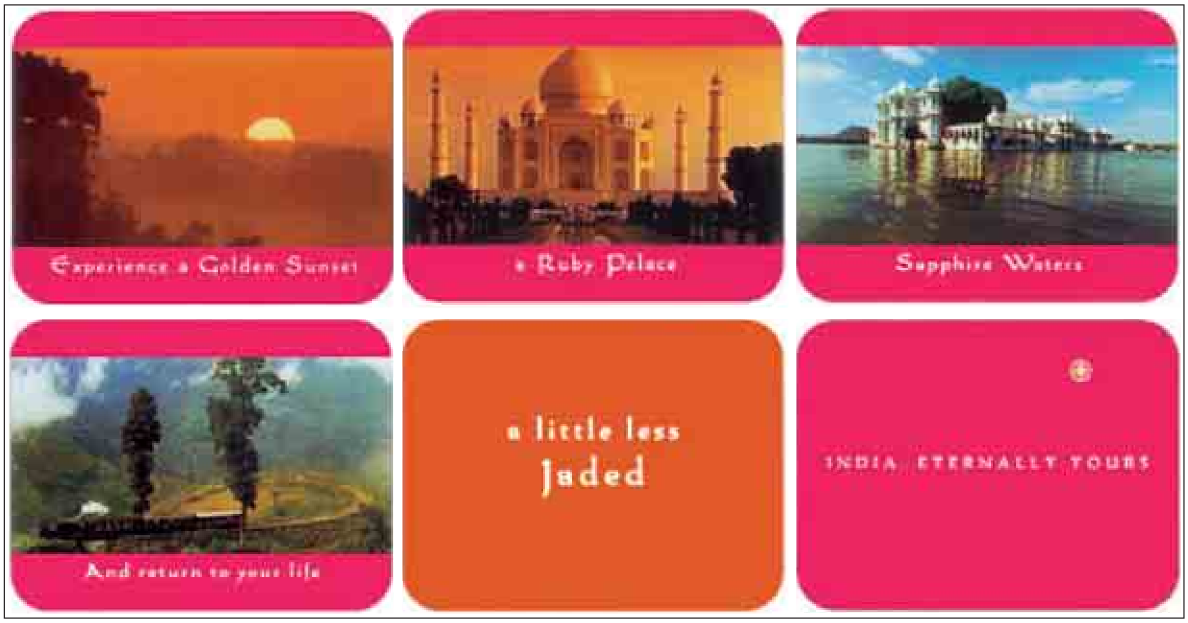
Families don't get to spend all of their income. **Disposable income** is what is left after taxes. Out of this disposable income—together with gifts, pensions, cash savings, or other assets—the family makes its expenditures. Some families don't spend all their disposable income—they save part of it. Therefore, when trying to estimate potential sales in target markets, we should distinguish among income, disposable income, and what consumers actually spend.

Discretionary income is elusive

Most families spend a good portion of their income on such "necessities" as food, rent or house payments, car and home furnishings payments, and insurance. A family's purchase of "luxuries" comes from **discretionary income**—what is left of disposable income after paying for necessities.

Discretionary income is an elusive concept because the definition of necessities varies from family to family and over time. It depends on what they think is necessary for their lifestyle. A cable TV service might be purchased out of discretionary income by a lower-income family but be considered a necessity by a higher-income family. But if many people in a lower-income neighborhood subscribe to cable TV, it might become a "necessity" for the others—and severely reduce the discretionary income available for other purchases.

The majority of U.S. families do not have enough discretionary income to afford the lifestyles they see on TV and in other mass media. On the other hand, some young adults and older people without family responsibilities have a lot of discretionary income. They may be especially attractive markets for electronic gear, digital



Purchases of luxuries, like overseas tourist travel, come from discretionary income.

cameras, new cars, foreign travel, cell phone services, and various kinds of recreation—tennis, skiing, boating, concerts, and fine restaurants.[19]

Spending varies over the family life cycle

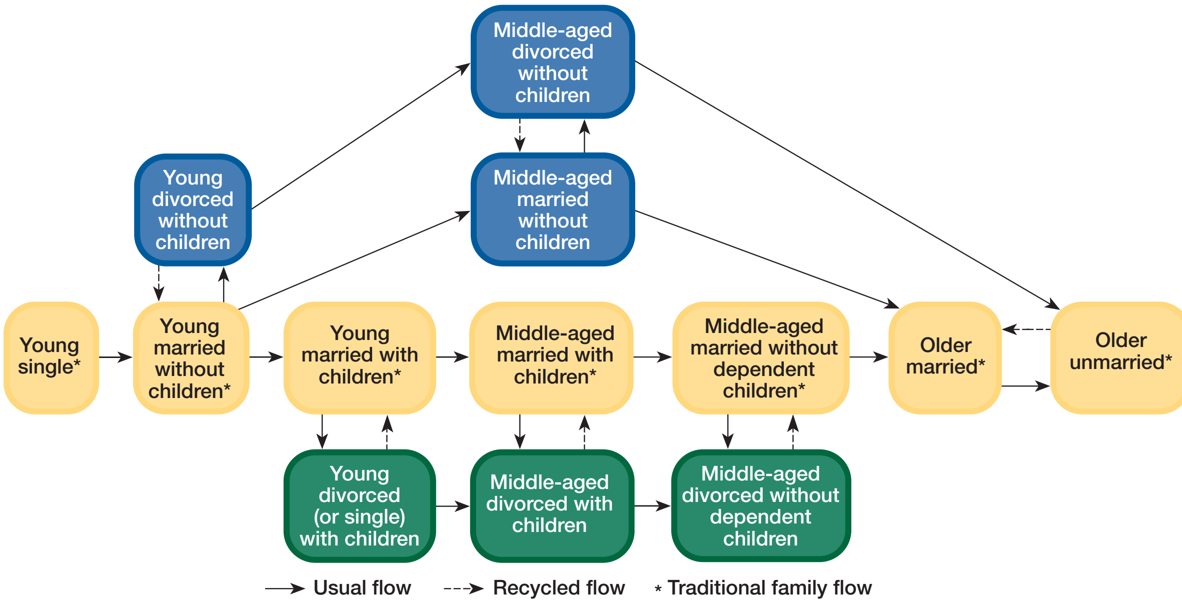
Income has a direct bearing on spending patterns, but many other demographic dimensions are also useful in understanding consumer buying. Marital status, age, and the age of any children in the family have an especially important effect on how people spend their income. Put together, these dimensions tell us about the life-cycle stage of a family. Exhibit 5-9 shows a summary of stages in the family life cycle. In our discussion, we will focus on the traditional flow from one stage to the next—as shown in the middle of the diagram. However, as shown at the top and bottom of the exhibit, divorce does interrupt the flow for many people; after a divorce, they may recycle through earlier stages.[20]

Young people and families accept new ideas

Singles and young couples seem to be more willing to try new products and brands—and they are careful, price-conscious shoppers. Younger people often earn less than older consumers, but they spend a greater proportion of their income on discretionary items because they don't have the major expenses of home ownership, education, and family rearing. Although many young people are waiting longer to marry, most do tie the knot eventually. These younger families—especially those with no children—are still accumulating durable goods, such as automobiles and home furnishings. They spend less on food. Only as children arrive and grow does family spending shift to soft goods and services, such as education, medical, and personal care. This usually happens when the family head reaches the 35–44 age group. To meet expenses, people in this age group often make more purchases on credit, and they save less of their income.

Divorce—increasingly a fact of American life—disrupts the family life-cycle pattern. Divorced parents don't spend like other singles. The mother usually has custody of the children, and the father may pay child support. The mother and children typically have much less income than two-parent families. Such families spend a larger percent of their income on housing, child care, and other necessities—with

Exhibit 5-9 Stages in Modern Family Life Cycles



little left for discretionary purchases. If a single parent remarries, the family life cycle may start over again.[21]

Reallocation for teenagers

Once children become teenagers, further shifts in spending occur. Teenagers eat more, want to wear expensive clothes, and develop recreation and education needs that are hard on the family budget. The parents—or, increasingly the single parent—may be forced to reallocate expenditures to cover these expenses—spending less on durable goods, such as appliances, automobiles, household goods, and housing. The fast-rising expense of sending a son or daughter to college can create a major financial crisis.

For many firms, teens are an important and attractive market. The amount of money involved may surprise you. America's teens currently spend over $150 billion a year and spending is growing at double-digit rates. Further, in today's families with a single parent or with two wage earners, teens play an increasingly important role in shopping and shaping family purchases. With teens spending more money, they are a target for many firms. For example, Siemens added an MP3 player to its wireless phone to help it win teen preference away from Nokia. Similarly, MasterCard is targeting teens with its credit card promotions and Bausch & Lomb's contact-lens sales hit record levels when the firm refocused its marketing efforts on teens.[22]

Selling to the empty nesters

Another important category is the **empty nesters**—people whose children are grown and who are now able to spend their money in other ways. Usually these people are in the 50–64 age group. But this is an elusive group because some people marry later and are still raising a family at this age. And in recent years lots of empty nesters have been surprised when adult singles move back in to avoid the big costs of housing.

Empty nesters are an attractive market for many items. They have paid for their homes, and the big expenses of raising a family are behind them. They are more interested in travel, small sports cars, and other things they couldn't afford before.

Much depends on their income, of course. But this is a high-income period for many workers—especially white-collar workers.[23]

Senior citizens are a big market

Finally, marketers should not neglect the **senior citizens**—people over 65. The number of people over 65 is increasing rapidly because of modern medicine, improved sanitary conditions, and better nutrition. This group now makes up almost 13 percent of the population.

Our senior citizens are more prosperous than ever before. Their income is lower than in their peak earning years, but most do have money to spend. They don't just squeak by on Social Security. Such prosperity is a dramatic change. In 1960, about a third of all senior citizens had incomes below the poverty level. Now, only about 10 percent are considered "poor"—lower than the 11.8 percent figure for all adults.

Older people also have very different needs. Many firms already cater to senior citizens—and more will be serving this market. For example, some companies developed housing and "life care" centers designed to appeal to older people. Casio makes a calculator with large, easy-to-read numbers. Publix Super Markets, a big Florida chain, trains employees to cater to older customers. Checkout clerks, for example, give older customers two light bags instead of one heavier one. Some travel agents find that senior citizens are an eager market for expensive tours and cruises. Other companies offer diet supplements and drug products—often in special easy-to-open packages. And senior citizen discounts at drugstores are more than just a courtesy—the elderly make up the biggest market for medicines.

Keep in mind, however, that older people are not all the same. With a group this large, generalities and stereotypes can be dangerous. Different senior citizen target markets have different needs—and require different marketing strategies.[24]

Ethnic Dimensions of the U.S. Market

Do ethnic groups buy differently?

America may be called the melting pot, but ethnic groups deserve special attention when analyzing markets. One basic reason is that people from different ethnic groups may be influenced by very different cultural variables. They may have quite different needs and their own ways of thinking. Moreover, Americans are beginning to recognize the value of multicultural diversity. The U.S. is becoming a multicultural market. As a result, rather than disappearing in a melting pot, some important cultural and ethnic dimensions are being preserved and highlighted. This creates both opportunities and challenges for marketers.

Some important ethnic differences are obvious. For example, more than 1 out of 10 families in the U.S. speaks a language other than English at home. Some areas have a much higher rate. In Miami and San Antonio, for example, about one out of three families speaks Spanish. This obviously affects promotion planning. Similarly, brand preferences vary for some ethnic groups. For example, cosmetic companies offer products tailored to different skin tones. But, ethnic groups don't just differ in the color of their skin. Differences in attitudes, experiences, and values, as well as where they shop and what advertising appeals they attend to, come together to shape differences in buying behavior.

Internet

Internet Exercise Visit the website for Ethnic Grocer (www.ethnicgrocer.com), select "Shop by Country," and then "Mexico." Are any of the carbonated beverages listed for Mexico likely to become popular in the U.S.? Why or why not?

Many firms are developing new strategies to appeal to fast-growing ethnic markets in the U.S. For example, this Spanish-language ad promotes Suavitel fabric softener, which has a special fragrance that appeals to many Hispanic-American consumers.

Stereotypes are common—and misleading

A marketer needs to study ethnic dimensions very carefully because they can be subtle and fast-changing. This is also an area where stereotyped thinking is the most common—and misleading. Many firms make the mistake of treating all consumers in a particular ethnic group as homogeneous. For example, some marketing managers treat all 35 million African-American consumers as "the black market," ignoring the great variability among African-American households on other segmenting dimensions. Income variability is a good example. While the median income of black families is still lower than for the whole population, that is changing. Today 51 percent of black couples have an income of at least $50,000—and 23 percent have an income of $75,000 or more. These affluent consumers are also a relatively youthful market and a larger percentage (compared with white consumers) are in earlier stages of the life cycle and therefore a better market for certain products—especially durable goods like cars, furniture, home appliances, and electronic equipment.

Ethnic markets are becoming more important

More marketers pay attention to ethnic groups now because the number of ethnic consumers is growing at a much faster rate than the overall society. Much of this growth results from immigration. In addition, however, the median age of Asian Americans, African Americans, and Hispanics is much lower than that of whites—and the birthrate is higher.

In combination, these factors have a dramatic effect. The Hispanic population in the U.S., now over 35 million and about 12.5 percent of the total population, surged by more than 60 percent since 1990. To put this in perspective, there are now more Hispanics in the U.S. than there are Canadians in Canada and more Hispanics in the U.S. than African Americans, previously the largest minority group. Hispanics are on average 10 years younger than the overall population, which helps to explain why one out of every five babies born in the U.S. is Hispanic. You can see why strong Hispanic influences among the youth culture will be even greater in the years ahead.

While there are fewer Asian Americans (about 11.6 million, or 3.6 percent of the total population), the number has tripled since 1980—one of the fastest growth rates for any segment of the population. These shifts are changing the face of the

American market. Already, more than 36 percent of American children are African American, Hispanic, or Asian. Longer term, whites are expected to become a minority by 2050.

The buying power of ethnic submarkets is also increasing rapidly. Estimates suggest that African American consumers now spend about $543 billion a year, Hispanics more than $383 billion a year, and Asian Americans more than $250 billion a year. It's also important to marketers that much of this buying power is concentrated in certain cities and states. For example, half of all Hispanics in the U.S. live in California and Texas, and another fourth live in New York, Florida, Arizona, and New Jersey. Over 20 percent of San Francisco's residents are Asians.

Strategy changes may be needed

Companies may need separate strategies for these ethnically or racially defined markets. Many of these strategies may require only changes in Place and Promotion. But sometimes companies have more difficulty developing strategies and segmenting ethnic submarkets. For example, Asian Americans emigrated from China, Japan, the Philippines, India, Korea, Vietnam, Laos, and Cambodia. Many come from very different backgrounds with no common language, religion, or culture. That adds to the marketing challenge; it means marketers must really understand the basic needs that motivate specific target markets to think and act as they do. This is important with any consumer market—regardless of people's ethnic or racial background or where in the world they live. We'll deal with that important issue in more detail in the next chapter.[25]

Conclusion

In this chapter, we studied population, income, and other demographic dimensions of consumer markets. Getting the facts straight on how about 6 billion people are spread over the world is important to marketing managers. We learned that the potential of a given market cannot be determined by population figures alone. Geographic location, income, stage in life cycle, ethnic background, and other factors are important too. We talked about some of the ways these dimensions—and changes in them—affect marketing strategy planning.

We also noted the growth of urban areas in countries around the world. The high concentration of population and spending power in large metropolitan areas of the U.S. has already made them attractive target markets. However, competition in these markets is often tough.

One of the outstanding characteristics of U.S. consumers is their mobility. Managers must pay attention to changes in markets. High mobility makes even relatively new data suspect. Data can only aid a manager's judgment—not replace it.

U.S. consumers are among the most affluent in the world. They have more discretionary income and can afford a wide variety of products that people in other parts of the world view as luxuries. However, in the U.S., as in most other societies, income is distributed unevenly among different groups. Consumers at the top income levels have a disproportionately large share of the total buying power.

The kind of data discussed in this chapter can be very useful for estimating the market potential within possible target markets. But, unfortunately, it is not very helpful in explaining specific customer behavior—why people buy *specific* products and *specific* brands. Yet such detailed forecasts are important to marketing managers. Better forecasts can come from a better understanding of consumer behavior—the subject of the next chapter.

Questions and Problems

1. Drawing on data in Exhibit 5-2, do you think that Romania would be an attractive market for a firm that produces home appliances? What about Finland? Discuss your reasons.
2. Discuss the value of gross national product and gross national product per capita as measures of market potential in international consumer markets. Refer to specific data in your answer.

3. Discuss how the worldwide trend toward urbanization is affecting opportunities for international marketing.
4. Discuss how slower population growth will affect businesses in your local community.
5. Discuss the impact of the new teen cycle on marketing strategy planning in the U.S.
6. Name three specific examples of firms that developed a marketing mix to appeal to senior citizens. Name three examples of firms that developed a marketing mix to appeal to teenagers.
7. Some demographic characteristics are more important than others in determining market potential. For each of the following characteristics, identify two products for which this characteristic is *most* important: *(a)* size of geographic area, *(b)* population, *(c)* income, *(d)* stage of life cycle.
8. Name three specific examples (specific products or brands—not just product categories) and explain how demand in the U.S. will differ by geographic location *and* urban–rural location.
9. Explain how the continuing mobility of U.S. consumers—as well as the development of big metropolitan areas—should affect marketing strategy planning in the future. Be sure to consider the impact on the four Ps.
10. Explain why the concept of the Metropolitan Statistical Area was developed. Is it the most useful breakdown for retailers?
11. Explain why mobile consumers can be an attractive market.
12. Explain how the redistribution of income in the U.S. has affected marketing planning thus far—and its likely impact in the future.
13. Why are marketing managers paying more attention to ethnic dimensions of consumer markets in the U.S.?
14. Name three categories of products marketed in the U.S. that are influenced by Hispanic culture.

Suggested Cases

8. Sophia's Ristorante
10. O'Keefe's Ice Arena
30. Deluxe Foods, Ltd.

Computer-Aided Problem

5. **Demographic Analysis**

Stylco, Inc., is a producer of specialty clothing. To differentiate its designs and appeal to its African American target market, Stylco uses authentic African prints. Originally, it just focused on designs targeted at adults in the 35–44 age range. However, in the late 1990s, when sales to these middle-aged adults started to level off, Stylco added a more conservative line of clothes for older consumers. Most buyers of the conservative styles are in the 45–59 age group.

Stylco has focused on distributing its products through select fashion boutiques in metropolitan market areas with the highest concentrations of African American consumers. This approach has reduced Stylco's personal selling expense; as a result, however, only a percentage of the total black population is served by current Stylco retailers. For example, about half of the consumers in the 35–44 age group are in the market areas served by Stylco retailers.

Naomi Davis, Stylco's marketing manager, recently read an article about the "graying of America." She is wondering how shifts in the age distribution might affect her market and sales.

To get a long-run view of these trends, she looked at census data on black consumers by age group. She also looked up estimates of the expected percent rate of change in the size of each group through the year 2005. By multiplying these rates by the size her target markets were in 2000, she can estimate how large they are likely to be in the year 2005. Further, from analysis of past sales data, she knows that the number of units the firm sells is directly proportional to the size of each age group. Specifically, the ratio of units sold to target market size has been about 5 units per 1,000 people (that is, a ratio of .005). Finally, she determined the firm's average unit profit for each of the lines. To see how changes in population are likely to affect Stylco units sold and future profits from each line, Davis programmed all of these data, and the relationships discussed above, into a spreadsheet.

a. *Briefly compare the profit data for 2000 and estimated profit for 2005 as it appears on the initial spreadsheet. What is the basic reason for the expected shift? What are the implications of these and other data in the spreadsheet for Stylco's marketing strategy planning?*

b. *The rate of growth or decline for different age groups tends to vary from one geographic region to another. Davis thinks that in the market areas that Stylco serves the size of the 35–44 age group may decrease by as much as 10 to 12 percent by 2005. However, the Census Bureau estimates that the decline of the black 35–44 age group for the whole country will only be about −1.7 percent. If the decline in the target market size for Davis' market areas turns out to be −1.7 percent rather than the −10.1 she has assumed, what is the potential effect on profits from the young adult line? On overall profits?*

c. *Because more firms are paying attention to fast-growing ethnic markets, Davis thinks competition may increase in lines targeted at affluent African Americans in the 45–59 age group. Because of price competition, the line targeted at this group already earns a lower average profit per unit. Further, as more firms compete for this business, she thinks that her "ratio of units sold to market size" may decrease. Use the what-if analysis to prepare a table showing how percent of profit from this group, as well as total profit, might change as the ratio of units sold to market size varies between a minimum of .001 and a maximum of .010. Explain the implications to the firm.*

For additional questions related to this problem, see Exercise 5-4 in the *Learning Aid for Use with Basic Marketing*, 14th edition.

When You Finish This Chapter, You Should

1. Understand the economic-buyer model of buyer behavior.

2. Understand how psychological variables affect an individual's buying behavior.

3. Understand how social influences affect an individual's and household's buying behavior.

4. See why the purchase situation has an effect on consumer behavior.

5. Know how consumers use problem-solving processes.

6. Have some feel for how a consumer handles all the behavioral variables and incoming stimuli.

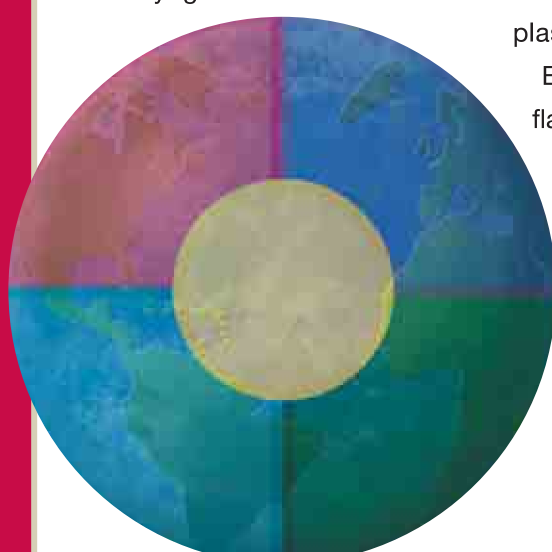
7. Understand the important new terms (shown in red).

Chapter Six

Behavioral Dimensions of the Consumer Market

In the 1970s, yogurt was a popular food in Europe but for the most part unknown in the U.S. culture. Most American consumers were not aware of it, had never tried it, and didn't know if they would like it. All of that changed when Dannon and other firms began to promote and distribute yogurt in the U.S. Sales grew slowly at first, but that changed in the 1980s as more adults became interested in healthy eating. For lots of on-the-go workers, yogurt was an economical lunch that tasted good and saved time. It didn't require preparation or clean up, and it could be eaten almost anywhere. All you needed was a plastic spoon.

By the 1990s, many brands and flavors of yogurt were on the market. Most consumers couldn't tell the difference between brands. When it was time to buy, they just picked up their routine brand or perhaps whatever was on sale. Most marketers felt that growth



place

price

promotion

produc

in the yogurt category was pretty much tapped out. But by carefully studying consumer behavior, Ian Friendly and others on his marketing team at Yoplait changed all of that. Their marketing plan for a new product, Go-Gurt, racked up $100 million in sales in the first year. Much of that represented new demand in the yogurt category because the percentage of kids eating yogurt doubled. That was no accident. They created Go-Gurt to have kid appeal.

Kids need nutritious food, but research showed that what they want in snacks is great taste, convenience, and fun. Traditional yogurt was convenient, but it still took one hand for the spoon and one to hold the carton. And a carton of yogurt didn't exactly impress the other kids as a cool thing to eat. Go-Gurt took care of that. It did away with the spoon by putting the yogurt in a 9-inch-long, one-handed squeeze tube. The creaminess of the product was adjusted to make it just right for on-the-go eating. Kids didn't have a very positive attitude about most standard yogurt flavors, so the foil-embossed Go-Gurt tube was filled with flavors kids could learn to love—like Strawberry Splash and Watermelon Meltdown.

Go-Gurt's introductory ads were placed on media like Nickelodeon so they'd reach kids directly. Then it was up to them to ask their parents to buy Go-Gurt at the store. The ads positioned Go-Gurt not just as a food but as a lifestyle accessory for kids. To build awareness of the benefits of

place price promotion product

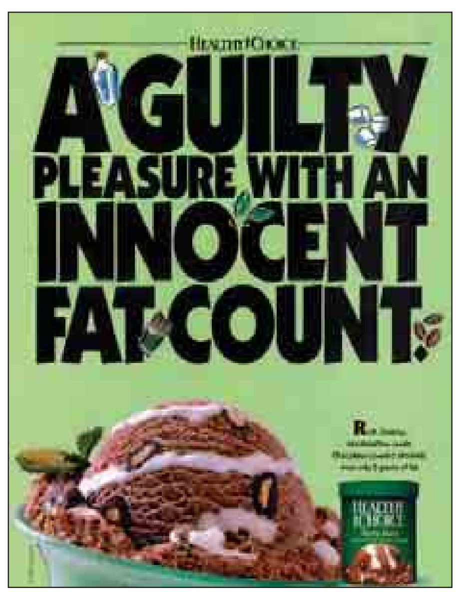
the package and interest in the product, the ads conveyed the idea that it was OK to play with your food. For example, in one spot, a young skateboarder holding a Go-Gurt blasts past another kid who looks bored eating from a carton of yogurt as the announcer asks, "Why eat yogurt like this when you can eat with your hands, not a spoon? Go-Gurt comes in a totally cool squeeze tube you can squeeze and slurp, grab and glurp." The Go-Gurt slurping skateboarder tells the other boy, "Hey, lose the spoon."

To follow up on the awareness and interest generated by the ads, a heavy sampling program played a crucial role in building product trial. No, the samples were not distributed at the grocery store. Kids on skateboards and scooters passed out samples from backpacks at festivals, theme parks, soccer games, and local parks.

Go-Gurt has been such a success that Yoplait has decided to give adult yogurt eaters something else to think about when they visit the yogurt aisle—four flavors of a comparable yogurt in a tube, Yoplait Expresse.[1]

Consumer Behavior—Why Do They Buy What They Buy?

In the last chapter, we discussed basic data on population, income, and consumer spending patterns. This information can help marketers predict basic *trends* in consumer spending patterns. For example, the average person in the U.S. or Canada consumes 5 times more than a Mexican person, 10 times more than a Chinese person, and 30 times more than a person from India. Unfortunately, when many firms sell similar products, demographic analysis isn't much help in predicting which specific products and brands consumers will purchase—and why. Our Go-Gurt example shows that many other variables can influence consumers and their buying behavior.



Economic needs affect many buying decisions, but for some purchases the behavioral influences on a consumer are more important.

To better understand why consumers buy as they do, many marketers turn to the behavioral sciences for help. In this chapter, we'll explore some of the thinking from economics, psychology, sociology, and the other behavioral disciplines.

Specific consumer behaviors vary a great deal for different products and from one target market to the next. In today's global markets, the variations are countless. That makes it impractical to try to catalog all the detailed possibilities for every different market situation. For example, how and why a given consumer buys a specific brand of cookies may be very different from how that same consumer buys a bicycle; and different customers in different parts of the world may have very different reactions to either product. But there are *general* behavioral principles—frameworks—that marketing managers can apply to learn more about their specific target markets. Our approach focuses on developing your skill in working with these frameworks.

The Behavioral Sciences Help You Understand the Buying Process

Economic needs affect most buying decisions

Most economists assume that consumers are **economic buyers**—people who know all the facts and logically compare choices in terms of cost and value received to get the greatest satisfaction from spending their time and money. A logical extension of the economic-buyer theory led us to look at consumer income patterns. This approach is valuable because consumers must at least have income to be in a market. Further, most consumers don't have enough income to buy everything they want; that's why economics is sometimes called the "dismal science."

This view assumes that economic needs guide most consumer behavior. **Economic needs** are concerned with making the best use of a consumer's time and money—as the consumer judges it. Some consumers look for the lowest price. Others will pay extra for convenience. And others may weigh price and quality for the best value. Some economic needs are:

1. Economy of purchase or use.
2. Convenience.
3. Efficiency in operation or use.
4. Dependability in use.
5. Improvement of earnings.

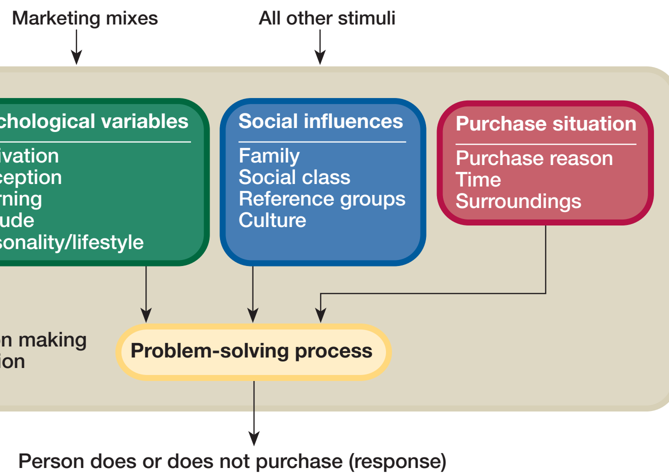
Clearly, marketing managers must be alert to new ways to appeal to economic needs. Most consumers appreciate firms that offer them improved value for the money they spend. But improved value does not just mean offering lower and lower prices. Many consumers face a "poverty of time." Carefully planned Place decisions can make it easier and faster for customers to make a purchase. Products can be designed to work better, require less service, or last longer. Promotion can inform consumers about their choices or explain product benefits in terms of measurable factors like operating costs, the length of the guarantee, or the time a product will save.

The economic value that a purchase offers a customer is an important factor in many purchase decisions. But most marketing managers think that buyer behavior is not as simple as the economic-buyer model suggests. A product that one person sees as a good value—and is eager to buy—is of no interest to someone else. So we can't expect to understand buying behavior without taking a broader view.

How we will view consumer behavior

Many behavioral dimensions influence consumers. Let's try to combine these dimensions into a model of how consumers make decisions. Exhibit 6-1 shows that psychological variables, social influences, and the purchase situation all affect a

Exhibit 6-1
A Model of Buyer Behavior



person's buying behavior. We'll discuss these topics in the next few pages. Then we'll expand the model to include the consumer problem-solving process.

Psychological Influences within an Individual

Here we will discuss some variables of special interest to marketers—including motivation, perception, learning, attitudes, and lifestyle. Much of what we know about these *psychological (intrapersonal) variables* draws from ideas originally developed in the field of psychology.

Needs motivate consumers

Everybody is motivated by needs and wants. **Needs** are the basic forces that motivate a person to do something. Some needs involve a person's physical well-being, others the individual's self-view and relationship with others. Needs are more basic than wants. **Wants** are "needs" that are learned during a person's life. For example, everyone needs water or some kind of liquid, but some people also have learned to want Clearly Canadian's raspberry-flavored sparkling water on the rocks.

When a need is not satisfied, it may lead to a drive. The need for liquid, for example, leads to a thirst drive. A **drive** is a strong stimulus that encourages action to reduce a need. Drives are internal—they are the reasons behind certain behavior patterns. In marketing, a product purchase results from a drive to satisfy some need.

Some critics imply that marketers can somehow manipulate consumers to buy products against their will. But marketing managers can't create internal drives. Most marketing managers realize that trying to get consumers to act against their will is a waste of time. Instead, a good marketing manager studies what consumer drives, needs, and wants already exist and how they can be satisfied better.

Consumers seek benefits to meet needs

We're all a bundle of needs and wants. Exhibit 6-2 lists some important needs that might motivate a person to some action. This list, of course, is not complete. But thinking about such needs can help you see what *benefits* consumers might seek from a marketing mix.

When a marketing manager defines a product-market, the needs may be quite specific. For example, the food need might be as specific as wanting a thick-crust pepperoni pizza—delivered to your door hot and ready to eat.

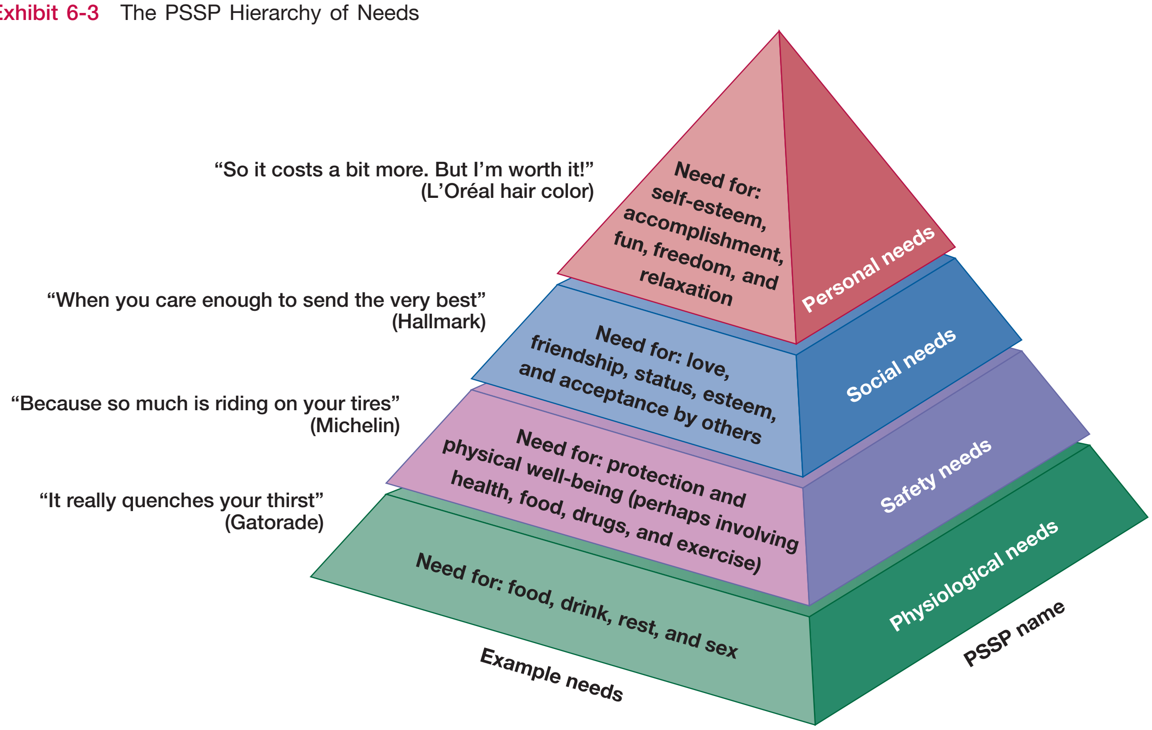
Exhibit 6-2 Possible Needs Motivating a Person to Some Action

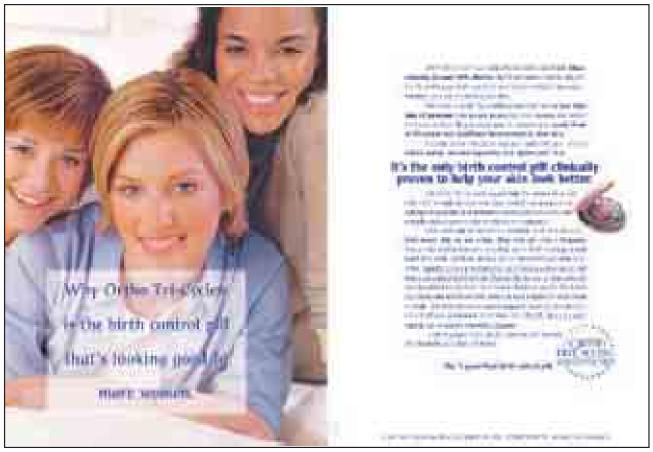
Types of Needs	Specific Examples			
Physiological needs	Hunger Sex Rest	Thirst Body elimination	Activity Self-preservation	Sleep Warmth/coolness
Psychological needs	Aggression Family preservation Nurturing Playing-relaxing Self-identification	Curiosity Imitation Order Power Tenderness	Being responsible Independence Personal fulfillment Pride	Dominance Love Playing-competition Self-expression
Desire for . . .	Acceptance Affiliation Comfort Esteem Knowledge Respect Status	Achievement Appreciation Leisure Fame Prestige Retaliation Sympathy	Acquisition Beauty Distance—"space" Happiness Pleasure Self-satisfaction Variety	Affection Companionship Distinctiveness Identification Recognition Sociability Fun
Freedom from . . .	Fear Pain Harm	Depression Stress Ridicule	Discomfort Loss Sadness	Anxiety Illness Pressure

Several needs at the same time

Some psychologists argue that a person may have several reasons for buying—at the same time. Maslow is well known for his five-level hierarchy of needs. We will discuss a similar four-level hierarchy that is easier to apply to consumer behavior. Exhibit 6-3 illustrates the four levels along with an advertising slogan showing how a company has tried to appeal to each need. The lowest-level needs are physiological. Then come safety, social, and personal needs. As a study aid, think of the PSSP needs.[2]

Exhibit 6-3 The PSSP Hierarchy of Needs





Some products fill more than one need at the same time.

Physiological needs are concerned with biological needs—food, drink, rest, and sex. **Safety needs** are concerned with protection and physical well-being (perhaps involving health, food, medicine, and exercise). **Social needs** are concerned with love, friendship, status, and esteem—things that involve a person's interaction with others. **Personal needs,** on the other hand, are concerned with an individual's need for personal satisfaction—unrelated to what others think or do. Examples include self-esteem, accomplishment, fun, freedom, and relaxation.

Motivation theory suggests that we never reach a state of complete satisfaction. As soon as we get our lower-level needs reasonably satisfied, those at higher levels become more dominant. This explains why marketing efforts targeted at affluent consumers in advanced economies often focus on higher-level needs. It also explains why these approaches may be useless in parts of the world where consumers' basic needs are not being met.

It is important to see, however, that a particular product may satisfy more than one need at the same time. In fact, most consumers try to fill a *set* of needs rather than just one need or another in sequence.

Obviously marketers should try to satisfy different needs. Yet discovering these specific consumer needs may require careful analysis. Consider, for example, the lowly vegetable peeler. Marketing managers for OXO International realized that many people, especially young children and senior citizens, have trouble gripping the handle of a typical peeler. OXO redesigned the peeler with a bigger handle that addressed this physical need. OXO also coated the handle with dishwasher-safe rubber. This makes cleanup more convenient—and the sharp peeler is safer to use when the grip is wet. The attractively designed grip also appeals to consumers who get personal satisfaction from cooking and who want to impress their guests. Even though OXO priced the peeler much higher than most kitchen utensils, it has sold very well because it appeals to people with a variety of needs.[3]

Perception determines what consumers see and feel

Consumers select varying ways to meet their needs sometimes because of differences in **perception**—how we gather and interpret information from the world around us.

We are constantly bombarded by stimuli—ads, products, stores—yet we may not hear or see anything. This is because we apply the following selective processes:

1. **Selective exposure**—our eyes and minds seek out and notice only information that interests us.
2. **Selective perception**—we screen out or modify ideas, messages, and information that conflict with previously learned attitudes and beliefs.

How consumers perceive a product or marketing communication may depend on consumer interest and the urgency of the need.

3. **Selective retention**—we remember only what we want to remember.

These selective processes help explain why some people are not affected by some advertising—even offensive advertising. They just don't see or remember it! Even if they do, they may dismiss it immediately. Some consumers are skeptical about any advertising message.

Our needs affect these selective processes. And current needs receive more attention. For example, Goodyear tire retailers advertise some sale in the newspaper almost weekly. Most of the time we don't even notice these ads—until we need new tires. Only then do we tune in to Goodyear's ads.

Marketers are interested in these selective processes because they affect how target consumers get and retain information. This is also why marketers are interested in how consumers *learn*.

Learning determines what response is likely

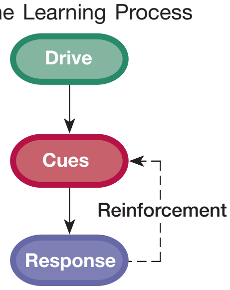
Learning is a change in a person's thought processes caused by prior experience. Learning is often based on direct experience: A little girl tastes her first cone of Ben & Jerry's Concession Obsession flavor ice cream, and learning occurs! Learning may also be based on indirect experience or associations. If you watch an ad that shows other people enjoying Ben & Jerry's Chocolate Fudge Brownie low-fat frozen yogurt, you might conclude that you'd like it too.

Consumer learning may result from things that marketers do, or it may result from stimuli that have nothing to do with marketing. Either way, almost all consumer behavior is learned.[4]

Experts describe a number of steps in the learning process. We've already discussed the idea of a drive as a strong stimulus that encourages action. Depending on the **cues**—products, signs, ads, and other stimuli in the environment—an individual chooses some specific response. A **response** is an effort to satisfy a drive. The specific response chosen depends on the cues and the person's past experience.

Reinforcement of the learning process occurs when the response is followed by satisfaction—that is, reduction in the drive. Reinforcement strengthens the relationship between the cue and the response. And it may lead to a similar response the next time the drive occurs. Repeated reinforcement leads to development of a habit—making the individual's decision process routine. Exhibit 6-4 shows the relationships of the important variables in the learning process.

Exhibit 6-4
The Learning Process



The learning process can be illustrated by a thirsty person. The thirst *drive* could be satisfied in a variety of ways. But if the person happened to walk past a vending machine and saw a Mountain Dew sign—a *cue*—then he might satisfy the drive with a *response*—buying a Mountain Dew. If the experience is satisfactory, positive *reinforcement* will occur, and our friend may be quicker to satisfy this drive in the same way in the future. This emphasizes the importance of developing good products that live up to the promises of the firm's advertising. People can learn to like or dislike Mountain Dew—reinforcement and learning work both ways. Unless marketers satisfy their customers, they must constantly try to attract new ones to replace the dissatisfied ones who don't come back.

Good experiences can lead to positive attitudes about a firm's product. Bad experiences can lead to negative attitudes that even good promotion won't be able to change. In fact, the subject of attitudes, an extremely important one to marketers, is discussed more fully in a later section.

Positive cues help a marketing mix

Sometimes marketers try to identify cues or images that have positive associations from some other situation and relate them to their marketing mix. Many people associate the smell of lemons with a fresh, natural cleanliness. So companies often add lemon scent to household cleaning products—Clorox bleach and Pledge furniture polish, for example—because it has these associations. Similarly, firms like Calvin Klein use ads suggesting that people who use their products have more appeal to the opposite sex. And some shampoos and deodorants are formulated to be clear and packaged in clear bottles because some consumers associate that look with being natural and pure.

Many needs are culturally learned

Many needs are culturally (or socially) learned. The need for food, for instance, may lead to many specific food wants. Many Japanese enjoy sushi (raw fish), and their children learn to like it. Fewer Americans, however, have learned to enjoy it.

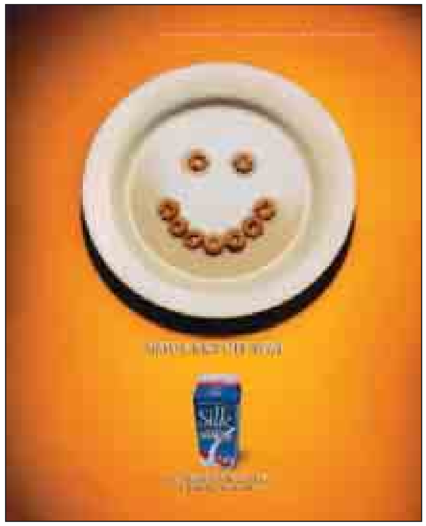
Some critics argue that marketing efforts encourage people to spend money on learned wants totally unrelated to any basic need. For example, Europeans are less concerned about perspiration, and many don't buy or use antiperspirants. Yet Americans spend millions of dollars on such products. Advertising says that using Ban deodorant "takes the worry out of being close." But is marketing activity the cause of the difference in the two cultures? Most research says that advertising can't convince buyers of something contrary to their basic attitudes.

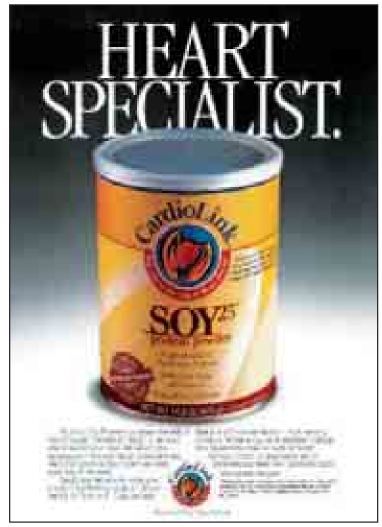
Attitudes relate to buying

An **attitude** is a person's point of view toward something. The "something" may be a product, an advertisement, a salesperson, a firm, or an idea. Attitudes are an important topic for marketers because attitudes affect the selective processes, learning, and eventually the buying decisions people make.

Because attitudes are usually thought of as involving liking or disliking, they have some action implications. Beliefs are not so action-oriented. A **belief** is a person's opinion about something. Beliefs may help shape a consumer's attitudes but don't necessarily involve any liking or disliking. It is possible to have a belief—say, that Listerine has a medicinal taste—without really caring what it tastes like. On the other hand, beliefs about a product may have a positive or negative effect in shaping consumers' attitudes. For example, a person with allergies is unlikely to switch to a new medicine like Claritin unless she believes it will be more effective than what she used in the past.

In an attempt to relate attitude more closely to purchase behavior, some marketers stretched the attitude concept to include consumer "preferences" or "intention to buy." Managers who must forecast how much of their brand customers





Companies that sell soy-based products are developing new marketing mixes to help overcome negative attitudes that some consumers have about the taste of soy. For example, White Wave Silk is now packaged like milk and promotion focuses on the health benefits. In the same vein, CardioLink's name and trade ads help position its soy powder as healthy for the heart.

will buy are particularly interested in the intention to buy. Forecasts would be easier if attitudes were good predictors of intentions to buy. Unfortunately, the relationships usually are not that simple. A person may have positive attitudes toward Jacuzzi whirlpool bathtubs but no intention of buying one.

Try to understand attitudes and beliefs

Research on consumer attitudes and beliefs can sometimes help a marketing manager get a better picture of markets. For example, consumers with very positive attitudes toward a new product idea might provide a good opportunity—especially if they have negative attitudes about competitors' offerings. Or they may have beliefs that would discourage them from buying a product.

Marketing managers for Purina Dog Chow faced this challenge. Research showed that one segment of consumers thought that Purina was a great dog food, but they didn't buy it all of the time. They believed that their dogs would get bored with it. After all, people don't like eating the same thing all of the time. But dogs are not people. Vets have found dogs benefit from a good, consistent diet. So, Purina developed an ad campaign to convince these dog owners that what they believed was not true. Each ad gives a dog's-eye-view reaction to being fed a different dog food. In one ad, after taking a few bites, the dog looks into the camera with a pained expression and walks away. He returns with a packet of antacid, which he drops in his water bowl. Advertising research and sales results both showed that the soft-sell ad hit the bull's-eye in convincing occasional customers that switching foods was not good. Many bought Purina more regularly, and Dog Chow sales increased by $36 million. Consumer beliefs—right or wrong—can have a significant impact on whether a strategy succeeds.[5]

Most marketers work with existing attitudes

Purina's efforts were successful in changing beliefs. But marketers generally try to understand the attitudes of their potential customers and work with them. We'll discuss this idea again when we review the way consumers evaluate product alternatives. For now, we want to emphasize that it's more economical to work with consumer attitudes than to try to change them. Attitudes tend to be enduring. Changing present attitudes—especially negative ones—is sometimes necessary. But that's probably the most difficult job marketers face.[6]

Marketing managers for new Olay Cleansing Cloths (and other Olay skin care products) wanted to take advantage of the familiar Oil of Olay brand name, but realized that many consumers didn't have a positive association between "oil" and beauty. So, the brand name was updated to just Olay and the logo of a woman's figure was changed slightly to appeal to younger women.

Ethical issues may arise

Part of the marketing job is to inform and persuade consumers about a firm's offering. An ethical issue sometimes arises, however, if consumers have *inaccurate* beliefs. For example, many consumers are confused about what foods are really healthy. Marketers for a number of food companies have been criticized for packaging and promotion that take advantage of inaccurate consumer perceptions about the meaning of the words *lite* or *low-fat*. A firm's lite donuts may have less fat or fewer calories than its other donuts—but that doesn't mean that the donut is *low* in fat or calories. Similarly, promotion of a "children's cold formula" may play off parents' fears that adult medicines are too strong—even though the basic ingredients in the children's formula are the same and only the dosage is different. And when Tiger Woods' happy smile appears in the American Express ad it's easy to forget that he's paid for his endorsement.

Marketers must also be careful about promotion that might encourage false beliefs, even if the advertising is not explicitly misleading. For example, ads for Ultra Slim-Fast low-fat beverage don't claim that anyone who buys the product will lose all the weight they want or look like the slim models who appear in the ads—but some critics argue that the advertising gives that impression.[7]

Meeting expectations is important

Attitudes and beliefs sometimes combine to form an **expectation**—an outcome or event that a person anticipates or looks forward to. Consumer expectations often focus on the benefits or value that the consumer expects from a firm's marketing mix. This is an important issue for marketers because a consumer is likely to be dissatisfied if his or her expectations are not met. For example, when Dryel home dry cleaning kits were introduced, ads portrayed Dryel as an alternative to expensive dry-cleaner services. Many consumers who tried it were disappointed because it failed to get out some stains and clothing still needed to be pressed.[8]

A key point here is that consumers may evaluate a product not just on how well it performs, but on how it performs *relative to their expectations*. A product that otherwise might get high marks from a satisfied consumer may be a disappointment if there's a gap between what the consumer gets and what the consumer expects. Promotion that overpromises what the rest of the marketing mix can really deliver leads to problems in this area. Finding the right balance, however, can be difficult. Consider the challenge faced by marketing managers for Van Heusen shirts. A few years ago Van Heusen came up with a new way to treat its shirts so that they look better when they come out of the wash than previous

Would You Like Those Peanuts with Sugar and Cream?

Marketing managers for Planters' peanuts wanted a new package that would keep peanuts fresh. They also wanted the package to be a cue to promote freshness to consumers. They thought that they had the right idea when they put Planters Fresh Roast Salted Peanuts in a vacuum-packed bric-pac, like the ones that coffee comes in. They were confident that when consumers saw the vacuum-packed peanuts it would remind them that they were fresh roasted, just like with fresh-roasted coffee. To reinforce that message, Planters put the words "Fresh Roast" in large print on the front of the package—right under the Planters name and over the words "salted peanuts." The familiar Mr. Peanut trademark character was there too. He looked dapper with his top hat and cane pointing toward the words "Fresh Roast." This all seemed like a good idea, but it didn't work as planned.

One problem was that the peanuts weren't the same size and shape as coffee, so the bags were pretty lumpy. That made the words harder to read on supermarket shelves. Also, the bags were supposed to be resealable. But that didn't work well because of the lumps. So, once the bag was opened, the peanuts got stale. Consumers who expected extra freshness were disappointed. But, other shoppers had a bigger surprise before they even left the store.

Some consumers opened the bag and put the contents into the grocery store's coffee grinder. You can imagine the gooey peanut butter mess that made. You can also imagine that the store manager was not happy with Planters. Were the consumers trying to make peanut butter? No. Everything on the bag made it clear that it was peanuts. However, the link of the bag with coffee was so strong that consumers didn't stop to think about it. Moreover, the new package came out at about the same time that flavored coffees were just becoming popular. Hey, if some ad is telling you to try hazelnut-flavored coffee, why not peanut-flavored coffee too? No, Planters doesn't want to compete with Starbucks, so this package is off the market.[9]

www.mhhe.com/fourps

wash-and-wear shirts. Van Heusen promotes these shirts as "wrinkle-free" and the label shows an iron stuffed in a garbage can. Most people agree that the new shirt is an improvement. Even so, consumers who buy a shirt expecting it to look as crisp as if it had just been ironed are disappointed. For them, the improvement is not enough.[10]

Personality affects how people see things

Many researchers study how personality affects people's behavior, but the results have generally been disappointing to marketers. A trait like neatness can be associated with users of certain types of products—like cleaning materials. But marketing managers have not found a way to use personality in marketing strategy planning.[11] As a result, they've stopped focusing on personality measures borrowed from psychologists and instead developed lifestyle analysis.

Psychographics focus on activities, interests, and opinions

Psychographics or **lifestyle analysis** is the analysis of a person's day-to-day pattern of living as expressed in that person's Activities, Interests, and Opinions—sometimes referred to as AIOs. Exhibit 6-5 shows a number of variables for each of the AIO dimensions—along with some demographics used to add detail to the lifestyle profile of a target market.

Lifestyle analysis assumes that marketers can plan more effective strategies if they know more about their target markets. Understanding the lifestyle of target customers has been especially helpful in providing ideas for advertising themes. Let's see how it adds to a typical demographic description. It may not help Mercury marketing managers much to know that an average member of the target market for a Mountaineer SUV is 34.8 years old, married, lives in a three-bedroom home, and has 2.3 children. Lifestyles help marketers paint a more human portrait of the target market. For example, lifestyle analysis might show that the 34.8-year-old is also a community-oriented consumer with traditional values who especially enjoys spectator sports and spends much time in other family activities. An ad might show the Mountaineer being used by a happy family at a ball game so the target market could really identify with the ad. And the ad might be placed on an ESPN show whose viewers match the target lifestyle profile.[12]

Exhibit 6-5 Lifestyle Dimensions (and some related demographic dimensions)

Dimension	Examples		
Activities	Work Hobbies Social events	Vacation Entertainment Club membership	Surfing Web Shopping Sports
Interests	Family Home Job	Community Recreation Fashion	Food Media Achievements
Opinions	Themselves Social issues Politics	Business Economics Education	Products Future Culture
Demographics	Income Age Family life cycle	Geographic area Ethnicity Dwelling	Occupation Family size Education

Marketing managers for consumer products firms who are interested in learning more about the lifestyle of a target market sometimes turn to outside specialists for help. For example, SRI Consulting, a research firm, offers a service called geoVALS (VALS is an abbreviation for values, attitudes, and lifestyles). GeoVALS uses psychographics to show where customers live and why they behave as they do; it is especially useful for targeting direct-mail ad campaigns. With another service, VALS 2, SRI describes a firm's target market in terms of a set of typical VALS lifestyle groups (segments). An advantage of this approach is that SRI has developed very detailed information about the various VALS groups. For example, the VALS approach has been used to profile consumers in the United Kingdom, Germany, Japan, and Canada as well as the United States. However, the disadvantage of VALS 2—and other similar approaches—is that it may not be very specific to the marketing manager's target market.[13]

Internet

Internet Exercise Go to the SRI Internet site (http://future.sri.com), click on VALS, and then click on "To the Survey" to review the VALS questionnaire. If you wish, complete the short questionnaire online. SRI will provide you with your VALS profile.

1965

1972

The original Betty, 1936 **1980** **1986** **Betty Crocker 2000**

General Mills has changed "Betty Crocker's" appearance as consumer attitudes and lifestyles have changed. The face of the newest Betty Crocker reflects her multicultural background.

Social Influences Affect Consumer Behavior

We've been discussing some of the ways needs, attitudes, and other psychological variables influence the buying process. Now we'll see that these variables—and the buying process—are usually affected by relations with other people too. We'll look at how the individual interacts with family, social class, and other groups who may have influence.

Who is the real decision maker in family purchases?

Relationships with other family members influence many aspects of consumer behavior. We saw specific examples of this in Chapter 5 when we considered the effects of the family life cycle on family spending patterns. Family members may also share many attitudes and values, consider each other's opinions, and divide various buying tasks. In years past, most marketers in the United States targeted the wife as the family purchasing agent. Now, with sex-role stereotypes changed and with night and weekend shopping more popular, men and older children may take more responsibility for shopping and decision making. In other countries, family roles vary. For example, in Norway women still do most of the family shopping.

Although only one family member may go to the store and make a specific purchase, when planning marketing strategy it's important to know who else may be involved. Other family members may have influenced the decision or really decided what to buy. Still others may use the product.

You don't have to watch much Saturday morning TV to see that Kellogg's knows this. Cartoon characters like Tony the Tiger tell kids about the goodies found in certain cereal packages and urge them to remind Dad or Mom to pick up that brand at the store. Similarly, the box for Post's Oreo O's cereal looks like the wrapper on the cookies, to get kid's attention in the store. Kids also influence grown-up purchases—to the tune of $250 billion a year. Surveys show that kids often have a big say in a family's choice of products such as apparel, cars, vacations, electronics, and health and beauty aids.

Family considerations may overwhelm personal ones

A husband and wife may jointly agree on many important purchases, but sometimes they may have strong personal preferences. However, such individual preferences may change if the other spouse has different priorities. One might want to take a family vacation to Disneyland—when the other wants a new Sony DVD player and large-screen TV. The actual outcome in such a situation is unpredictable. The preferences of one spouse might change because of affection for the other or because of the other's power and influence.

Buying responsibility and influence vary greatly depending on the product and the family. A marketer trying to plan a strategy will find it helpful to research the specific target market. Remember, many buying decisions are made jointly, and thinking only about who actually buys the product can misdirect the marketing strategy.[14]

Social class affects attitudes, values, and buying

Up to now, we've been concerned with individuals and their family relationships. Now let's consider how society looks at an individual and perhaps the family—in terms of social class. A **social class** is a group of people who have approximately equal social position as viewed by others in the society.

Almost every society has some social class structure. In most countries social class is closely related to a person's occupation, but it may also be influenced by education,

Exhibit 6-6 Characteristics and Relative Sizes of Different Social Class Groups in the United States

Relative size	Group	Description
1.5%	**Upper-class**	People from old wealthy families (the upper-upper) as well as socially prominent new rich (lower-upper), such as top professionals and corporate executives. These people have high discretionary income, often have second homes, and are a good market for antiques, art, rare jewelry, luxury travel, and unique designer products.
12.5%	**Upper-middle class**	Successful professionals, owners of small businesses, or managers of large corporations. They want quality products that are symbols of their success. They are community minded and want to be socially acceptable. They are ambitious for their children and more "future oriented" than the lower-class groups.
32%	**Lower-middle class***	Small-businesspeople, office workers, teachers, and technicians—the white-collar workers. They are in the "average" income group and try to save something for the future. The American moral code and emphasis on hard work come from this class. This is the most "conforming" segment of society. They are home- and family-oriented.
38%	**Upper-lower ("working") class***	The blue-collar workers—factory workers, skilled laborers, and service people. Most earn good incomes (especially in two-career families) but are still very concerned about security. They are less confident in their own judgments about products and may rely more on salespeople and advertising. They often feel controlled by the world around them.
16%	**Lower-lower class**	Unskilled laborers and people in very low-status occupations. These people usually don't have much income but are good markets for necessities and products that help them enjoy the present. At the lowest end of this group are people without steady employment and people who live in severe poverty. Many of America's illiterate are in this group.

* Note: in combination, these groups form America's "mass market."

community participation, where a person lives, income, possessions, social skills, and other factors—including what family a person is born into. Because of such differences, people in different social classes tend to have different beliefs and feelings.

In most countries—including the United States—there is *some* general relationship between income level and social class. But the income level of people within the same social class can vary greatly, and people with the same income level may be in different social classes. So income by itself is usually not a good measure of social class. And people in different social classes may spend, save, and borrow money in very different ways. For example, spending for clothing, housing, home furnishings, and leisure activities, as well as choices of where and how to shop, often vary with social class.

The U.S. class system is far less rigid than those in most countries. Children start out in the same social class as their parents—but they can move to a different social class depending on their educational levels or the jobs they hold. By contrast, India's social structure is much more rigid, and individuals can't easily move up in the class system.

Marketers want to know what buyers in various social classes are like. In the United States, simple approaches for measuring social class groupings are based on a person's *occupation, education,* and *type and location of housing.* By using marketing research surveys or available census data, marketers can get a feel for the social class of a target market. Exhibit 6-6 illustrates a multilevel social class structure for the United States. Note the relative sizes of the groupings.

Although the exhibit uses traditional technical terms like *upper, middle,* and *lower,* a word of warning is in order. These terms may seem to imply "superior" and

Reference group influence is usually more important when others will be able to see which product a consumer is using, but Jockey wants young people to view its underwear as in fashion and encourages them to "Let 'em know you're Jockey."

"inferior." But in sociological and marketing usage, no value judgment is intended. We cannot say that any one class is "better" or "happier" than another.

What do these classes mean?

Social class studies suggest that the old saying "A rich man is simply a poor man with more money" is not true. Given the same income as middle-class consumers, people belonging to the lower class handle themselves and their money very differently. Many people think of America as a middle-class society. In fact, when asked to classify themselves, most people just say that they're middle class or working class. But in many marketing situations the social class groups are more distinct than that suggests. Various classes shop at different stores. They prefer different treatment from salespeople. They buy different brands of products—even though prices are about the same. And they have different spending–saving attitudes.

Reference groups are relevant too

A **reference group** is the people to whom an individual looks when forming attitudes about a particular topic. People normally have several reference groups for different topics. Some they meet face-to-face. Others they just wish to imitate. In either case, they may take values from these reference groups and make buying decisions based on what the group might accept.

We're always making comparisons between ourselves and others. So reference groups are more important when others will be able to "see" which product or brand we're using. Influence is stronger for products that relate to status in the group. For one group, owning an expensive fur coat may be a sign of "having arrived." A group of animal lovers might view it as a sign of bad judgment. In either case, a consumer's decision to buy or not buy a fur coat might depend on the opinions of others in that consumer's reference group.[15]

Reaching the opinion leaders who are buyers

An **opinion leader** is a person who influences others. Opinion leaders aren't necessarily wealthier or better educated. And opinion leaders on one subject aren't necessarily opinion leaders on another. For example, you may have a friend who is ahead of the curve in knowing about computer products, but you might not want that friend's opinion about new clothing styles and cosmetics. On the other hand, sometimes a leader in one area earns respect in another. For example, George Foreman, former heavyweight champion of the world, has become a household name representing his line of Foreman grills. Each

social class and age group tends to have its own opinion leaders. Some marketing mixes aim especially at these people since their opinions affect others and research shows that they are involved in many product-related discussions with "followers." Favorable word-of-mouth publicity from opinion leaders can really help a marketing mix. But the opposite is also true. If opinion leaders aren't satisfied, they're likely to talk about it and influence others.[16]

Culture surrounds the other influences

Culture is the whole set of beliefs, attitudes, and ways of doing things of a reasonably homogeneous set of people. In Chapters 4 and 5, we looked at the broad impact of culture.

We can think of the American culture, the French culture, or the Latin American culture. People within these cultural groupings tend to be more similar in outlook and behavior. But sometimes it is useful to think of subcultures within such groupings. For example, within the American culture, there are various religious and ethnic subcultures; also different cultural forces tend to prevail in different regions of the country.

Failure to consider cultural differences, even subtle ones, can result in problems. To promote their product and get people to try it, marketers for Pepto-Bismol often provide free samples at festivals and street fairs. Their idea is that people tend to overindulge at such events. However, when they distributed sample packets at a festival in San Francisco's Chinatown, they insulted many of the people they wanted to influence. Booths with Chinese delicacies lined the streets, and many of the participants interpreted the sample packets (which featured the word "Nauseous" in large letters) as suggesting that Chinese delicacies were nauseating. The possibility of this misinterpretation may seem obvious in hindsight, but if it had been that obvious in advance the whole promotion would have been handled differently.[17]

Culture varies in international markets

Planning strategies that consider cultural differences in international markets can be even harder—and such cultures usually vary more. Each foreign market may need to be treated as a separate market with its own submarkets. Ignoring cultural differences—or assuming that they are not important—almost guarantees failure in international markets.

For example, Japanese consumers tend to snap up the latest gadgets, but only about 7 percent of Japanese households have a dishwasher (compared to about 50 percent in the U.S.). Appliance manufacturers who have tried to export their standard models to Japan have met with failure. One reason is that Japanese kitchens are much too small for units that are standard in the U.S. Another problem is that fermented soybeans and other common Japanese foods tend to be very sticky. A standard dishwasher won't clean the dishes well. To address these cultural differences, manufacturers have developed small countertop machines with powerful jets to do the cleaning. But another obstacle remains. Many traditional Japanese feel that it is the woman's duty to wash the dishes. For many housewives, the guilt of having dishes done by a machine is worse than the aggravation of doing the job. Foreign firms seem to have missed that. But it became more obvious when Matsushita, the Japanese firm whose washers lead the market, got increases in sales by focusing its promotion on conservation of hot water and hygiene—rather than convenience—as the important reasons to buy a dishwasher.[18]

From a target marketing point of view, a marketing manager probably wants to aim at people within one culture or subculture. A firm developing strategies for two cultures often needs two different marketing plans.[19]

The attitudes and beliefs that we usually associate with culture tend to change slowly. Consider something as unemotional as a cup of tea. For a long time, tea has been a basic part of British culture. Taking a break for a cup of hot tea is tradition—a social moment with friends. In striking contrast, few British consumers ever drink iced tea. Lipton, Nestea, and other iced-tea makers would like to change that. They look at the 330 million gallons of iced tea routinely purchased by Americans each year and ask, "Why not in Britain?" But they face tough odds—and it's not just the cooler weather in England. Consumers there associate iced tea with the dregs left in the bottom of the teapot after it's cooled off. It's not an appealing image, and it isn't likely to change quickly. Iced-tea sales won't pick up until it does.[20]

Because cultural forces tend to change slowly, marketers can often get good help from someone who already has a good understanding of the culture of the target customers. This helps to avoid problems. Then the marketers should be able to focus on the more dynamic variables discussed above.

Individuals Are Affected by the Purchase Situation

Needs, benefits sought, attitudes, motivation, and even how a consumer selects certain products all vary depending on the purchase situation. So different purchase situations may require different marketing mixes—even when the same target market is involved. Let's briefly consider some of the ways that the purchase situation can vary.

Purchase reason can vary

Why a consumer makes a purchase can affect buying behavior. For example, a student buying a pen to take notes might pick up an inexpensive Bic. But the same student might choose a Cross pen as a gift for a friend.

Time affects what happens

Time influences a purchase situation. *When* consumers make a purchase—and the time they have available for shopping—will influence their behavior. A leisurely dinner or socializing with friends at a Starbucks induces different behavior than grabbing a quick cup of 7-Eleven coffee on the way to work.

The urgency of the need is another time-related factor. A sports buff who needs a VCR in time for the Super Bowl—that evening—might spend an hour driving across town in heavy traffic to get the right unit. In a different circumstance, the same person might order the VCR online from a website and figure that the extra time for it to be shipped is well worth the money saved.

The nature of the purchase situation and the problem-solving processes that consumers use are typically different when they are shopping on the Internet rather than at a store.

On the other hand, how long something takes may be relative. Our online shopper might be frustrated by a web page that takes two minutes to load and abandon his virtual shopping cart after the VCR is already selected. This happens all of the time online. On the other hand, you don't often see a consumer walk away from a shopping cart because of a two-minute wait in a checkout line at a store.

Surroundings affect buying too

Surroundings can affect buying behavior. The excitement at an auction may stimulate impulse buying. Checking out an auction online might lead to a different response.

Surroundings may discourage buying too. For example, some people don't like to stand in a checkout line where others can see what they're buying—even if the other shoppers are complete strangers.[21]

Consumers Use Problem-Solving Processes

The variables discussed affect *what* products a consumer finally decides to purchase. Marketing managers also need to understand *how* buyers use a problem-solving process to select particular products.

Most consumers seem to use the following five-step problem-solving process:

1. Becoming aware of—or interested in—the problem.
2. Recalling and gathering information about possible solutions.
3. Evaluating alternative solutions—perhaps trying some out.
4. Deciding on the appropriate solution.
5. Evaluating the decision.[22]

Exhibit 6-7 presents an expanded version of the buyer behavior model shown in Exhibit 6-1. Note that this exhibit integrates the problem-solving process with the whole set of variables we've been reviewing.

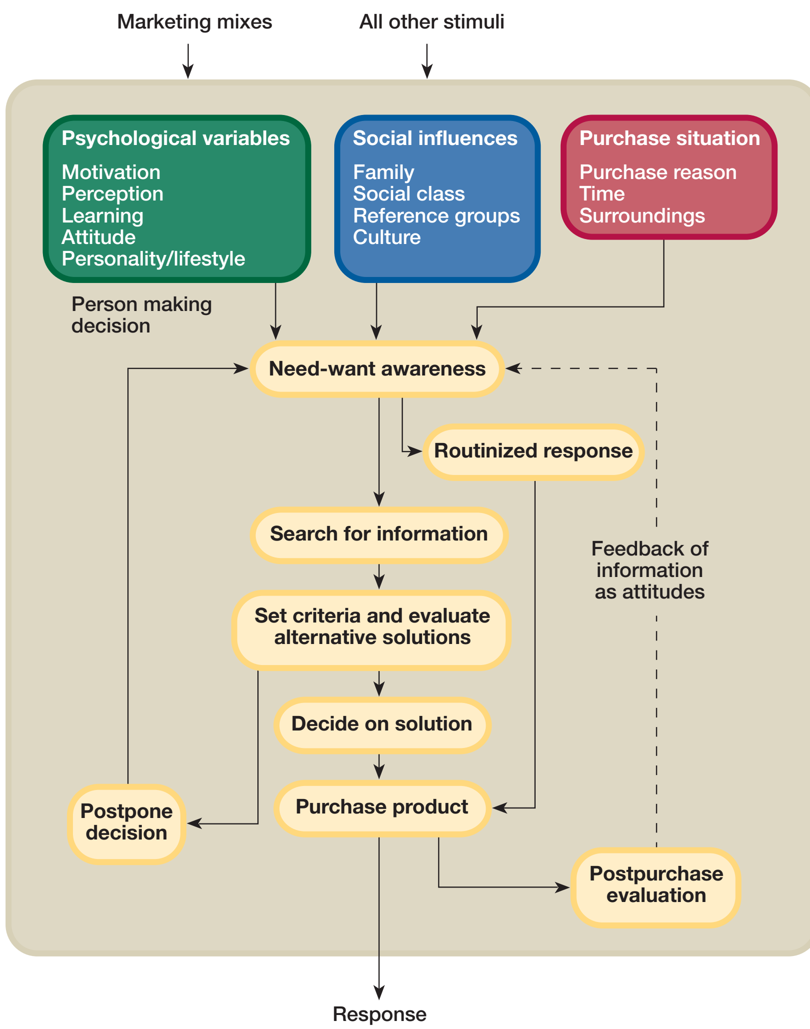
When consumers evaluate information about purchase alternatives, they may weigh not only a product type in relation to other types of products but also differences in brands within a product type *and* the stores where the products may be available. This can be a very complicated evaluation procedure, and, depending on their choice of criteria, consumers may make seemingly irrational decisions. If convenient service is crucial, for example, a buyer might pay list price for an unexciting car from a very convenient dealer. Marketers need a way to analyze these decisions.

Grid of evaluative criteria helps

On the basis of studies of how consumers seek out and evaluate product information, researchers suggest that marketing managers use an evaluative grid showing features common to different products (or marketing mixes). For example, Exhibit 6-8 shows some of the features common to three different cars a consumer might consider.

The grid encourages marketing managers to view each product as a bundle of features or attributes. The pluses and minuses in Exhibit 6-8 indicate one consumer's attitude toward each feature of each car. If members of the target market don't rate a feature of the marketing manager's brand with pluses, it may indicate a problem. The manager might want to change the product to improve that feature or perhaps use more promotion to emphasize an already acceptable feature. The consumer in Exhibit 6-8 has a minus under gas mileage for the Nissan. If the Nissan really gets better gas mileage than the other cars, promotion might focus on mileage to improve consumer attitudes toward this feature and toward the whole product.

Exhibit 6-7
An Expanded Model of the Consumer Problem-Solving Process



Some consumers will reject a product if they see *one* feature as substandard—regardless of how favorably they regard the product's other features. The consumer in Exhibit 6-8 might avoid the Saab, which he saw as less than satisfactory on ease of service, even if it were superior in all other aspects. In other instances, a consumer's overall attitude toward the product might be such that a few good features could make up for some shortcomings. The comfortable interior of the Toyota (Exhibit 6-8) might make up for less exciting styling—especially if the consumer viewed comfort as really important.

Of course, most consumers don't use a grid like this. However, constructing such a grid helps managers think about what evaluative criteria target consumers consider really important, what consumers' attitudes are toward their product (or marketing mix) on each criteria, and how consumers combine the criteria to reach a final decision. Having a better understanding of the process should help a manager develop a better marketing mix.[23]

Exhibit 6-8
Grid of Evaluative Criteria for Three Car Brands

Brands	Common features			
	Gas mileage	Ease of service	Comfortable interior	Styling
Nissan	$\boxed{-}$	+	+	–
Saab	+	$\boxed{-}$	+	+
Toyota	+	+	$\boxed{+}$	$\boxed{-}$

Note: Pluses and minuses indicate a consumer's evaluation of a feature for a brand.

Three levels of problem solving are useful

The basic problem-solving process shows the steps consumers may go through trying to find a way to satisfy their needs—but it doesn't show how long this process will take or how much thought a consumer will give to each step. Individuals who have had a lot of experience solving certain problems can move quickly through some of the steps or almost directly to a decision.

It is helpful, therefore, to recognize three levels of problem solving: extensive problem solving, limited problem solving, and routinized response behavior. See Exhibit 6-9. These problem-solving approaches are used for any kind of product. Consumers use **extensive problem solving** for a completely new or important need—when they put much effort into deciding how to satisfy it. For example, a music lover who wants to download music might decide to buy an MP3 player—but not have any idea what model to buy. After talking with friends to find out about their experiences with different models, she might do a search on the Internet to see if highly recommended models were still available, to get the details about features, and even to look for published product reviews. She might also compare prices listed by firms selling the players over the Internet. After thinking about her needs some more, she might want to visit a local dealer to listen to a Sony unit with an optional memory card to hold more tracks. And if she likes the sound—and the store has a good extended service guarantee at the right price—she'll buy it. This is not exactly an impulse purchase!

Consumers use **limited problem solving** when they're willing to put *some* effort into deciding the best way to satisfy a need. Limited problem solving is typical when a consumer has some previous experience in solving a problem but isn't certain which choice is best at the current time. If our music lover also wanted some new compact discs for her car CD player, she would already know what type of music she enjoys. She might go to a familiar store and evaluate what new CDs they had in stock for her favorite types of music.

Consumers use **routinized response behavior** when they regularly select a particular way of satisfying a need when it occurs. Routinized response behavior is typical when a consumer has considerable experience in how to meet a need and has no need for additional information. For example, our music lover might routinely buy the latest recording by her favorite band as soon as it's available.

Exhibit 6-9 Problem-Solving Continuum

Most marketing managers would like their target consumers to buy their products in this routinized way. Some firms provide special services for frequent buyers, encourage repeat business with discounts, or do other things to build a good relationship so that the customer purchases from them in a routinized way.

Routinized response behavior is also typical for **low-involvement purchases**—purchases that have little importance or relevance for the customer. Let's face it, buying a box of salt is probably not one of the burning issues in your life.[24]

Problem solving is a learning process

The reason problem solving becomes simpler with time is that people learn from experience—both positive and negative things. As consumers approach the problem-solving process, they bring attitudes formed by previous experiences and social training. Each new problem-solving process may then contribute to or modify this attitude set.

New concepts require an adoption process

When consumers face a really new concept, their previous experience may not be relevant. These situations involve the **adoption process**—the steps individuals go through on the way to accepting or rejecting a new idea. Although the adoption process is similar to the problem-solving process, learning plays a clearer role and promotion's contribution to a marketing mix is more visible.

In the adoption process, an individual moves through some fairly definite steps:

1. *Awareness*—the potential customer comes to know about the product but lacks details. The consumer may not even know how it works or what it will do.
2. *Interest—if* the consumer becomes interested, he or she will gather general information and facts about the product.
3. *Evaluation*—a consumer begins to give the product a mental trial, applying it to his or her personal situation.
4. *Trial*—the consumer may buy the product to experiment with it in use. A product that is either too expensive to try or isn't available for trial may never be adopted.
5. *Decision*—the consumer decides on either adoption or rejection. A satisfactory evaluation and trial may lead to adoption of the product and regular use. According to psychological learning theory, reinforcement leads to adoption.
6. *Confirmation*—the adopter continues to rethink the decision and searches for support for the decision—that is, further reinforcement.[25]

Marketers often want to make it easier for consumers to adopt a product. Colgate offers free samples to encourage consumers in Colombia to try its Protex Fresh soap bars; AOL gives away free diskettes in dozens of ways, including with newspapers.

PepsiCo had to work with the adoption process when it introduced Pepsi One, a low-calorie cola. Many consumers are interested in staying trim, but diet sodas have an image of bad taste. In light of that, Pepsi's initial ads didn't directly say that Pepsi One was a diet drink. Rather, they used the slogan "True Cola Taste. One Calorie." But that confused a lot of consumers who couldn't tell what made it different from Diet Pepsi. As a result, consumer interest was not as great as Pepsi had expected. Because awareness and interest were low among consumers, retailers didn't devote much shelf space to Pepsi One, so it often wasn't even there for a consumer to evaluate. Even after a year on the market, trial was low. To help more consumers through the adoption process, Pepsi made changes. To build awareness and interest, new ads explained that Pepsi One was using a new sweetener, recently approved by the government, which tasted better than the sweetener used in other diet drinks. The ads showed consumers drinking Pepsi One and not being able to taste the difference from a regular cola; they used the tagline "Too good to be one calorie, but it is." Pepsi also changed the packaging graphics to put more emphasis on the sweetener at the point of purchase. To generate more trial, Pepsi pushed to get Pepsi One promoted on special end-aisle displays and stepped up its sampling program with taste-testing booths on campuses, in office cafeterias, and at movie theaters. Of course, consumers will decide to regularly buy Pepsi One only if they are satisfied with the taste.[26]

Internet

Internet Exercise To make it easier for consumers to visualize how certain fashions will look, the Lands' End website (www.landsend.com) has an interactive "virtual model" feature. Go to the Lands' End website, click on "My Model," and check out this feature. Do you think that it makes it easier to evaluate a potential purchase?

Dissonance may set in after the decision

A buyer may have second thoughts after making a purchase decision. The buyer may have chosen from among several attractive alternatives—weighing the pros and cons and finally making a decision. Later doubts, however, may lead to **dissonance**—tension caused by uncertainty about the rightness of a decision. Dissonance may lead a buyer to search for additional information to confirm the wisdom of the decision and so reduce tension. Without this confirmation, the adopter might buy something else next time or not comment positively about the product to others.[27]

Several Processes Are Related and Relevant to Strategy Planning

Exhibit 6-10 shows the interrelation of the problem-solving process, the adoption process, and learning. It is important to see this interrelation and to understand that promotion can modify or accelerate it. Also note that the potential buyers' problem-solving behavior should affect how firms design their distribution systems. Similarly, customers' attitudes may determine how price sensitive they are and what price the firm should charge. Knowing how target markets handle these processes helps companies with their marketing strategy planning.

Exhibit 6-10
Relation of Problem-Solving Process, Adoption Process, and Learning (given a problem)

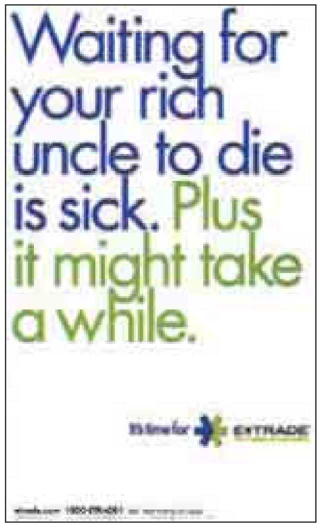
Problem-solving steps	Adoption process steps	Learning steps
1. Becoming aware of or interested in the problem	Awareness and interest	Drive
2. Gathering information about possible solutions	Interest and evaluation	Cues
3. Evaluating alternative solutions, perhaps trying some out	Evaluation, maybe trial	Reinforcement
4. Deciding on the appropriate solution	Decision	Response
5. Evaluating the decision	Confirmation	

Consumer Behavior in International Markets

All the influences interact—often in subtle ways

You're a consumer, so you probably have very good intuition about the many influences on consumer behavior that we've been discussing. For many different purchase situations you also intuitively know from experience which variables are most important. That's good, but it's also a potential trap—especially when developing marketing mixes for consumers in international markets. The less a marketing manager knows about the *specific* social and intrapersonal variables that shape the behavior of target customers, the more likely it is that relying on intuition will be misleading. We all have a tendency to try to explain things we don't understand by generalizing from what we do know. Yet when it comes to consumer behavior, many of the specifics do not generalize from one culture to another.

Cadbury's effort to develop a Japanese market for its Dairy Milk Chocolate candy bar illustrates the point. Cadbury marketing managers conducted marketing research to find out more about candy preferences among Japanese consumers. The consumers said that they didn't like the high milk-fat content of Cadbury's bar. Cadbury's managers, however, reasoned that this reaction must be from lack of opportunity to become accustomed to the candy. After all, in most other countries it's the rich taste of the candy that turns consumers into "chocoholics." When Cadbury introduced the bar in Japan, it was a real flop. Taste preferences in other countries simply didn't generalize to Japan. It also wasn't just a matter of opportunity. The whole diet in Japan is different enough that eating the candy was unpleasant. By contrast, Dannon was successful because it took similar research findings to heart and dramatically modified its yogurt dairy desserts until they satisfied Japanese tastes.



E*Trade ads often rely on humor in the U.S. and abroad. For example, this Swedish ad says, "Here is a service for all of you that inherited money. Or brains." However, because humor may not work in the same way in different cultures, E*Trade often uses locally produced ads and in some countries, like France, a more serious approach is taken.

Sometimes important influences on consumer behavior are more subtle. When P&G first introduced disposable diapers in Japan, interest was limited. Research suggested that price and health concerns were a sticking point, as was product fit. The diapers leaked because the design was too large for most Japanese babies. From the Western vantage point, these were reasonable problems to work on. However, another powerful cultural force was also at work. At that time, most Japanese mothers were expected to dedicate themselves to caring for their babies. Many women who could afford the convenience of disposable diapers felt guilty using them. Japanese firms that entered the market later used ads to emphasize that disposables were best *for the baby*. That appeal relieved the mother's guilt. Even so, it took time for basic attitudes to change.

Watch out for stereotypes, and change

Our diaper example can also serve as a reminder to watch out for oversimplifying stereotypes. Consumers in a foreign culture may be bound by some similar cultural forces, but that doesn't mean that they are all the same. Further, changes in the underlying social forces may make outdated views irrelevant.

Many Westerners believe that the typical Japanese executive works very long hours and devotes very little time to family life. That stereotype has been highlighted in the Western media. It's still partly true. Yet in today's Japan, many young Japanese executives want a more balanced family life; they don't want to continue the almost total dedication to business accepted by the previous generation. A marketer who didn't recognize this change probably wouldn't fully understand these people, their needs, or buying behavior in their families.

Developing a marketing mix that really satisfies the needs of a target market takes a real understanding of consumer behavior and the varied forces that shape it. That holds whether the target market is local or half way around the world. So when planning strategies for international markets, it's best to involve locals who have a better chance of understanding the experience, attitudes, and interests of your customers. Many companies, even very sophisticated ones, have faltered because they failed to heed that simple advice.[28]

Conclusion

In this chapter, we analyzed the individual consumer as a problem solver who is influenced by psychological variables, social influences, and the purchase situation. All of these variables are related, and our model of buyer behavior helps integrate them into one process. Marketing strategy planning requires a good grasp of this material.

Assuming that everyone behaves the way you do—or even like your family or friends do—can lead to expensive marketing errors.

Consumer buying behavior results from the consumer's efforts to satisfy needs and wants. We discussed some reasons why consumers buy and saw that consumer behavior can't be fully explained by only a list of needs.

We also saw that most societies are divided into social classes, a fact that helps explain some consumer behavior. And we discussed the impact of reference groups and opinion leaders.

We presented a buyer behavior model to help you interpret and integrate the present findings—as well as any new data you might get from marketing research. As of now, the behavioral sciences can only offer insights and theories, which the marketing manager must blend with intuition and judgment to develop marketing strategies.

Companies may have to use marketing research to answer specific questions. But if a firm has neither the money nor the time for research, then marketing managers have to rely on available descriptions of present behavior and guesstimates about future behavior. Popular magazines and leading newspapers often reflect the public's shifting attitudes. And many studies of the changing consumer are published regularly in the business and trade press. This material—coupled with the information in this book—will help your marketing strategy planning.

Remember that consumers—with all their needs and attitudes—may be elusive, but they aren't invisible. Research has provided more data and understanding of consumer behavior than business managers generally use. Applying this information may help you find your breakthrough opportunity.

Questions and Problems

1. In your own words, explain economic needs and how they relate to the economic-buyer model of consumer behavior. Give an example of a purchase you recently made that is consistent with the economic-buyer model. Give another that is not explained by the economic-buyer model. Explain your thinking.
2. Explain what is meant by a hierarchy of needs and provide examples of one or more products that enable you to satisfy each of the four levels of need.
3. Cut out (or copy) two recent advertisements: one full-page color ad from a magazine and one large display from a newspaper. In each case, indicate which needs the ads are appealing to.
4. Explain how an understanding of consumers' learning processes might affect marketing strategy planning. Give an example.
5. Briefly describe your own *beliefs* about the potential value of wearing automobile seat belts, your *attitude* toward seat belts, and your *intention* about using a seat belt the next time you're in a car.
6. Give an example of a recent purchase experience in which you were dissatisfied because a firm's marketing mix did not meet your expectations. Indicate how the purchase fell short of your expectations—and also explain whether your expectations were formed based on the firm's promotion or on something else.
7. Explain psychographics and lifestyle analysis. Explain how they might be useful for planning marketing strategies to reach college students, as opposed to average consumers.
8. A supermarket chain is planning to open a number of new stores to appeal to Hispanics in southern California. Give some examples that indicate how the four Ps might be adjusted to appeal to the Hispanic subculture.
9. How should the social class structure affect the planning of a new restaurant in a large city? How might the four Ps be adjusted?

10. What social class would you associate with each of the following phrases or items? In each case, choose one class if you can. If you can't choose one class but rather feel that several classes are equally likely, then so indicate. In those cases where you feel that all classes are equally interested or characterized by a particular item, choose all five classes.
    a. A gun rack in a pickup truck.
    b. The *National Enquirer.*
    c. *New Yorker* magazine.
    d. *Working Woman* magazine.
    e. People watching soap operas.
    f. Jaguar automobile.
    g. Men who drink beer after dinner.
    h. Families who vacation at a Disney theme park.
    i. Families who distrust banks (keep money in socks or mattresses).
    j. Owners of pit bulls.
11. Illustrate how the reference group concept may apply in practice by explaining how you personally are influenced by some reference group for some product. What are the implications of such behavior for marketing managers?
12. Give two examples of recent purchases where the specific purchase situation influenced your purchase decision. Briefly explain how your decision was affected.
13. Give an example of a recent purchase in which you used extensive problem solving. What sources of information did you use in making the decision?
14. On the basis of the data and analysis presented in Chapters 5 and 6, what kind of buying behavior would you expect to find for the following products: *(a)* a haircut, *(b)* a dishwasher detergent, *(c)* a printer for a personal computer, *(d)* a tennis racket, *(e)* a dress belt, *(f)* a telephone answering machine, *(g)* life insurance, *(h)* an ice cream cone, and *(i)* a new checking account? Set up a chart for your answer with products along the left-hand margin as the row headings and the following factors as headings for the columns: *(a)* how consumers would shop for these products, *(b)* how far they would travel to buy the product, *(c)* whether they would buy by brand, *(d)* whether they would compare with other products, and *(e)* any other factors they should consider. Insert short answers—words or phrases are satisfactory—in the various boxes. Be prepared to discuss how the answers you put in the chart would affect each product's marketing mix.
15. Review the Go-Gurt case that introduces this chapter, and identify which of the key terms (that appear in red) from the text of the chapter that you think are illustrated in the case. Write down each key term you identify and briefly explain how it is illustrated.

Suggested Cases

1. McDonald's "Seniors" Restaurant
3. Pillsbury's Häagen-Dazs
9. SleepyTime Motel
11. Runners World

Computer-Aided Problem

6. **Selective Processes**

Submag, Inc., uses direct-mail promotion to sell magazine subscriptions. Magazine publishers pay Submag $3.12 for each new subscription. Submag's costs include the expenses of printing, addressing, and mailing each direct-mail advertisement plus the cost of using a mailing list. There are many suppliers of mailing lists, and the cost and quality of different lists vary.

Submag's marketing manager, Shandra Debose, is trying to choose between two possible mailing lists. One list has been generated from phone directories. It is less expensive than the other list, but the supplier acknowledges that about 10 percent of the names are out-of-date (addresses where people have moved away.) A competing supplier offers a list of active members of professional associations. This list costs 4 cents per name more than the phone list, but only 8 percent of the addresses are out-of-date.

In addition to concerns about out-of-date names, not every consumer who receives a mailing buys a subscription. For example, *selective exposure* is a problem. Some target customers never see the offer—they just toss out junk mail without even opening the envelope. Industry studies show that this wastes about 10 percent of each mailing—although the precise percentage varies from one mailing list to another.

Selective perception influences some consumers who do open the mailing. Some are simply not interested. Others don't want to deal with a subscription service. Although the price is good, these consumers worry that they'll never get the magazines. Submag's previous experience is that selective perception causes more than half of those who read the offer to reject it.

Of those who perceive the message as intended, many are interested. But *selective retention* can be a problem. Some people set the information aside and then forget to send in the subscription order.

Submag can mail about 25,000 pieces per week. Shandra Debose has set up a spreadsheet to help her study effects of the various relationships discussed above and to choose between the two mailing lists.

a. *If you were Debose, which of the two lists would you buy based on the initial spreadsheet? Why?*
b. *For the most profitable list, what is the minimum number of items that Submag will have to mail to earn a profit of at least $3,500?*
c. *For an additional cost of $.01 per mailing, Submag can include a reply card that will reduce the percent of consumers who forget to send in an order (Percent Lost—Selective Retention) to 45 percent. If Submag mails 25,000 items, is it worth the additional cost to include the reply card? Explain your logic.*

For additional questions related to this problem, see Exercise 6-3 in the *Learning Aid for Use with Basic Marketing*, 14th edition.

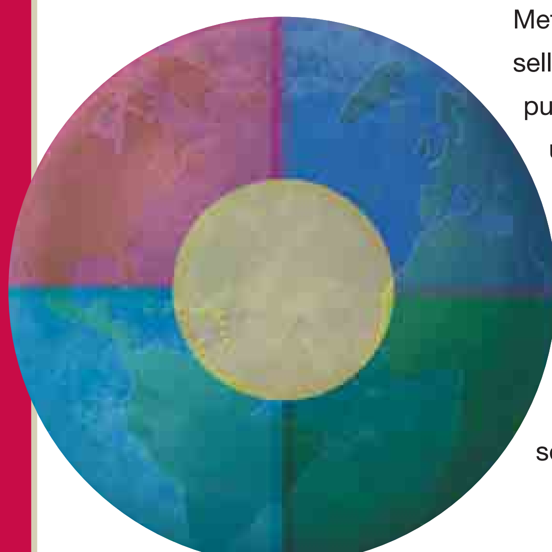
When You Finish This Chapter, You Should

1. Know who the business and organizational customers are.
2. See why multiple influence is common in business and organizational purchase decisions.
3. Understand the problem-solving behavior of organizational buyers.
4. Understand the different types of buyer–seller relationships and their benefits and limitations.
5. Know the basic e-commerce methods used in organizational buying.
6. Know about the number and distribution of manufacturers and why they are an important customer group.
7. Know how buying by service firms, retailers, wholesalers, and governments is similar to—and different from—buying by manufacturers.
8. Understand the important new terms (shown in red).

Chapter Seven

Business and Organizational Customers and Their Buying Behavior

MetoKote Corp. specializes in protective coatings, like powder-coat and liquid paint, that other manufacturers need for the parts and equipment they make. For example, when you see John Deere (JD) agricultural or construction equipment, its familiar green finish probably came from MetoKote. In fact, John Deere and MetoKote have a close buyer–seller relationship. While purchasing managers at Deere use Internet portals to identify suppliers and get competitive bids for many items they need, it's different with MetoKote. Deere isn't going to switch to some other supplier just because an Internet search identifies some cheaper



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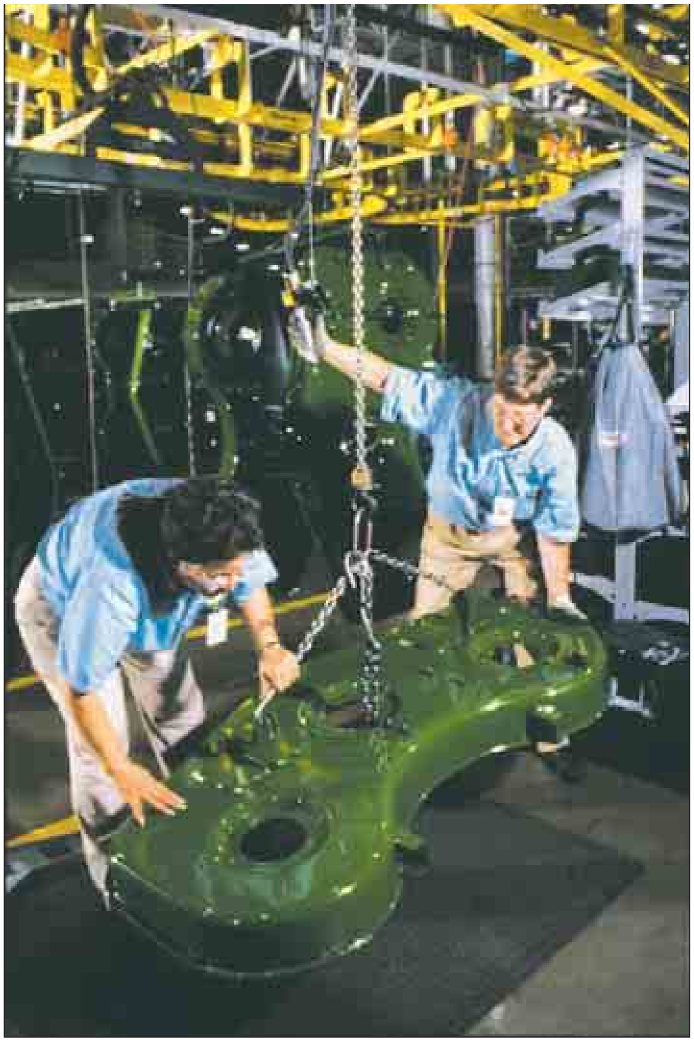


coating. MetoKote doesn't just supply Deere with coatings; it handles the whole coating job for Deere. In fact, it has built facilities right next to some Deere plants. When it's time for a part to be coated, a conveyer belt moves it out of the JD plant and into the MetoKote facility. Four hours later it's back—and it's green. The decision to purchase coating services this way wasn't made casually and many people were involved. JD's production people favored this arrangement. They let MetoKote's experts keep up with all of the environmental regulations and new technologies for coatings, so Deere can worry about what it does best. Deere's finance people liked the idea that a Deere plant could be smaller and less costly to build and maintain if it didn't need space for big spray booths. Because MetoKote does not have to ship the parts to Deere after they are coated, there are fewer scratches and dents—which the quality people like. And the purchasing people don't have to worry about parts being there when they're needed. Of course, this was not a simple sale for MetoKote—and on an ongoing basis many people cooperate and share information to make it work for both firms.

John Deere needs high-quality protective finishes because the buyers for its customers want durable, long-lasting equipment. Like Deere, they want good value from their suppliers. That means that marketers at Deere need to think about the quality of Deere service as well as the quality of Deere equipment. For example, when a huge commercial farm in California or Brazil needs a repair part they can't afford delays. Deere helps them, and the dealers who sell its parts and equipment, with information technology. At any hour an equipment customer can check Deere's website (www.deere.com) to see which dealers have a needed part in inventory, to check the price, and to place an order for fast delivery. But helping its customers earn better profits in their own operations doesn't stop there. For example, some Deere farm equipment includes global positioning devices that track exactly where the equipment goes. That makes it possible for the owner to use JD's VantagePoint Network to collect, store, and interpret detailed data generated by their farming operations online, right down to creation of maps of fields that need to be plowed, seeded, or cut. It is benefits like this that make Deere the supplier of choice for many business customers.[1]

Business and Organizational Customers—A Big Opportunity

Most of us think about individual final consumers when we hear the term *customer.* But many marketing managers aim at customers who are not final consumers. In fact, more purchases are made by businesses and other organizations than by final consumers. As the John Deere case illustrates, the buying behavior of these organizational customers can be very different from the buying behavior of final consumers. Developing marketing strategies for these markets requires a solid understanding of who these customers are and how they buy. That is the focus of this chapter.

What types of customers are involved?

Business and organizational customers are any buyers who buy for resale or to produce other goods and services. Exhibit 7-1 shows the different types of customers in these markets. As you can see, not all of the organizational customers in these markets are business firms. Even so, to distinguish them from the final consumer market, managers sometimes refer to them collectively as the "business-to-business" market, or simply the *B2B market.*

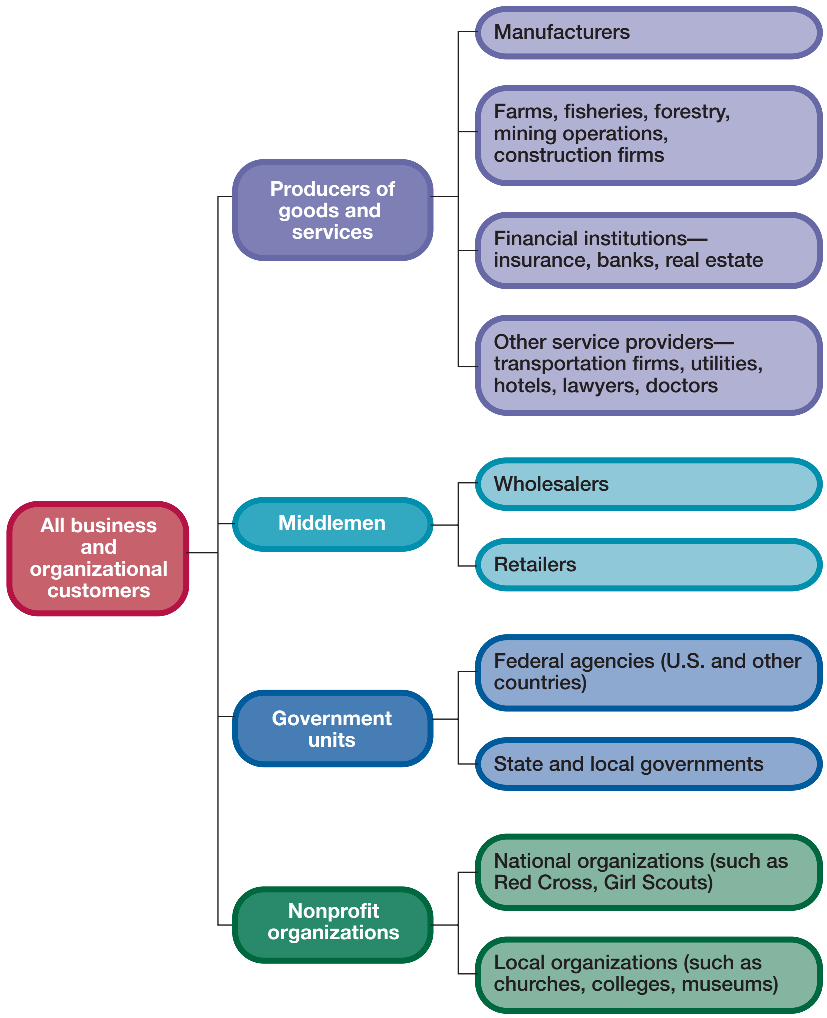
Many characteristics of buying behavior are common across these varied types of organizations. That's why the different kinds of organizational customers are sometimes loosely called "business buyers," "intermediate buyers," or "industrial buyers." As we discuss organizational buying, we will intermix examples of buying by many different types of organizations. Later in the chapter, however, we will highlight some of the specific characteristics of the different customer groups.

Organizational Customers Are Different

Organizations buy for a basic purpose

Like final consumers, organizations make purchases to satisfy needs. But it's often easier to understand an organization's needs because most organizations make purchases for the same basic reason. They buy goods and services that will help them meet the demand for the goods and services that they in turn supply to their markets. In other words, their basic need is to satisfy their own customers and clients. A producer buys because it wants to earn a profit by making and selling

Exhibit 7-1
Examples of Different Types of Business and Organizational Customers



goods or services. A wholesaler or retailer buys products it can profitably resell to its customers. A town government wants to meet its legal and social obligations to citizens. Similarly, a country club wants to help its members enjoy their leisure time.

Basic purchasing needs are economic

Organizational buyers typically focus on economic factors when they make purchase decisions. They are usually less emotional in their buying than final consumers.

Buyers try to consider the total cost of selecting a supplier and its particular marketing mix, not just the initial price of the product. For example, a hospital that needs a new type of X-ray equipment might look at both the original cost and ongoing costs, how it would affect doctor productivity, and of course the quality of the images it produces. The hospital might also consider the seller's reliability and general cooperativeness; the ability to provide speedy maintenance and repair, steady supply under all conditions, and reliable and fast delivery; and any past and present relationships (including previous favors and cooperation in meeting special requests).

The matter of dependability deserves further emphasis. An organization may not be able to function if purchases don't arrive when they're expected. For example,

Business customers usually focus on economic needs when they make purchase decisions, so Microsoft wants top decision makers to realize that its reliable server software eliminates downtime costs because it is up and running 99.999 percent of the time.

there's nothing worse to a manufacturer than shutting down a production line because sellers haven't delivered the goods. Dependable product quality is important too. For example, a bug in e-commerce software purchased by a firm might cause the firm's online order system to shut down. The costs of finding and correcting the problem—to say nothing about the cost of the lost business—could be completely out of proportion to the original cost of the software.

Even small differences are important

Understanding how the buying behavior of a particular organization differs from others can be very important. Even seemingly trivial differences in buying behavior may be important because success often hinges on fine-tuning the marketing mix.

Sellers often approach each organizational customer directly, usually through a sales representative. This gives the seller more chance to adjust the marketing mix for each individual customer. A seller may even develop a unique strategy for each individual customer. This approach carries target marketing to its extreme. But sellers often need unique strategies to compete for large-volume purchases.

In such situations, the individual sales rep takes much responsibility for strategy planning. The sales rep often coordinates the whole relationship between the supplier and the customer. That may involve working with many people—including top management—in both firms. This is relevant to your career planning since these interesting jobs are very challenging, and they pay well too.

Serving customers in international markets

Many marketers discover that there are good opportunities to serve business customers in different countries around the world. Specific business customs do vary from one country to another—and the differences can be important. For example, a salesperson working in Japan must know how to handle a customer's business card with respect. Japanese consider it rude to write notes on the back of a card or put it in a wallet while the person who presented it is still in the room. But the basic approaches marketers use to deal with business customers in different parts of the world are much less varied than those required to reach individual consumers.

This is probably why the shift to a global economy has been so rapid for many firms. Their business customers in different countries buy in similar ways and can be reached with similar marketing mixes. Moreover, business customers are often willing to work with a distant supplier who has developed a superior marketing mix.

Steel bearings are a small portion of the cost of producing an airplane, but Timken wants decision makers to keep in mind that it's critical to get the proven quality of its products.

Specifications describe the need

Organizational buyers often buy on the basis of a set of **purchasing specifications**—a written (or electronic) description of what the firm wants to buy. When quality is highly standardized, as is often the case with manufactured items, the specification may simply consist of a brand name or part number. With products like agricultural commodities, where there is more variation, the specification may include information about the grade of the product. Often, however, the purchase requirements are more complicated; then the specifications may set out detailed information about the performance standards the product must meet. Purchase specifications for services tend to be detailed because services tend to be less standardized and usually are not performed until after they're purchased.

Customers may expect quality certification

Organizational customers considering a new supplier or one from overseas may be concerned about product quality. However, this is becoming less of an obstacle because of ISO 9000. **ISO 9000** is a way for a supplier to document its quality procedures according to internationally recognized standards.

ISO 9000 assures a customer that the supplier has effective quality checks in place, without the customer having to conduct its own costly and time-consuming audit. Some customers won't buy from any supplier who doesn't have it. To get ISO 9000 certified, a company basically must prove to outside auditors that it documents in detail how the company operates and who is responsible for quality every step of the way.[2]

Many Different People May Influence a Decision

Purchasing managers are specialists

Many organizations, especially large ones, rely on specialists to ensure that purchases are handled sensibly. These specialists have different titles in different firms (such as purchasing agent, procurement officer, or buyer), but basically they are all **purchasing managers**—buying specialists for their employers. In large organizations, they usually specialize by product area and are real experts.

A person who works on a utility firm's high-power wires needs safe, durable climbing gear. A number of different people may influence the decision about which gear the firm should buy.

Some people think purchasing is handled by clerks who sit in cubicles and do the paperwork to place orders. That view is out-of-date. Today, most firms look to their purchasing departments to help cut costs and provide competitive advantage. In this environment, purchasing people have a lot of clout. And there are good job opportunities in purchasing for capable business graduates.

Salespeople often have to see a purchasing manager first—before they contact any other employee. These buyers hold important positions and take a dim view of sales reps who try to go around them. Rather than being "sold," these buyers want salespeople to provide accurate information that will help them buy wisely. They like information on new goods and services, and tips on potential price changes, supply shortages, and other changes in market conditions. Sometimes all it takes for a sales rep to keep a buyer up-to-date is to send an occasional e-mail. But a buyer can tell when a sales rep has the customer firm's interest at heart.

Although purchasing managers usually coordinate relationships with suppliers, other people may also play important roles in influencing the purchase decision.[3]

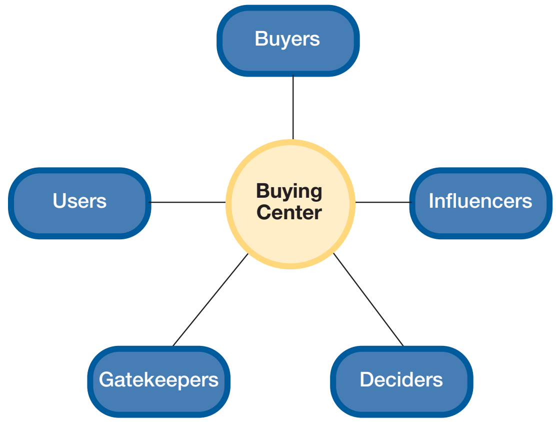
Multiple buying influence in a buying center

Multiple buying influence means that several people—perhaps even top management—share in making a purchase decision. Possible buying influences include:

1. *Users*—perhaps production line workers or their supervisors.
2. *Influencers*—perhaps engineering or R&D people who help write specifications or supply information for evaluating alternatives.
3. *Buyers*—the purchasing managers who have the responsibility for working with suppliers and arranging the terms of the sale.
4. *Deciders*—the people in the organization who have the power to select or approve the supplier—often a purchasing manager but perhaps top management for larger purchases.
5. *Gatekeepers*—people who control the flow of information within the organization—perhaps a purchasing manager who shields users or other deciders. Gatekeepers can also include receptionists, secretaries, research assistants, and others who influence the flow of information about potential purchases.

An example shows how the different buying influences work.

Exhibit 7-2
Multiple Influence and Roles in the Buying Center



Suppose Electrolux, the Swedish firm that produces vacuum cleaners, wants to buy a machine to stamp out the various metal parts it needs. An assistant to the purchasing manager does an Internet search to identify possible vendors. However, the list that the assistant (a gatekeeper) prepares for the manager excludes a few vendors on the basis of an initial evaluation of information from their websites. The manager e-mails a description of the problem to vendors on the list. It turns out that each of them is eager to get the business and submits a proposal. Several people (influencers) at Electrolux help to evaluate the vendors' proposals. A finance manager worries about the high cost and suggests leasing the machine. The quality control people want a machine that will do a more accurate job—although it's more expensive. The production manager is interested in speed of operation. The production line workers and their supervisors want the machine that is easiest to use so workers can continue to rotate jobs.

The company president (the decider) asks the purchasing department to assemble all the information but retains the power to select and approve the supplier. The purchasing manager's assistant schedules visits for salespeople. After all these buying influences are considered, one of the purchasing agents for the firm (the buyer) will be responsible for making recommendations and arranging the terms of the sale.

It is helpful to think of a **buying center** as all the people who participate in or influence a purchase. Different people may make up a buying center from one decision to the next. This makes the marketing job difficult.

The salesperson must study each case carefully. Just learning who to talk with may be hard, but thinking about the various roles in the buying center can help. See Exhibit 7-2.

The salesperson may have to talk to every member of the buying center—stressing different topics for each. This not only complicates the promotion job but also lengthens it. Approval of a routine order may take anywhere from a day to several months. On very important purchases—a new computer system, a new building, or major equipment—the selling period may take a year or more.[4]

Vendor analysis considers all of the influences

Considering all of the economic factors and influences relevant to a purchase decision is sometimes complex. A supplier or product that is best in one way may not be best in others. To try to deal with these situations, many firms use **vendor analysis**—a formal rating of suppliers on all relevant areas of performance. The purpose isn't just to get a low price from the supplier on a given part or service. Rather, the goal is to lower the *total costs* associated with purchases. Analysis might show that the best vendor is the one that helps the customer reduce costs of excess inventory, retooling of equipment, or defective parts.[5]

Internet

Internet Exercise At the Computer Discount Warehouse website (www.cdw.com) a buyer can compare the features and prices of alternative products. Click on "Notebooks" (under the PRODUCTFINDER heading) and then search for notebooks with a Processor Speed of at least 1GHz. Select two notebooks from two different manufacturers and click compare. How helpful would this analysis be if you were a computer buyer?

Behavioral needs are relevant too

Vendor analysis tries to focus on economic factors, but purchasing in organizations may also involve many of the same behavioral dimensions we discussed in Chapter 6. Purchasing managers and others involved in buying decisions are human, and they want friendly relationships with suppliers.

The purchasing people in some firms are eager to imitate progressive competitors or even to be the first to try new products. Such "innovators" deserve special attention when new products are being introduced.

The different people involved in purchase decisions are also human with respect to protecting their own interests and their own position in the company. That's one reason people from different departments may have different priorities in trying to influence what is purchased. Similarly, purchasing managers may want to avoid taking risks that might reflect badly on their decisions. They have to buy a wide variety of products and make decisions involving many factors beyond their control. If a new source delivers late or quality is poor, you can guess who will be blamed. Marketers who can help the buyer avoid risk have a definite appeal. In fact, this may make the difference between a successful and unsuccessful marketing mix.

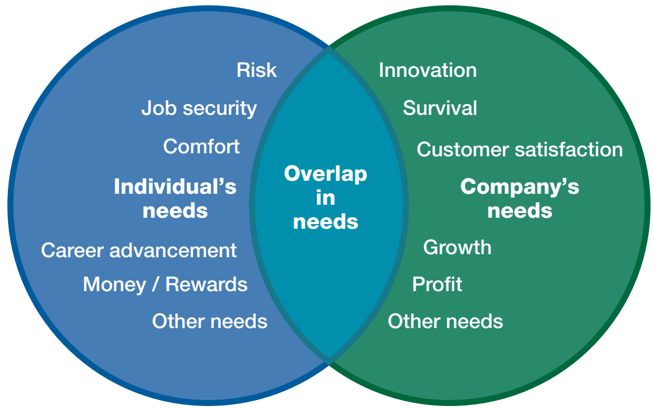
A seller's marketing mix should satisfy *both* the needs of the customer company as well as the needs of individuals who influence the purchase. Therefore, sellers need to find an overlapping area where both can be satisfied. See Exhibit 7-3 for a summary of this idea.

Ethical conflicts may arise

Although organizational buyers are influenced by their own needs, most are serious professionals who are careful to avoid a conflict between their own self-interest and company outcomes. Marketers must be careful here. A salesperson who offers one of his company pens to a prospect may view the giveaway as part of the promotion effort—but the customer firm may have a policy against any employee accepting *any* gift from a supplier. For example, General Motors developed an ethics policy that forbids employees from accepting anything of value from a vendor. It specifically includes entertainment—like a golf outing, a steak dinner, or tickets to a sporting event.

Organizational customers want reliable suppliers who will deliver on their promises and not reflect badly on the buyer's decisions.

Exhibit 7-3
Overlapping Needs of Individual Influencers and the Customer Organization



Most organizational buyers do their work ethically and expect marketers to do the same. Yet there have been highly publicized abuses. For example, some members of the site selection committee for the 2000 Olympic Games asked for personal gifts that may have influenced where the games were held. In another case, the telephone company that serves New York found out that some of its buyers were giving contracts to suppliers who offered them vacation trips and other personal favors. Abuses of this sort have prompted many organizations to set up policies that prohibit a buyer or other employees from accepting anything from a potential supplier.

Marketers need to take concerns about conflict of interest very seriously. Part of the promotion job is to persuade different individuals who may influence an organization's purchase. Yet the whole marketing effort may be tainted if it even *appears* that a marketer has encouraged a person who influences a decision to put personal gain ahead of company interest.[6]

Purchasing may be centralized

If a large organization has facilities at many locations, much of the purchasing work may be done at a central location. With centralized buying, a sales rep may be able to sell to facilities all over a country—or even across several countries—without leaving a base city. Wal-Mart handles most of the purchase decisions for stores in its retail chain from its headquarters in Arkansas. Many purchasing decisions for agencies of the U.S. government are handled in Washington, D.C.

Many firms also have centralized controls on who can make purchases. A person who needs to purchase something usually completes a **requisition**—a request to buy something. This is frequently handled online to cut time and paper shuffling. Even so, there may be delays before a supervisor authorizes the requisition and a purchasing manager can select the "best" seller and turn the authorization into a purchase order. The process may take a few hours for a simple purchase—but it may turn into months for a complex purchase.

Organizational Buyers Are Problem Solvers

Three kinds of buying processes are useful

In Chapter 6, we discussed problem solving by consumers and how it might vary from extensive problem solving to routine buying. In organizational markets, we can adapt these concepts slightly and work with three similar buying processes: a new-task buying process, a modified rebuy process, or a straight rebuy.[7] See Exhibit 7-4.

Exhibit 7-4
Organizational Buying Processes

Characteristics	Type of Process		
	New-Task Buying	Modified Rebuy	Straight Rebuy
Time Required	Much	Medium	Little
Multiple Influence	Much	Some	Little
Review of Suppliers	Much	Some	None
Information Needed	Much	Some	Little

New-task buying occurs when an organization has a new need and the customer wants a great deal of information. New-task buying can involve setting product specifications, evaluating sources of supply, and establishing an order routine that can be followed in the future if results are satisfactory. Multiple buying influence is typical in new-task buying.

A **straight rebuy** is a routine repurchase that may have been made many times before. Buyers probably don't bother looking for new information or new sources of supply. Most of a company's small or recurring purchases are of this type—but they take only a small part of an organized buyer's time. Important purchases may be made this way too—but only after the firm has decided what procedure will be "routine."

The **modified rebuy** is the in-between process where some review of the buying situation is done—though not as much as in new-task buying. Sometimes a competitor will get lazy enjoying a straight rebuy situation. An alert marketer can turn these situations into opportunities by providing more information or a better marketing mix.

New-task buying requires information

Customers in a new-task buying situation are likely to seek information from a variety of sources. See Exhibit 7-5. Keep in mind that many of the impersonal sources are readily available in electronic form online as well as in other formats. How much information a customer collects depends on the importance of the purchase and the level of uncertainty about what choice might be best. The time and expense of searching for information may not be justified for a minor purchase. But a major purchase often involves real detective work by the buyer.

Of course, the flip side of the new-task buying situation is that a seller's promotion has much more chance to have an impact. At the very least, the marketer needs to be certain that his or her firm will turn up in the buyer's search. In this regard, a good website is a crucial piece of insurance. Later we will talk more about the role of e-commerce at this stage, but for now you should see that even a simple website is likely to turn up in a buyer's Internet search.[8]

Exhibit 7-5
Major Sources of Information Used by Organizational Buyers

	Marketing sources	Nonmarketing sources
Personal sources	• Salespeople • Others from supplier firms • Trade shows	• Buying center members • Outside business associates • Consultants and outside experts
Impersonal sources	• Advertising in trade publications • Sales literature • Sales catalogs • Web page	• Rating services • Trade associations • News publications • Product directories • Internet news pointcasts

What buying procedure becomes routine is critical

Once a buying firm gets beyond the early stages of a new-task buying decision, it needs to make important decisions about how it is going to deal with one or more suppliers to meet its needs. At one extreme, a buyer might want to rely on competition among all available vendors to get the best price on each and every order it places. At the other extreme, it might just routinely buy from one vendor with whom it already has a good relationship. In practice, there are many important and common variations between these extremes. To better understand the variations—and why firms rely on different approaches in different situations—let's take a closer look at the benefits and limitations of different types of buyer–seller relationships. That will also help you to see why new e-commerce developments in business markets have become so important.

Buyer–Seller Relationships in Business Markets

Close relationships may produce mutual benefits

There are often significant benefits of a close working relationship between a supplier and a customer firm. And such relationships are becoming common. Many firms are reducing the number of suppliers with whom they work—expecting more in return from the suppliers that remain. The best relationships involve real partnerships where there's mutual trust and a long-term outlook.

Closely tied firms can often share tasks at lower total cost than would be possible working at arm's length. Costs are sometimes reduced simply by reducing uncertainty and risk. A supplier is often able to reduce its selling price if a customer commits to larger orders or orders over a longer period of time. A large sales volume may produce economies of scale and reduce selling costs. The customer benefits from lower cost and also is assured a dependable source of supply.

A firm that works closely with a supplier can resolve joint problems. For example, it may cost both the supplier and the customer more to resolve the problems of a defective product after it is delivered than it would have cost to prevent the problem. But without the customer's help it may be impossible for the supplier to identify a solution to the problem. As the head of purchasing at Motorola puts it, "Every time we make an error it takes people at both ends to correct it."

In business-to-business markets, the Internet has prompted explosive growth in e-commerce and new central market "portals" that bring buyers and sellers together more quickly and at lower cost.

In today's business markets, suppliers of both goods and services are working to build closer relationships with their business customers—to meet needs better and create a competitive advantage.

The partnership between AlliedSignal and Betz Laboratories shows the benefits of a good relationship. A while back, Betz was just one of several suppliers that sold Allied chemicals to keep the water in its plants from gunking up pipes and rusting machinery. But Betz didn't stop at selling commodity powders. Teams of Betz experts and engineers from Allied studied each plant to find places where water was being wasted. In less than a year a team in one plant found $2.5 million in potential cost reductions. For example, by adding a few valves to recycle the water in a cooling tower, Betz was able to save 300 gallons of water a minute, which resulted in savings of over $100,000 a year and reduced environmental impact. Because of ideas like this, Allied's overall use of water treatment chemicals decreased. However, Betz sales to Allied doubled because it became Allied's sole supplier.[9]

Relationships may not make sense

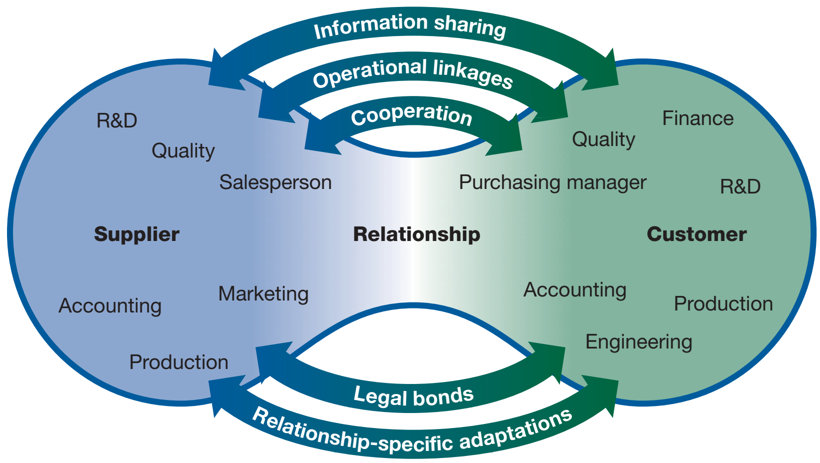
Although close relationships can produce benefits, they are not always best. A long-term commitment to a partner may reduce flexibility. When competition drives down prices and spurs innovation, the customer may be better off letting suppliers compete for the business. It may not be worth the customer's investment to build a relationship for purchases that are not particularly important or made that frequently.

It may at first appear that a seller would *always* prefer to have a closer relationship with a customer, but that is not so. Some customers may place orders that are too small or require so much special attention that the relationship would never be profitable for the seller. Also, in situations where a customer doesn't want a relationship, trying to build one may cost more than it's worth. Further, many small suppliers have made the mistake of relying too heavily on relationships with too few customers. One failed relationship may bankrupt the business.[10]

Relationships have many dimensions

Relationships are not "all or nothing" arrangements. Firms may have a close relationship in some ways and not in others. Thus, it's useful to know about five key dimensions that help characterize most buyer–seller relationships: cooperation, information sharing, operational linkages, legal bonds, and relationship-specific adaptations. Purchasing managers for the buying firm and salespeople for the supplier

Exhibit 7-6
Key Dimensions of Relationships in Business Markets



usually coordinate the different dimensions of a relationship. However, as shown in Exhibit 7-6, close relationships often involve direct contacts between a number of people from other areas in both firms.[11]

Cooperation treats problems as joint responsibilities

In cooperative relationships, the buyer and seller work together to achieve both mutual and individual objectives. This doesn't mean that the buyer (or seller) will always do what the other wants. Rather, the two firms treat problems that arise as a joint responsibility.

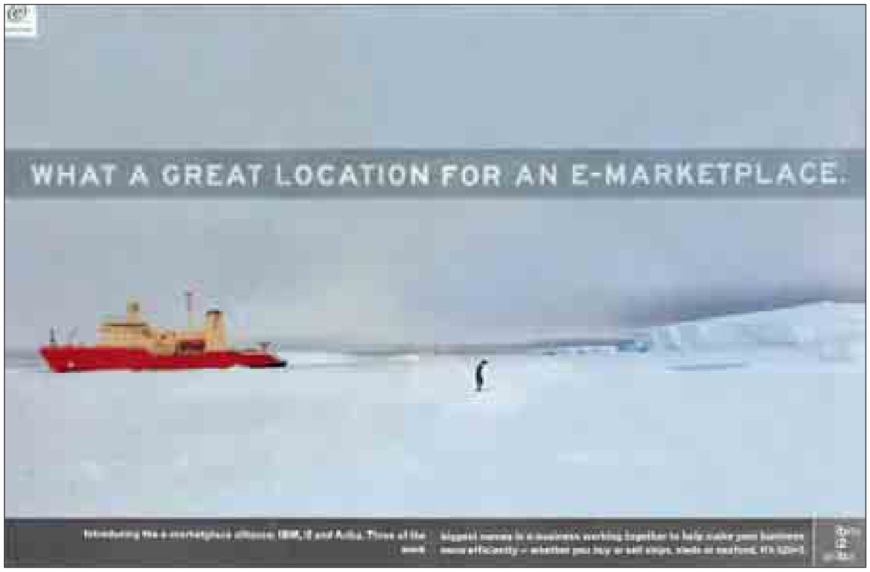
National Semiconductor (NS) and Siltec, a supplier of silicon wafers, have found clever ways to cooperate and cut costs. For example, workers at the NS plant used to throw away the expensive plastic cassettes that Siltec uses to ship the silicon wafers. Now Siltec and NS cooperate to recycle the cassettes. This helps the environment and also saves more than $300,000 a year. Siltec passes along most of that to NS as lower prices.[12]

Shared information is useful but may be risky

Some relationships involve open sharing of information that is useful to both the buyer and seller. This might include the exchange of proprietary cost data, discussion of demand forecasts, and joint work on new product designs. Information might be shared through information systems or over the Internet. This is often a key facet of relationships that involve e-commerce.

Many firms share information by providing relationship partners with access to password-protected websites. One big advantage of this approach is that it is fast and easy to update the information. A customer can trust information that is the same information used by someone inside the company. In addition, it provides easy "click-here" self-service access for customers who might have very different computer systems in their own firms. It also saves time. A customer can check detailed product specs or the status of a job on the production line without having to wait for a sales rep or someone else to answer the question.

Information sharing can lead to better decisions, reduced uncertainty about the future, and better planning. However, firms don't want to share information if there's a risk that a partner might misuse it. For example, some suppliers claim that General Motors' former purchasing chief showed blueprints of their secret technology to competing suppliers. Such violations of trust in a relationship are an ethical matter and should be taken seriously. However, as a practical matter, it makes sense to know a partner well before revealing all.



IBM, I2, and Ariba have formed an alliance to work together cooperatively and develop closer relationships with business customers, no matter what the customer's e-commerce purchasing needs may be.

Operational linkages share functions between firms

Operational linkages are direct ties between the internal operations of the buyer and seller firms. These linkages usually involve formal arrangements and ongoing coordination of activities between the firms. Shared activities are especially important when neither firm, working on its own, can perform a function as well as the two firms can working together. John Deere's relationship with MetoKote, described at the start of this chapter, involves operational linkages.

Operational linkages are often required to reduce total inventory costs. Business customers want to maintain an adequate inventory—certainly enough to prevent stock-outs or keep production lines moving. On the other hand, keeping too much inventory is expensive. Providing a customer with inventory when it's needed may require that a supplier be able to provide **just-in-time delivery**—reliably getting products there *just* before the customer needs them. We'll discuss just-in-time systems in more detail in Chapter 12. For now, it's enough to see that just-in-time relationships between buyers and sellers usually require operational linkages (as well as information sharing). For example, Wal-Mart might want a producer of socks to pack cartons so that when they are unloaded at a Wal-Mart distribution facility all of the cartons for a certain store or district are grouped together. This makes it easier and faster for forklifts to "cross dock" the pallets and load them onto an outbound truck. This also reduces Wal-Mart's costs because the cartons only need to be handled one time. However, it means that the supplier's production and packing of socks in different colors and sizes must be closely linked to the precise store in the Wal-Mart chain that places each order.

Operational linkages may also involve the routine activities of individuals who almost become part of the customer's operations. Design engineers, salespeople, and service representatives may participate in developing solutions to ongoing problems, conduct regular maintenance checks on equipment, or monitor inventory and coordinate orders. At the DaimlerChrysler design center, for example, 30 offices are set aside for full-time use by people employed by suppliers.

Linkages may be customized to a particular relationship, or they may be standardized and operate the same way across many exchange partners. For example, in the channel of distribution for grocery products many different producers are standardizing their distribution procedures and coordinating with retail chains to make it faster and cheaper to replenish grocery store shelves.

When a customer's operations are dependent on those of a supplier, it may be difficult or expensive to switch to another supplier. So buyers sometimes avoid a relationship that would result in these "switching costs."

Contracts spell out obligations

Many purchases in business markets are simple transactions. The seller's basic responsibility is to transfer title to goods or perform services, and the buyer's basic responsibility is to pay the agreed price. However, in some buyer–seller relationships the responsibilities of the parties are spelled out in a detailed legal contract. An agreement may apply only for a short period, but long-term contracts are also common.

For example, a customer might ask a supplier to guarantee a 6 percent price reduction for a particular part for each of the next three years and pledge to virtually eliminate defects. In return, the customer might offer to double its orders and help the supplier boost productivity. This might sound attractive to the supplier but also require new people or facilities. The supplier may not be willing to make these long-term commitments unless the buyer is willing to sign a contract for promised purchases. The contract might spell out what would happen if deliveries are late or if quality is below specification.

Sometimes the buyer and seller know roughly what is needed but can't fix all the details in advance. For example, specifications or total requirements may change over time. Then the relationship may involve **negotiated contract buying,** which means agreeing to a contract that allows for changes in the purchase arrangements. In such cases, the general project and basic price is described but with provision for changes and price adjustments up or down. Or a supplier may be asked to accept a contract that provides some type of incentive—such as full coverage of costs plus a fixed fee or full costs plus a profit percentage tied to costs.

When a contract provides a formal plan for the future of a relationship, some types of risk are reduced. But a firm may not want to be legally locked in when the future is unclear. Alternatively, some managers figure that even a detailed contract isn't a good substitute for regular, good-faith reviews to make sure that neither party gets hurt by changing business conditions.

Harley-Davidson used this approach when it moved toward closer relationships with a smaller number of suppliers. Purchasing executives tossed out detailed contracts and replaced them with a short statement of principles to guide relationships between Harley and its suppliers. This "operate on a handshake" approach is typical of relationships with Japanese firms. Many other firms have adopted it. It's great when it works, and a disaster when it doesn't.

Specific adaptations invest in the relationship

Relationship-specific adaptations involve changes in a firm's product or procedures that are unique to the needs or capabilities of a relationship partner. Industrial suppliers often custom design a new product for just one customer; this may require investments in R&D or new manufacturing technologies. Donnelly Corp. is an extreme example. It had been supplying Honda with mirrors for the interiors of its cars. Honda's purchasing people liked Donnelly's collaborative style, so they urged Donnelly to supply exterior mirrors as well. Donnelly had never been in that business—so it had to build a factory to get started.

Buying firms may also adapt to a particular supplier; a computer maker may design around Intel's Pentium chip, and independent photo processors say "We use Kodak paper for the good look" in their advertising. However, buyers are often hesitant about making big investments that increase dependence on a specific supplier. Typically, they do it only when there isn't a good alternative—perhaps because only one or a few suppliers are available to meet a need—or if the benefits of the investment are clear before it's made. On the other hand, sometimes a buyer will invest in a relationship because the seller has already demonstrated a willingness to do so.[13]

The relationship between Flex-N-Gate and Toyota illustrates relationship-specific adaptations. Flex-N-Gate had a contract to supply some of the rear bumpers Toyota needed for its U.S. facilities. After a while, however, Toyota's quality control people were unhappy about the number of minor defects in the bumpers. Further, Flex-N-Gate's deliveries were not as dependable as Toyota's production people required. Rather than just end the relationship, Toyota and Flex-N-Gate both made investments to improve it. Toyota sent a team of experts who spent a lot of time figuring out the reasons for the problems and then showing Flex-N-Gate how to build better bumpers faster and cheaper. Following the advice of Toyota's experts, Shahid Khan (Flex-N-Gate's owner) reorganized equipment in his factory. He also had to retrain his employees to do their jobs in new ways. The changes were so complicated that two of Khan's six production supervisors quit in frustration. But the trouble was worth the effort. Productivity went up 60 percent, the number of defects dropped by 80 percent, and Flex-N-Gate got a larger share of Toyota's business. Toyota got something it wanted, too: a committed supplier that could meet its standards and a big price reduction on bumpers.[14]

A seller may have more incentive to propose new ideas that save the customer money when the firms have a mutual investment in a long-term relationship. The customer firm usually rewards the seller with more orders or a larger share of its business, and this encourages future suggestions and loyalty by the supplier. In contrast, buyers who use a competitive bid system exclusively—either by choice or necessity, as in some government and institutional purchasing—may not be offered much beyond basic goods and services. They are interested primarily in price.

Powerful customer may control the relationship

Although a marketing manager may want to work in a cooperative partnership, that may be impossible with large customers who have the power to dictate how the relationship will work. For example, Duall/Wind, a plastics producer, was a supplier of small parts for Polaroid instant cameras. But when Duall/Wind wanted to raise its prices to cover increasing costs, Polaroid balked. Polaroid's purchasing manager demanded that Duall/Wind show a breakdown of all its costs, from materials to labor to profit. As Duall/Wind's president said, "I had a tough time getting through my head that Polaroid wanted to come right in here and have us divulge all that." But Polaroid is a big account—and it got the information it wanted. Polaroid buyers agreed to a price increase only after they were confident that Duall/Wind was doing everything possible to control costs.[15]

Buyers may still use several sources to spread their risk

Even if a marketing manager develops the best marketing mix possible and cultivates a close relationship with the customer, the customer may not give *all* of its business to one supplier. Buyers often look for several dependable sources of supply to protect themselves from unpredictable events such as strikes, fires, or floods in one of their suppliers' plants. A good marketing mix is still likely to win a larger share of the total business—which can prove to be very important. From a buyer's point of view, it may not seem like a big deal to give a particular supplier a 30 percent share of the orders rather than a 20 percent share. But for the seller that's a 50 percent increase in sales![16]

Reciprocity may influence relationship

We've emphasized that most buyer–seller relationships are based on reducing the customer's total procurement costs. However, for completeness we should mention that some relationships are based on reciprocity. **Reciprocity** means trading sales for sales—that is, "if you buy from me, I'll buy from you." If a company's customers also can supply products that the firm buys, then the sales departments of both buyer and seller may try to trade sales for sales. Purchasing managers generally resist reciprocity but often face pressure from their sales departments.

When prices and quality are otherwise competitive, an outside supplier seldom can break a reciprocity relationship. The supplier can only hope to become an alternate source of supply and wait for the competitor to let its quality slip or prices rise.

Reciprocity is often a bigger factor in other countries than it is in the United States. In Japan, for example, reciprocity is very common.[17]

We've been discussing some of the differences in how customer firms and their suppliers relate to each other. How a customer uses e-commerce is also related to these differences.

Internet E-Commerce Is Reshaping Many Business Markets

The Internet and new types of B2B e-commerce websites have quickly and dramatically changed the way in which many purchase decisions are made and how a firm relates to its suppliers. In general, the Web is making it possible for all types of information to flow back and forth between buyers and sellers much more quickly and efficiently. This lowers the cost of the search for market information and, in many cases, the cost of transactions. For example, online order systems can cut out paper-shuffling bottlenecks, speed the delivery of purchases, and reduce inventory costs. We'll discuss distribution service related issues in more detail in Chapter 12.

Here, we'll consider basic e-commerce website resources that many buyers use and the role that they play. We'll consider them separately, but often one website (or linked set of websites) combines them.

Community sites mainly offer digital information

Like online trade magazines (or online trade associations), community sites offer information and communications of interest for specific industries. A website may focus on a single "community" or feature different sections for many different industries. For example, www.verticalnet.com has many separate communities for different industries, ranging from food processing and solid-waste management to health care and utilities. Community sites were among the first on the Web because many just put in digital form information that was already being distributed in other ways. Initially they relied on advertising revenue to operate, but now some of them are trying to earn commissions based on sales referrals.

Catalog sites make it convenient to search for products

Catalog sites, as the name implies, offer digital product catalogs, usually for a number of different sellers. For example, PlasticsNet.com focuses on polymers and resins used in the plastic industry. The basic benefit of catalog sites is that they make it easy for industrial buyers to search for a product and do one-stop shopping. For example, Grainger's OrderZone.com features a vast array of supply items that are used across many different industries. Some catalog sites are trying to upgrade their software and service to make it easier for a buyer to place an order, track delivery status, and update inventory information. Others are trying to improve the quality of the information available. For example, rather than just give a basic description of an electric motor a site might also provide a link so the buyer can download detailed engineering drawings and electrical details.

Exchanges bring buyers and sellers together

Exchanges operate much like a stock exchange (for example, the New York Stock Exchange) by bringing buyers and sellers together, usually anonymously, to agree on prices for commodities such as energy (see, for example, www.altranet.com) or telecommunications capacity. Exchanges are sometimes independent intermediaries or they may be backed by major firms in the industry. Either way, an exchange must maintain a neutral role and not favor either buyers or sellers if it expects return visits.

Procurement hubs operate for the benefit of buyers

Procurement hub sites direct suppliers to particular companies (or industries) in one place. Some large companies have created procurement hubs to handle purchasing for all of their own divisions. In some industries, recognized leaders have banded together to create procurement hubs. The big three automakers in the U.S. are doing this. These hubs are becoming an important, buyer-driven force in e-commerce. They make it easier for a larger number of suppliers to find out about the purchasing needs of customers in target industries. As a result, the number of suppliers competing for a buyer's business increases, and this tends to drive down selling prices or provide benefits to the buyer with respect to other terms of the sale. On the other hand, procurement hubs are a way for a seller to find out about and pursue sales opportunities with new customers (or new markets) without a lot of additional selling expense.

Interactive competitive bidding systems drive down prices

Most procurement hubs incorporate some sort of interactive system to get competitive bids. **Competitive bids** are the terms of sale offered by different suppliers in response to the purchase specifications posted by the buyer. Usually, the focus is on the supplier's price. Firms have used the competitive bidding process for a long time. However, before the Internet it was usually too slow and too inconvenient to go through several rounds of bids. Now, however, the Internet makes it fast and easy for the customer firm to run what is sometimes called a *reverse auction*. Vendors are invited (via e-mail or at the procurement hub) to place a bid for a purchase with a given specification. Usually the bidding still focuses on price, but sometimes other terms of sales (like warranty period or delivery time) are considered as well. Each bid, and who made it, is typically visible to all potential bidders via the website. That way, other bidders can decide whether or not to offer the customer a lower price. Depending on the preferences of the customer, the bidding can be limited by a specific deadline.

Auction sites focus on unique items

Auction sites tend to be more seller-driven and are especially popular for items such as used equipment and vehicles, surplus inventory, and perishable products (such as unsold advertising space or produce) that are unique and only available for sale once. For example, www.avbid.new runs auctions related to aircraft parts and services. At these auctions the seller lists and describes what's for sale, and potential buyers place their bids (what they would pay) at a website. Auctions use a variety of formats, but in general the highest bidder (prior to the deadline) purchases the product. Some auction sites also handle reverse auctions for the benefit of buyers.

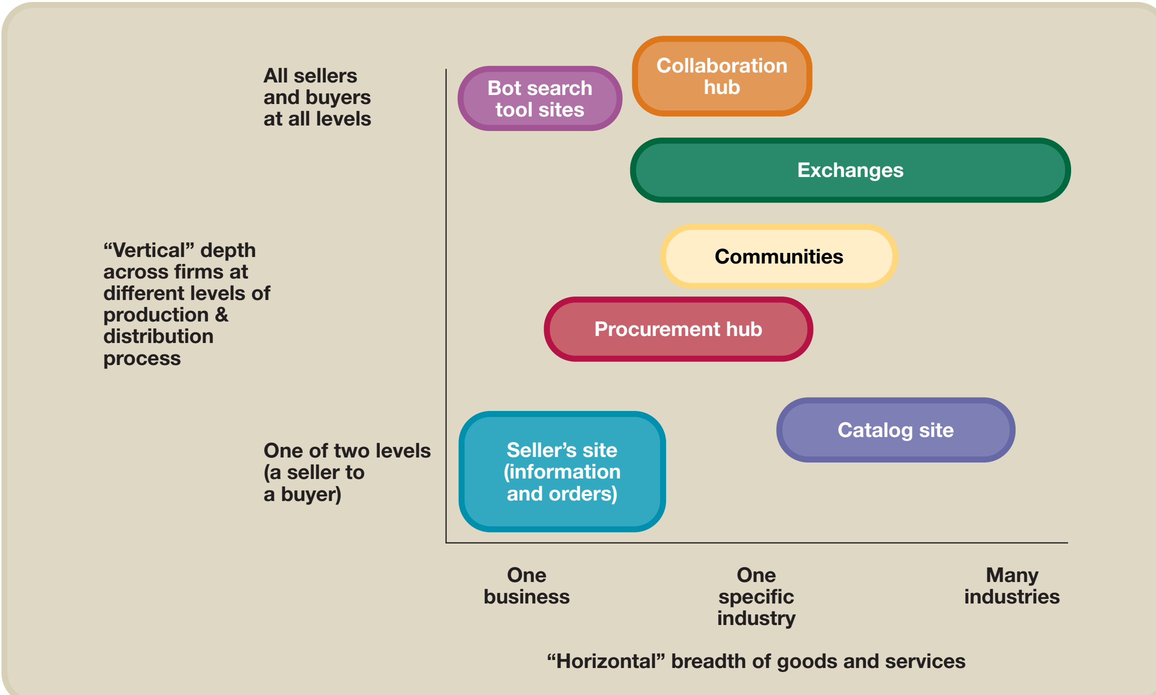
Collaboration hubs support cooperation

Collaboration hubs go beyond matching buyers and sellers for a one-time transaction and instead are designed to help firms work together. The collaboration might involve design, manufacturing, and distribution. Many of these sites focus on the needs of smaller firms, usually within a vertical industry. For instance, Citadon (www.citadon.com) provides a single online workplace for construction contractors to collaborate with architects, store blueprints, work through building permit requirements, and purchase building materials.

Websites within and across industries

As the examples above suggest, some B2B e-commerce websites are specialized for firms at different levels of production and distribution within a particular industry. For example, one of these "vertical" sites that specializes on the plastics industry might be of interest to firms that make the basic chemicals from which plastics are formed, firms that create plastic injection molding equipment, and

Exhibit 7-7 Examples of Different B2B E-Commerce Sites Used by Organizational Buyers and Sellers



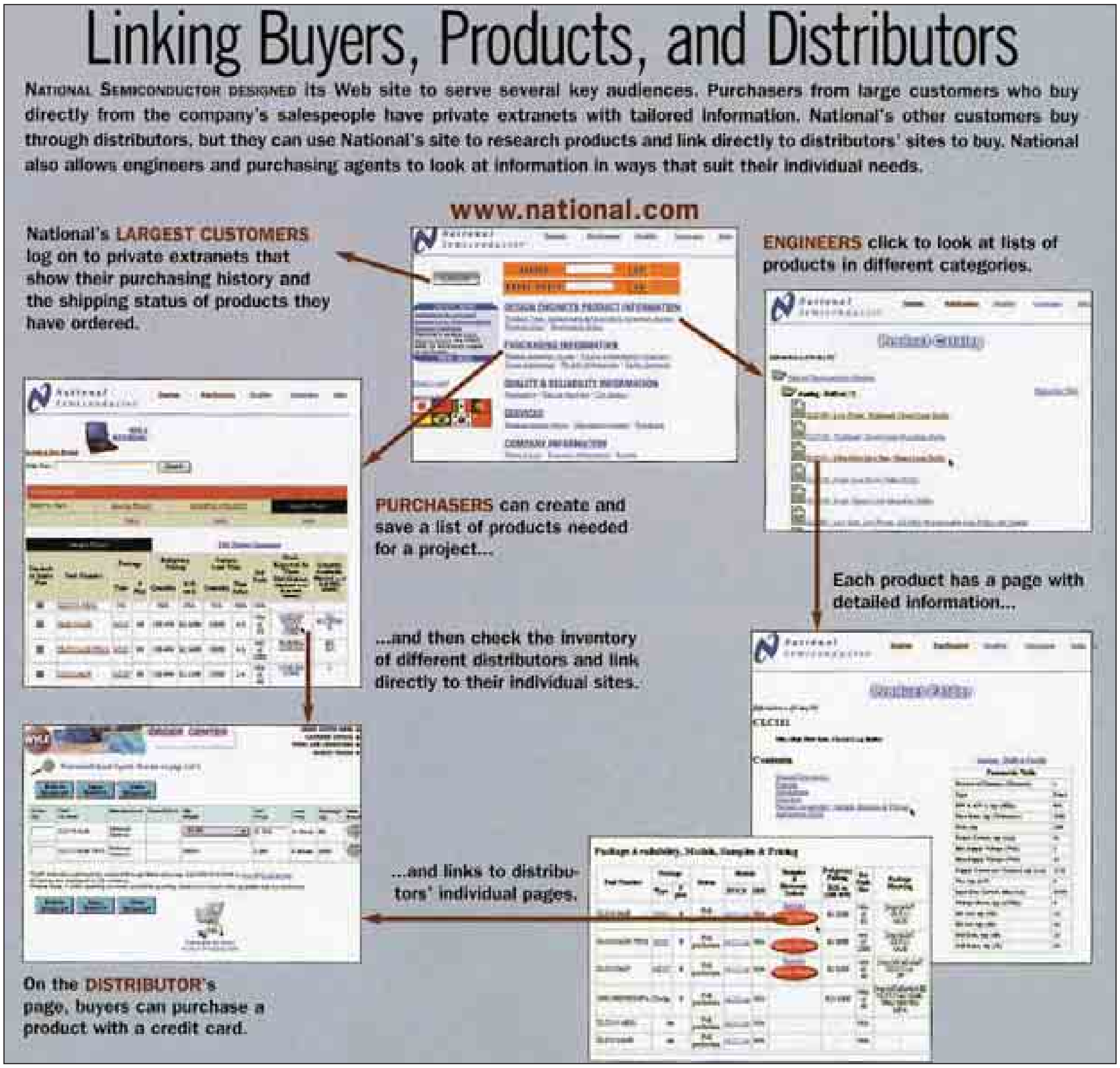
firms that use that equipment to make finished goods. On the other hand, some websites are designed to serve a broad ("horizontal") cross section of firms from different industries. For example, a horizontal site might serve manufacturers regardless of whether they produce bearings, truck frames, or construction equipment. See Exhibit 7-7.

One consequence of these differences in focus is that there are many sites with potentially overlapping coverage. While some industries are not covered well, in other industries many sites compete to be *the* central market. As a result, this is an arena in which there are still many ongoing changes. Hundreds, or perhaps thousands, of B2B websites that were established just a few years ago have already disappeared, and consolidation is still underway. In some industries there are so many sites that instead of simplifying the buying and selling process they have made it unnecessarily complicated. For example, a seller who posts an auction on the wrong site may get few bids, or no bids, from firms who might be serious buyers. Those buyers, in turn, might waste time checking other sites not included in the sellers' efforts.

Internet (ro)bots search for products—by description

Because of such problems, purchasing managers often turn to special software packages to help with their search effort. For example, if a purchasing manager can specify a certain model of a product the search "bot" (short for *robot*) looks at all of the websites on the Internet to find everywhere that the product is mentioned. Some bots take things further and assemble price comparisons or e-mail distribution lists.

Bots are also helping purchasing people who have trouble figuring out exactly how to describe what they want. By searching for descriptions of products in a broad product category, it is often possible to develop a better understanding not only of what alternatives exist but also of what specs are best for the particular need.



Some purchasing managers are using this basic approach to locate hard-to-find, off-the-shelf products that eliminate the need for custom-produced items. For example, Allstates Rubber & Tools in the suburbs of Chicago is a small firm, but it's on the Internet. Allstates recently got a $1,000 order for rubber grommets (tiny rings used to protect electric wires) from a company in Saudi Arabia. If the customer had not been able to locate Allstates' website on the Internet it probably would have paid higher prices to have the grommets custom-produced—and Allstates would have missed the business.[18]

GE Lights the Way for E-Commerce

General Electric is a true pioneer in e-commerce—and its successes provide evidence of what is possible. Even so, some of its early efforts didn't work. When it first tried to solicit bids from vendors over the Internet, it only focused on price. So it got a lot of lowball quotes from firms that didn't have the ability to fill orders. By 1995 GE was on a smarter track. It developed an Internet-based system called the Trading Process Network (TPN) that eliminated the delays of traditional purchasing approaches still using paper documents and snail mail. With TPN, a buyer for GE's lighting division could search the Net to find possible suppliers for the custom-made machine tools it needed. To eliminate the paper shuffle, electronic blueprints could be sent with a bid request via e-mail. As a GE purchasing manager put it, they could "simply point and click and send out a bid package to suppliers around the world." Suppliers could respond quickly, too. So a bid process that previously took about a month could be reduced to only days, or even hours.

When GE executives saw how e-commerce was improving their purchasing, they decided to offer the TPN service to outside companies. A small firm could try the TPN Web (www.getradeweb.com) for a fee of only $65 a month. However, the monthly fee for a large company was $70,000. That pricing gives a hint of the kind of savings big purchasers could reap—and why GE's Global eXchange Services (GXS) division pushed to develop a full-service Internet portal (www.gegxs.com). GSX now operates one of the largest B2B e-commerce networks in the world. It has more than 100,000 trading partners. The network handles 1 billion transactions a year for goods and services worth $1 trillion.

GE has continued to drive down its own purchasing costs with e-commerce. In the first six months that it used real-time, online competitive bidding, GE saved $480 million. However, even GE does not purchase everything this way. Its current target is to do about 30 percent of purchases online. And even with online competitive bidding it does not always select the lowest bid. A supplier with a higher bid may get the business when it offers service or other value that GE needs.[19]

www.mhhe.com/fourps

More progress is needed

You can see that there are many different B2B e-commerce sites that are helping sellers find interested buyers and vice versa. Until recently, much of the attention was on providing information to drive down the purchase price for specific transactions. Yet as we've said from the start, business customers are usually interested in the total cost of working with a supplier and the value of a supplier's marketing mix—not just in the product price. When everything else is the same, a buyer would obviously prefer low prices. But "everything else" is not always the same. We considered many examples of this earlier when we reviewed why a buyer might prefer closer relationships with fewer sellers. So it is important to see that Internet tools that focus primarily on lowering purchase prices do not necessarily lower total purchasing costs or apply to all types of purchases.

On the other hand, great strides are being made in developing websites and Internet-based software tools that help both buyers and sellers work together in more efficient and effective relationships. National Semiconductor's website is a good example. It is designed to create easy links between its customers, products, and distributors. Its large customers get special services, like access to a secure website that shows specific purchase histories and production or shipping status of their orders. Smaller customers can get all the product information they need and then link directly to the order page for the distributor that serves them. This system does not go as far as some, but it does illustrate how shared information and cooperation over the Internet is helping to create better relationships in business markets.[20]

E-commerce order systems are common

We've been discussing ways in which buyers and sellers use the Web. But e-commerce computer systems now *automatically* handle a large portion of routine order-placing. Buyers program decision rules that tell the computer how to order

Many firms, including Hertz and Chevrolet (a division of GM), are developing new strategies to target small businesses—a fast growing sector of the economy.

and leave the details of following through to the machine. For example, when an order comes in that requires certain materials or parts, the computer system automatically orders them from the appropriate suppliers, the delivery date is set, and production is scheduled.

When economic conditions change, buyers modify the computer instructions. When nothing unusual happens, however, the computer system continues to routinely rebuy as needs develop—electronically sending purchase orders to the regular supplier.

Obviously, it's a big sale to be selected as the major supplier that routinely receives all of a customer's electronic orders for the products you sell. Often this type of customer will be more impressed by an attractive marketing mix for a whole *line* of products than just a lower price for a particular order. Further, it may be too expensive and too much trouble to change the whole buying system just because somebody is offering a low price on a particular day.

It pays to have an ongoing relationship

In this sort of routine order situation, it's very important to be one of the regular sources of supply. For straight rebuys, the buyer (or computer) may place an order without even considering other potential sources. However, if a buyer believes that there are several suppliers who could meet the specs, the buyer may request competitive bids. If different suppliers' quality, dependability, and delivery schedules all meet the specs, the buyer will select the low-price bid. But a creative marketer needs to look carefully at the purchaser's specs—and the need—to see if other elements of the marketing mix could provide a competitive advantage.

Sellers' sales reps (and perhaps whole teams of people) regularly call on these customers, but *not* to sell a particular item. Rather, they want to maintain relations, become a preferred source, or point out new developments that might cause the buyer to reevaluate the present straight rebuy procedure and give more business to the sales rep's company.

Variations in buying by customer type

We've been discussing aspects of relationships and e-commerce that generally apply with different types of customer organizations—in both the U.S. and internationally. However, it's also useful to have more detail about specific types of customers.

Manufacturers Are Important Customers

There are not many big ones

One of the most striking facts about manufacturers is how few there are compared to final consumers. This is true in every country. In the United States, for example, there are about 366,000 factories. Exhibit 7-8 shows that the majority of these are quite small—over half have less than 10 workers. But these small firms account for less than 3 percent of manufacturing value. In small plants, the owners often do the buying. And they buy less formally than buyers in the relatively few large manufacturing plants—which employ most of the workers and produce a large share of the value added by manufacturing. For example, plants with 250 or more employees make up less than 4 percent of the total—yet they employ nearly half of the production employees and produce about 61 percent of the value added by manufacturers.

In other countries, the size distribution of manufacturers varies. But across different countries, the same general conclusion holds: It is often desirable to segment industrial markets on the basis of customer size because large firms do so much of the buying.

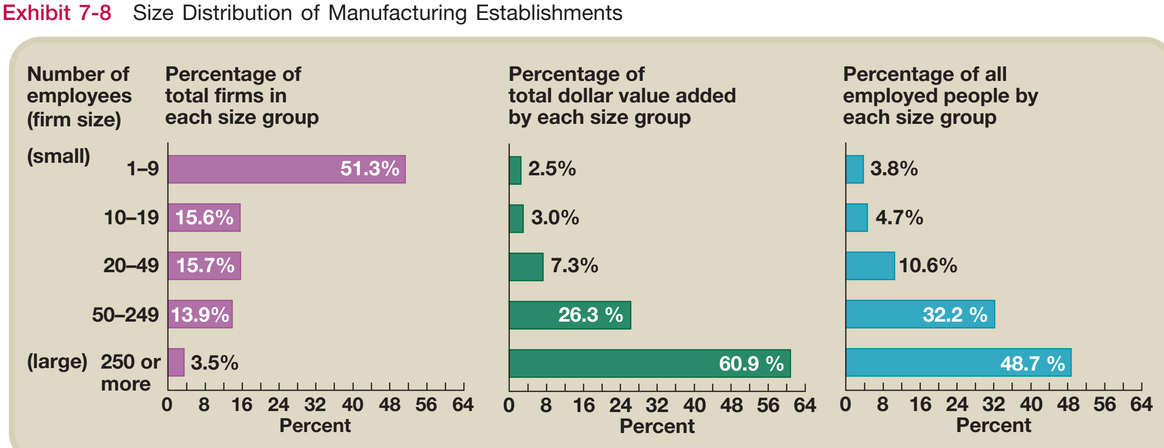
Customers cluster in geographic areas

In addition to concentration by company size, industrial markets are concentrated in certain geographic areas. Internationally, industrial customers are concentrated in countries that are at the more advanced stages of economic development. From all the talk in the news about the U.S. shifting from an industrial economy to a service economy or an information economy you might conclude that the U.S. is an exception—that the industrial market in this country is shrinking. But that's a myth. The U.S. is still the world's leading industrial economy. What's more, manufacturing output is higher than at any other time in the nation's history. So in a global sense, there is a high concentration of manufacturers in the U.S.

Within a country, there is often further concentration in specific areas. In the U.S., many factories are concentrated in big metropolitan areas—especially in New York, Pennsylvania, Ohio, Illinois, Texas, and California.[21]

There is also concentration by industry. In Germany, for example, the steel industry is concentrated in the Ruhr Valley. Similarly, U.S. manufacturers of high-tech electronics are concentrated in California's famous Silicon Valley near San Francisco and also along Boston's Route 128.

Exhibit 7-8 Size Distribution of Manufacturing Establishments





A firm like Alcoa Aluminum is likely to find that the majority of its customers are concentrated within a few industries that it can identify by Industry Classification System code number.

Business data often classifies industries

The products an industrial customer needs to buy depend on the business it is in. Because of this, sales of a product are often concentrated among customers in similar businesses. For example, apparel manufacturers are the main customers for buttons. Marketing managers who can relate their own sales to their customers' type of business can focus their efforts.

Detailed information is often available to help a marketing manager learn more about customers in different lines of business. The U.S. government collects and publishes data by the **North American Industry Classification System (NAICS) codes**—groups of firms in similar lines of business. (NAICS is pronounced like "nakes.") The number of establishments, sales volumes, and number of employees—broken down by geographic areas—are given for each NAICS code. A number of other countries collect similar data, and some of them try to coordinate their efforts with an international variation of the NAICS system. However, in many countries data on business customers is incomplete or inaccurate.

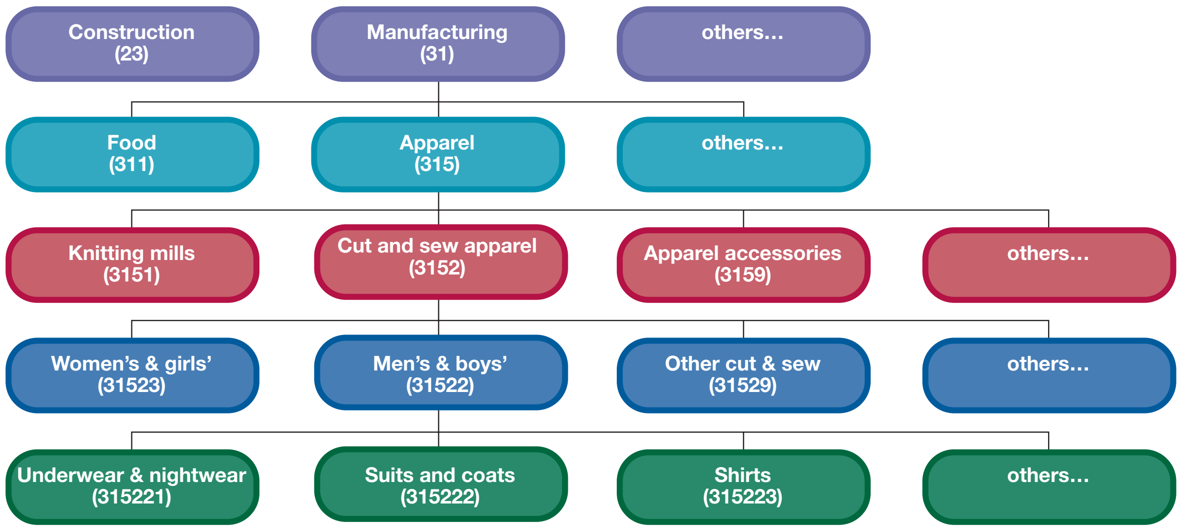
The NAICS is a recent development. The U.S. adopted it as a standard in 1997. However, it is being phased in over time. The phase-in makes it easier to use the system because in the past data were reported using Standard Industrial Classification (SIC) codes. Many of the codes are similar; check the website at www.naics.com for details. However, the move to the new system should help business marketers. The NAICS system is suited for identifying new or fast-changing industries—and for marketers that spells opportunity. NAICS is also more detailed than SIC and works better for services such as financial institutions, health care providers, and firms in the entertainment business. The general logic of NAICS and SIC is similar. So let's take a closer look at how the NAICS codes work.

The NAICS code breakdowns start with broad industry categories such as construction (23), manufacturing (31), wholesale trade (42), finance and insurance (52), and so on. Within each two-digit industry breakdown, much more detailed data may be available for three-digit industries (that is, subindustries of the

Internet

Internet Exercise Comprehensive information about NAICS codes is available online (www.naics.com). At the website select "Find Your NAICS Code" and when the search page appears submit a query for the keyword "welding." If your firm was interested in selling its lasers to manufacturers of laser welding equipment, what is the NAICS code of the industry for which you would want to get a list of manufacturers?

Exhibit 7-9 Illustrative NAICS Code Breakdown for Apparel Manufacturers



two-digit industries). For example, within the two-digit manufacturing industry (code 31) there are manufacturers of food (311), beverages and tobacco (312), and others, including apparel manufacturers (315). Then each three-digit group of firms is further subdivided into more detailed four-, five-, and six-digit classifications. For instance, within the three-digit (315) apparel manufacturers there are four-digit subgroups for knitting mills (3151), cut and sew firms (3152), and producers of apparel accessories (3159). Exhibit 7-9 illustrates that breakdowns are more detailed as you move to codes with more digits. However, detailed data (say, broken down at the four-digit level) isn't available for all industries in every geographic area. The government does not provide detail when only one or two plants are located in an area.

Many firms find their *current* customers' NAICS (or SIC) codes and then look at NAICS-coded lists for similar companies that may need the same goods and services. Other companies look at which NAICS categories are growing or declining to discover new opportunities.

If companies aiming at business target markets in the United States know exactly who they are aiming at, readily available data organized by NAICS (or SIC) codes can be valuable. Most trade associations and private organizations that gather data on business markets also use these codes.

The NAICS codes are an improvement over the old approach, but they are not perfect. Some companies have sales in several categories but are listed in only one—the code with the largest sales. In addition, some businesses don't fit any of the categories very well. So although a lot of good information is available, the codes must be used carefully.[22]

Producers of Services—Smaller and More Spread Out

Marketing managers need to keep in mind that the service side of the U.S. economy is large and has been growing fast. Service operations are also growing in some other countries. There may be good opportunities in providing these companies with the products they need to support their operations. But there are also challenges.

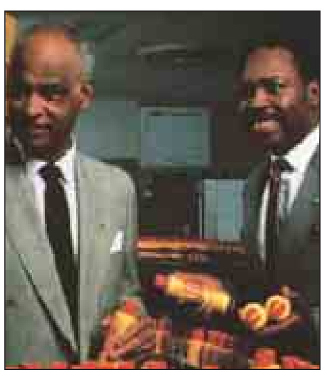
The United States has about 2.5 million service firms—over six times as many as it has manufacturers. Some of these are big companies with international operations. Examples include AT&T, Hilton Hotels, Prudential Insurance, CitiGroup, and EDS (Electronic Data Systems). These firms have purchasing departments that are like those in large manufacturing organizations. But as you might guess given the large number of service firms, most of them are small. They're also more spread out around the country than manufacturing concerns. Factories often locate where transportation facilities are good, raw materials are available, and it is less costly to produce goods in quantity. Service operations, in contrast, often have to be close to their customers.

Buying may not be as formal

Purchases by small service firms are often handled by whoever is in charge. This may be a doctor, lawyer, owner of a local insurance agency, or manager of a hotel. Suppliers who usually deal with purchasing specialists in large organizations may have trouble adjusting to this market. Personal selling is still an important part of promotion, but reaching these customers in the first place often requires more advertising. And small service firms may need much more help in buying than a large corporation.

Canon, the familiar name in office copiers, was very successful serving the needs of smaller service firms like law offices. Canon developed promotion materials to help first-time buyers understand differences in copiers. It emphasized that its machines were easy to use and maintain. And Canon also used retail channels to make the copiers available in smaller areas where there wasn't enough business to justify using a sales rep.[23]

Retailers and Wholesalers Buy for Their Customers



Most retail and wholesale buyers see themselves as purchasing agents for their target customers—remembering the old saying that "Goods well bought are half sold." Typically, retailers do *not* see themselves as sales agents for particular manufacturers. They buy what they think they can profitably sell. For example, the buying specialist at Walgreens Drugstores who handles products targeted at ethnic consumers is a real expert. He knows what ethnic customers want and won't be persuaded by a sales rep for a manufacturer who can't provide it. Of course, there is a place for collaboration, as when the Walgreens buyer works with people at Soft Sheen Products to develop a new product for the African American target market. That's profitable for both firms.

Similarly, wholesalers buy what they think their retailers can sell. In other words, they focus on the needs and attitudes of *their* target customers. For example, Super Valu—a leading food distributor in the U.S.—calls itself "the retail support company." As a top manager at Super Valu put it, "Our mandate is to try to satisfy our retailer customers with *whatever it takes*."[24]

Committee buying is impersonal

Some buyers—especially those who work for big retail chains—are annoyed by the number of wholesalers' and manufacturers' representatives who call on them. Space in their stores is limited and they simply are not interested in carrying every

Colgate and Carrefour executives in France work together to create mutually beneficial programs not only for the retailer's home country but for the many other countries where Carrefour is expanding.

product that some salesperson wants them to sell. Consider the problem facing grocery chains. In an average week, 150 to 250 new items are offered to the buying offices of a large chain like Safeway. If the chain accepted all of them, it would add 10,000 new items during a single year! Obviously, these firms need a way to deal with this overload.[25]

Decisions to add or drop lines or change buying policies may be handled by a *buying committee*. The seller still calls on and gives a pitch to a buyer—but the buyer does not have final responsibility. Instead, the buyer prepares forms summarizing proposals for new products and passes them on to the committee for evaluation. The seller may not get to present her story to the buying committee in person. This rational, almost cold-blooded approach certainly reduces the impact of a persuasive salesperson. On the other hand, it may favor a firm that has hard data on how its whole marketing mix will help the retailer to attract and keep customers.

Buyers watch computer output closely

Most larger firms now use sophisticated computerized inventory replenishment systems. Scanners at retail checkout counters keep track of what goes out the door—and computers use this data to update the records. Even small retailers and wholesalers use automated control systems that create daily reports showing sales of every product. Buyers with this kind of information know, in detail, the profitability of the different competing products. If a product isn't moving, the retailer isn't likely to be impressed by a salesperson's request for more in-store attention or added shelf space.

Reorders are straight rebuys

Retailers and wholesalers usually carry a large number of products. A drug wholesaler, for example, may carry up to 125,000 products. Because they deal with so many products, most middlemen buy their products on a routine, automatic reorder basis—straight rebuys—once they make the initial decision to stock specific items. Automatic computer ordering is a natural outgrowth of computerized checkout systems. Sellers to these markets must understand the size of the buyer's job and have something useful to say and do when they call.

Some are not "open to buy"

Retail buyers are sometimes controlled by a miniature profit and loss statement for each department or merchandise line. In an effort to make a profit, the buyer tries to forecast sales, merchandise costs, and expenses. The figure for "cost of merchandise" is the amount buyers have budgeted to spend over the budget period. If the money has not yet been spent, buyers are **open to buy**—that is, the buyers have budgeted funds that can be spent during the current period. However, if the budget has been spent, they are no longer in the market and no amount of special promotion or price-cutting is likely to induce them to buy.[26]

Buying and selling are closely related

In wholesale and retail firms, there is usually a very close relationship between buying and selling. Buyers are often in close contact with their firm's salespeople and with customers. The housewares buyer for a local department store, for example, may even supervise the salespeople who sell housewares. Salespeople are quick to tell the buyer if a customer wants a product that is not available—especially if the salespeople work on commission.

Resident buyers may help a firm's buyers

Resident buyers are independent buying agents who work in central markets (New York City, Paris, Rome, Hong Kong, Chicago, Los Angeles) for several retailer or wholesaler customers based in outlying areas or other countries. They buy new styles and fashions and fill-in items as their customers run out of stock during the year.

Resident buying organizations fill a need. They help small channel members (producers and middlemen) reach each other inexpensively. Resident buyers usually are paid an annual fee based on their purchases.

The Government Market

Size and diversity

Some marketers ignore the government market because they think that government red tape is more trouble than it's worth. They probably don't realize how big the government market really is. Government is the largest customer group in many countries—including the United States. About 35 percent of the U.S. gross national product is spent by various government units; the figure is much higher in some economies. Different government units in the United States spend about $2,866,000,000,000 (think about it!) a year to buy almost every kind of product. They run not only schools, police departments, and military organizations, but also supermarkets, public utilities, research laboratories, offices, hospitals, and even liquor stores. These huge government expenditures cannot be ignored by an aggressive marketing manager.

Competitive bids may be required

Government buyers in the United States are expected to spend money wisely—in the public interest—so their purchases are usually subject to much public review. To avoid charges of favoritism, most government customers buy by specification using a mandatory bidding procedure. Often the government buyer must accept the lowest bid that meets the specifications. You can see how important it is for the buyer to write precise and complete specifications. Otherwise, sellers may submit a bid that fits the specs but doesn't really match what is needed. By law, a government unit might have to accept the lowest bid—even for an unwanted product.

Writing specifications is not easy—and buyers usually appreciate the help of well-informed salespeople. Salespeople *want* to have input on the specifications so their product can be considered or even have an advantage. One company may get the business—even with a bid that is not the lowest—because the lower bids don't meet minimum specifications.

Government agencies are important customers for a wide variety of products, even rental truck services (for example, if they have to unexpectedly move ballot boxes from one place to another as was the case in Florida in the 2000 national election).

Rigged specs are an ethical concern

At the extreme, a government customer who wants a specific brand or supplier may try to write the description so that no other supplier can meet all the specs. The buyer may have good reasons for such preferences—a more reliable product, prompt delivery, or better service after the sale. This kind of loyalty sounds great, but marketers must be sensitive to the ethical issues involved. Laws that require government customers to get bids are intended to increase competition among suppliers, not reduce it. Specs that are written primarily to defeat the purpose of these laws may be viewed as illegal bid rigging.

The approved supplier list

Specification and bidding difficulties aren't problems in all government orders. Some items that are bought frequently—or for which there are widely accepted standards—are purchased routinely. The government unit simply places an order at a previously approved price. To share in this business, a supplier must be on the list of approved suppliers. The list is updated occasionally, sometimes by a bid procedure. Government units buy school supplies, construction materials, and gasoline this way. Buyers and sellers agree on a price that will stay the same for a specific period—perhaps a year.

Negotiated contracts are common too

Contracts may be negotiated for items that are not branded or easily described, for products that require research and development, or in cases where there is no effective competition. Depending on the government unit involved, the contract may be subject to audit and renegotiation, especially if the contractor makes a larger profit than expected.

Negotiation is often necessary when there are many intangible factors. Unfortunately, this is exactly where favoritism and influence can slip in. And such influence is not unknown—especially in city and state government. Nevertheless, negotiation is an important buying method in government sales—so a marketing mix should emphasize more than just low price.[27]

Learning what government wants

In the United States, there are more than 85,000 local government units (school districts, cities, counties, and states) as well as many federal agencies that make purchases. Keeping on top of all of them is nearly impossible. Potential suppliers should focus on the government units they want to cater to and learn the bidding methods of those units. Then it's easier to stay informed since most government contracts are advertised. Target marketing can make a big contribution here—making sure the marketing mixes are well matched with the different bidding procedures.

A marketer can learn a lot about potential government target markets from various government publications and by using the Internet. For example, there is an online government contractors' resource center at www.govcon.com. It includes a link to the online version of the U.S. federal government's *Commerce Business Daily*, which lists most current purchase bid requests. The Small Business Administration (www.sba.gov) offers many resources, including the *U.S. Purchasing, Specifications, and Sales Directory*. It explains government procedures to encourage competition for such business. Various state and local governments also offer guidance, as do government units in many other countries.

Trade magazines and trade associations provide information on how to reach schools, hospitals, highway departments, park departments, and so on. These are unique target markets and must be treated as such when developing marketing strategies.

Dealing with foreign governments

Selling to government units in foreign countries can be a real challenge. In many cases, a firm must get permission from the government in its own country to sell to a foreign government. Moreover, most government contracts favor domestic suppliers if they are available. Even if such favoritism is not explicit, public sentiment may make it very difficult for a foreign competitor to get a contract. Or the government bureaucracy may simply bury a foreign supplier in so much red tape that there's no way to win.

Is it unethical to "buy help"?

In some countries, government officials expect small payments (grease money) just to speed up processing of routine paperwork, inspections, or decisions from the local bureaucracy. Outright influence peddling—where government officials or their friends request bribe money to sway a purchase decision—is common in some markets. In the past, marketers from some countries have looked at such bribes as a cost of doing business. However, the **Foreign Corrupt Practices Act**, passed by the U.S. Congress in 1977, prohibits U.S. firms from paying bribes to foreign officials. A person who pays bribes, or authorizes an agent to pay them, can face stiff penalties. However, the law was amended in 1988 to allow small grease money payments if they are customary in a local culture. Further, a manager isn't held responsible if an agent in the foreign country secretly pays bribes. An ethical dilemma may arise if a marketing manager *thinks* that money paid to a foreign agent might be used, in part, to bribe a government official. However, most U.S. businesses have learned to live with this law—and in general they comply with its intent.[28]

Conclusion

In this chapter, we considered the number, size, location, and buying behavior of various types of organizational customers—to try to identify logical dimensions for segmenting markets and developing marketing mixes. We looked at who makes and influences organizational buying decisions, and how multiple influence may make the marketing job more difficult. We also saw that the nature of the buyer and the buying situation are relevant and that the problem-solving models of buyer behavior introduced in Chapter 6 apply here, with modifications.

Buying behavior—and marketing opportunities—may change when there's a close relationship between a supplier and a customer. However, close relationships are not an all-or-nothing thing. There are different ways that a supplier can build a closer relationship with its customers. We identified key dimensions of relationships and their benefits and limitations.

We also looked at how buyers use e-commerce in the buying process. Some capabilities, like interactive competitive bidding, have already had a major impact. And much progress is underway toward fostering more efficient relationships.

The chapter focuses on aspects of buying behavior that often apply to different types of organizational customers. However, we discussed some key differences in the manufacturer, services, middleman, and government markets.

A clear understanding of organizational buying habits, needs, and attitudes can aid marketing strategy planning. And since there are fewer organizational customers than final consumers, it may even be possible for some marketing managers (and their salespeople) to develop a unique strategy for each potential customer.

This chapter offers some general principles that are useful in strategy planning—but the nature of the products being offered may require adjustments in the plans. Different product classes are discussed in Chapter 9. Variations by product may provide additional segmenting dimensions to help a marketing manager fine-tune a marketing strategy.

Questions and Problems

1. In your own words, explain how buying behavior of business customers in different countries may have been a factor in speeding the spread of international marketing.
2. Compare and contrast the buying behavior of final consumers and organizational buyers. In what ways are they most similar and in what ways are they most different?
3. Briefly discuss why a marketing manager should think about who is likely to be involved in the buying center for a particular purchase. Is the buying center idea useful in consumer buying? Explain your answer.
4. If a nonprofit hospital were planning to buy expensive MRI scanning equipment (to detect tumors), who might be involved in the buying center? Explain your answer and describe the types of influence that different people might have.
5. Describe the situations that would lead to the use of the three different buying processes for a particular product—lightweight bumpers for a pickup truck.
6. Why would an organizational buyer want to get competitive bids? What are some of the situations when competitive bidding can't be used?
7. How likely would each of the following be to use competitive bids: *(a)* a small town that needed a road resurfaced, *(b)* a scouting organization that needed a printer to print its scouting handbook, *(c)* a hardware retailer that wants to add a new lawn mower line, *(d)* a grocery store chain that wants to install new checkout scanners, and *(e)* a sorority that wants to buy a computer to keep track of member dues? Explain your answers.
8. Discuss the advantages and disadvantages of just-in-time supply relationships from an organizational buyer's point of view. Are the advantages and disadvantages merely reversed from the seller's point of view?
9. Explain why a customer might be willing to work more cooperatively with a small number of suppliers rather than pitting suppliers in a competition against each other. Give an example that illustrates your points.
10. Would a tool manufacturer need a different marketing strategy for a big retail chain like Home Depot than for a single hardware store run by its owner? Discuss your answer.
11. How do you think a furniture manufacturer's buying habits and practices would be affected by the specific type of product to be purchased? Consider fabric for upholstered furniture, a lathe for the production line, cardboard for shipping cartons, and lubricants for production machinery.
12. Discuss the importance of target marketing when analyzing organizational markets. How easy is it to isolate homogeneous market segments in these markets?
13. Explain how NAICS codes might be helpful in evaluating and understanding business markets. Give an example.
14. Considering the nature of retail buying, outline the basic ingredients of promotion to retail buyers. Does it make any difference what kinds of products are involved? Are any other factors relevant?

15. The government market is obviously an extremely large one, yet it is often slighted or even ignored by many firms. Red tape is certainly one reason, but there are others. Discuss the situation and be sure to include the possibility of segmenting in your analysis.

16. Some critics argue that the Foreign Corrupt Practices Act puts U.S. businesses at a disadvantage when competing in foreign markets with suppliers from other countries that do not have similar laws. Do you think that this is a reasonable criticism? Explain your answer.

Suggested Cases

5. Republic Polymer Company

6. Three Rivers Steel Company

Computer-Aided Problem

7. **Vendor Analysis**

CompuTech, Inc., makes circuit boards for microcomputers. It is evaluating two possible suppliers of electronic memory chips.

The chips do the same job. Although manufacturing quality has been improving, some chips are always defective. Both suppliers will replace defective chips. But the only practical way to test for a defective chip is to assemble a circuit board and "burn it in"—run it and see if it works. When one chip on a board is defective at that point, it costs $2.00 for the extra labor time to replace it. Supplier 1 guarantees a chip failure rate of not more than 1 per 100 (that is, a defect rate of 1 percent). The second supplier's 2 percent defective rate is higher, but its price is lower.

Supplier 1 has been able to improve its quality because it uses a heavier plastic case to hold the chip. The only disadvantage of the heavier case is that it requires CompuTech to use a connector that is somewhat more expensive.

Transportation costs are added to the price quoted by either supplier, but Supplier 2 is further away so transportation costs are higher. And because of the distance, delays in supplies reaching CompuTech are sometimes a problem. To ensure that a sufficient supply is on hand to keep production going, CompuTech must maintain a backup inventory—and this increases inventory costs. CompuTech figures inventory costs—the expenses of finance and storage—as a percentage of the total order cost.

To make its vendor analysis easier, CompuTech's purchasing agent has entered data about the two suppliers on a spreadsheet. He based his estimates on the quantity he thinks he will need over a full year.

a. *Based on the results shown in the initial spreadsheet, which supplier do you think CompuTech should select? Why?*
b. *CompuTech estimates it will need 100,000 chips a year if sales go as expected. But if sales are slow, fewer chips will be needed. This isn't an issue with Supplier 2; its price is the same at any quantity. However, Supplier 1's price per chip will be $1.95 if CompuTech buys less than 90,000 during the year. If CompuTech only needs 84,500 chips, which supplier would be more economical? Why?*
c. *If the actual purchase quantity will be 84,500 and Supplier 1's price is $1.95, what is the highest price at which Supplier 2 will still be the lower-cost vendor for CompuTech? (Hint: You can enter various prices for Supplier 2 in the spreadsheet—or use the analysis feature to vary Supplier 2's price and display the total costs for both vendors.)*

For additional questions related to this problem, see Exercise 7-3 in the *Learning Aid for Use with Basic Marketing*, 14th edition.

When You Finish This Chapter, You Should

1. Know about marketing information systems.

2. Understand a scientific approach to marketing research.

3. Know how to define and solve marketing problems.

4. Know about getting secondary and primary data.

5. Understand the role of observing, questioning, and using experimental methods in marketing research.

6. Understand the important new terms (shown in red).

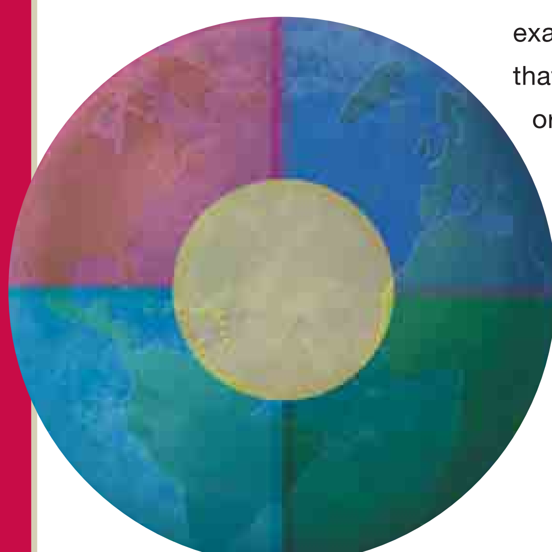
Chapter Eight

Improving Decisions with Marketing Information

With over 850 stores, LensCrafters has quickly become one of the largest chains of eyewear stores in the United States, Canada, and Puerto Rico.

A key to LensCrafters' success is that its managers use marketing research to better understand target market needs and to plan strategies. It's also easy for managers to get—and share—marketing information. That's because the company has its own intranet, and the information on it is constantly updated.

When LensCrafters was first evaluating the eye care market, a situation analysis revealed that there was a big opportunity. For example, library research revealed that 57 percent of people aged 18 or older wear eyeglasses, contact lenses, or both. Many also get sunglasses. Similarly, government statistics showed that demographic trends were favorable to long-run growth in the $10 billion a year eye care market.

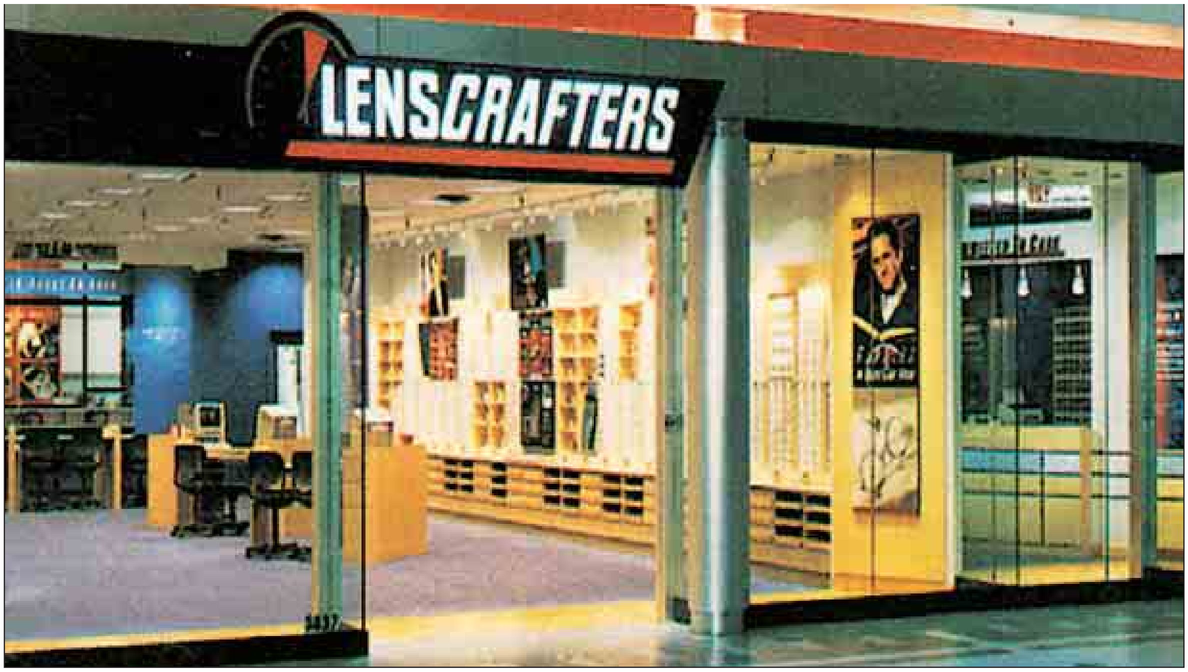


price

place

promotion

produc



Subsequent LensCrafters research provided guidance for turning this opportunity into a marketing strategy. Focus group interviews and consumer surveys confirmed that most consumers viewed shopping for glasses as very inconvenient. Frame selections were too small, opticians' shops were typically closed when customers were off work and had time to shop, and the whole process usually required long waits and repeat trips. So LensCrafters put the labs that make the glasses right in its stores and kept the stores open nights and weekends. Ads tout LensCrafters' high-quality, one-hour service. With LensCrafters' new, patented Accu-Fit Measuring System, customers are assured of a perfect-fitting pair of glasses.

To be sure that service quality lives up to the advertising promises, LensCrafters sends a customer satisfaction survey to every customer. Surveys are analyzed by store and used to find out what's going on where. LensCrafters even ties satisfaction results to employee bonuses.

To make it convenient for more consumers to shop at LensCrafters, the chain has been aggressively opening new stores. The firm's Internet website (www.lenscrafters.com) offers a store locator. Because the size and growth rate of various age groups in a geographic market drive demand for vision products, LensCrafters analyzes demographic data to locate new stores where profit potential is greatest. And each store carries a very large selection of frame styles, lenses, and sunglasses tailored to the age, gender, and ethnic makeup of the local market.

Managers at LensCrafters also routinely analyze sales data that is available in the firm's marketing information system. By breaking down sales by product, store, and time period, they can spot buying trends early and plan for them.

Research also guides promotion decisions. For example, LensCrafters uses direct-mail advertising targeted to customers in segments where interest in its convenient eyeglass service is highest.

LensCrafters' new advertising and positioning is also based on research. The campaign is designed to encourage consumers to think of LensCrafters as "my personal vision place." The ads speak to the importance and value of vision care and foster LensCrafters' identity as the consumer's first choice for quality eye care and quality eyewear. The research shows that this message appeals to consumers and sets LensCrafters apart from competitors—who mainly rely on price-oriented messages about discounts and price points.[1]

The LensCrafters case shows that successful marketing strategies require information about potential target markets and their likely responses to marketing mixes as well as about competition and other marketing environment variables. Managers also need information for implementation and control. Without good information, managers are left to guess—and in today's fast-changing markets, that invites failure.

Radical Changes Are Underway in Marketing Information

Marketing managers for some companies make decisions based almost totally on their own judgment—with very little hard data. The manager may not even know that he or she is about to make the same mistake that the previous person in that job already made! When it's time to make a decision, they may wish they had more information. But by then it's too late, so they do without.

MIS makes information available and accessible

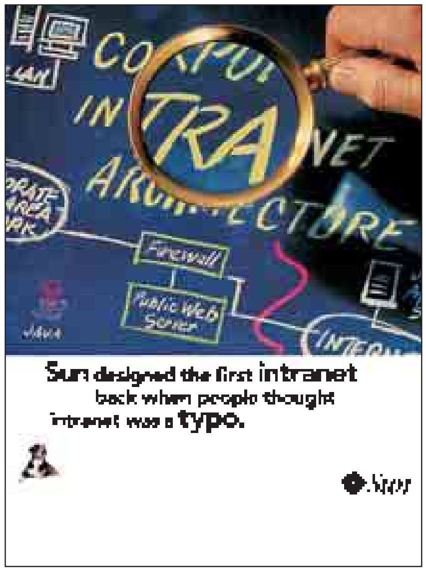
There is a difference between information that is *available* and information that is readily *accessible*. Some information—such as the details of competitors' plans—is just not available. Other information may be available, but not really accessible without a time-consuming effort. For example, a company may have file cabinets full of records of customer purchases, what was sold by sales reps last month, past marketing plans, or what is in the warehouse. In a sense, all of this information is available. But, if a manager can't quickly get this information when it's needed, it isn't useful. By contrast, making the same information instantly accessible over a computer network could be very useful.

Firms like LensCrafters realize that it doesn't pay to wait until you have important questions you can't answer. They anticipate the information they will need. They work to develop a *continual flow of information* that is available and quickly accessible when it's needed.

A **marketing information system (MIS)** is an organized way of continually gathering, accessing, and analyzing information that marketing managers need to make decisions.

We won't cover all of the technical details of planning for an MIS. That's beyond the scope of this course. But you should understand what an MIS is so you know some of the possibilities. So, we'll be discussing the elements of a complete MIS as

New developments in computer networks and software are making it easier for companies to gather and analyze marketing information.

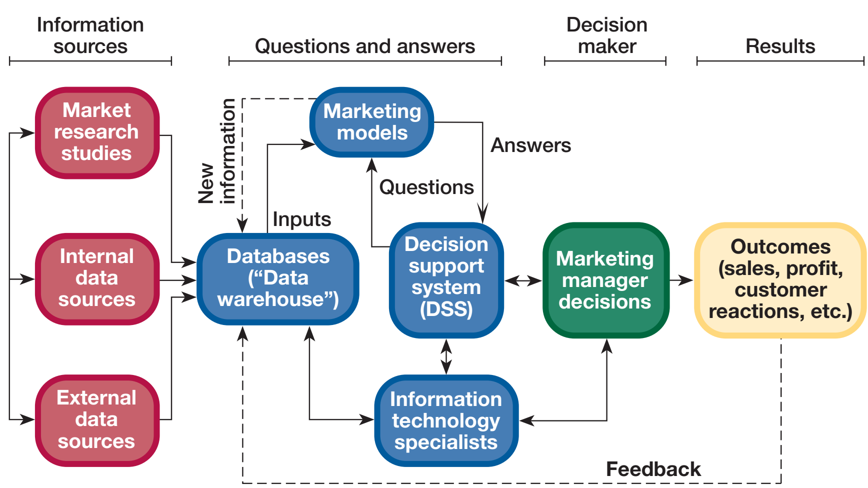


shown in Exhibit 8-1. As part of that review, we'll highlight how technology is changing MIS use.

Get more information—faster and easier

Basic MIS concepts are not very different today than they were 20 years ago. However, recent developments in information technology are having a *radical* impact on what information is available to marketing managers and how quickly. A big difference today is how easy it is to set up and use an MIS. A short time ago, connecting remote computers or exchanging data over networks was very difficult. Now, it's standard. And even a manager with little computer experience can quickly learn to use an MIS. As a result, managers everywhere have access to much more information. It's instantly available, and often just a mouse click away.

Exhibit 8-1
Elements of a Complete Marketing Information System



Equally important, the *type* of information available is changing dramatically. As recently as 1995, most marketing managers with information needs relied on computers mainly for number crunching. The multimedia revolution in computing has quickly lifted that limitation. Now it doesn't matter whether marketing information takes the form of a marketing plan, report, memo, spreadsheet, database, presentation, photo, graphic, or table of statistics. It is all being created on computer. So it can be easily stored and accessed by computer. Moreover, programs exist to help find whatever information is available—even if it is "lost" on the computer hard drive of a manager in an office across the ocean. When we talk about a database of marketing information, keep in mind that it may include all types of information, not just numbers.

An intranet is easy to update

We covered some of the important ways that the Internet is making more information available and changing marketing. In addition, many firms, even very small ones, have their own **intranet**—a system for linking computers within a company. An intranet works like the Internet. However, to maintain security, access to websites on an intranet is usually limited to employees. Even so, information is available on demand. Further, it's a simple matter to "publish" new information to a website as it becomes available. So, information can be constantly updated. Prior to this decade managers could only dream about this sort of capability.

Information technology is expanding what an MIS can do and how well it works. Even so, you seldom have all the information you need. Both customers and competitors can be unpredictable. Getting the precise information you want may cost too much or take too long. For example, data on international markets is often incomplete, outdated, or difficult to obtain. So a manager often must decide what information is really critical and how to get it.

Marketing managers must help develop an MIS

Computers are getting easier to use, but setting up and supporting an MIS still requires technical skill. In fact, converting an existing MIS to take advantage of Internet capabilities can be a real challenge. So in some companies, an MIS is set up by a person or group that provides *all* departments in the firm with information technology support. Or it may be set up by marketing specialists.

These specialists are important, but the marketing manager should play an important role, too. Marketing managers may not know in advance exactly what questions they will have or when. But they do know what data they've routinely used or needed in the past. They can also foresee what types of data might be useful. They should communicate these needs to the specialists so the information will be there when they want it and in the form they want it.

Decision support systems put managers online

An MIS system organizes incoming information into a **data warehouse**—a place where databases are stored so that they are available when needed. You can think of a data warehouse as a sort of electronic library, where all of the information is indexed extremely well. Firms with an MIS often have information technology specialists who help managers get specialized reports and output from the warehouse. However, to get better decisions, most MIS systems now provide marketing managers with a decision support system. A **decision support system (DSS)** is a computer program that makes it easy for a marketing manager to get and use information *as he or she is making decisions*.

A decision support system usually involves some sort of **search engine**—a computer program that helps a marketing manager find information that is needed. Often, the manager provides a word or phrase to guide the search. For example, a manager who wants sales data for the previous week or day might search for any database or computer file that references the term *unit sales* as well as the relevant data. The search engine would identify any files where that term appeared. If there were many, the manager could narrow the search further (say by specifying the product of interest), or the manager could briefly review the files to find the most appropriate one.

When the search is focused on numerical data, simply finding the information may not go far enough. Thus, a DSS typically helps change raw data—like product sales for the previous day—into more *useful information*. For example, it may draw graphs to show relationships in data—perhaps comparing yesterday's sales to the sales on the same day in the last four weeks. The MIS that managers at Frito-Lay use illustrates the possibilities.

All of Frito-Lay's salespeople are equipped with hand-held computers. Throughout the day they input sales information at the stores they visit. In the evening they send all the data over telephone lines to a central computer, where it is analyzed. Within 24 hours marketing managers at headquarters and in regional offices get reports and graphs that summarize how sales went the day before—broken down by brands and locations. The information system even allows a manager to zoom in and take a closer look at a problem in Peoria or a sales success in Sacramento.[2]

Some decision support systems go even further. They allow the manager to see how answers to questions might change in various situations. For example, a manager at Kraft Foods may want to estimate how much sales will increase if the firm uses a certain type of promotion in a specific market area. The DSS will ask the manager for a *personal* judgment about how much business could be won from each competitor in that market. Then, using this input and drawing on data in the database about how the promotion had worked in other markets, the system will make a sales estimate using a marketing model. A **marketing model** is a statement of relationships among marketing variables.

In short, the decision support system puts managers online so they can study available data and make better marketing decisions—faster.[3]

Information makes managers greedy for more

Once marketing managers see how a functioning MIS—and perhaps a DSS—can help their decision making, they are eager for more information. They realize that they can improve all aspects of their planning—blending individual Ps, combining the four Ps into mixes, and developing and selecting plans. Further, they can monitor the implementation of current plans, comparing results against plans and making necessary changes more quickly. (Note: The sales and cost analysis techniques discussed in Chapter 18 are often used in an MIS.) Marketing information systems will become more widespread as managers become more sensitive to the possibilities and as more information is available in a form that makes it easy to transfer from one computer program format to another. This may seem like a small problem, but it has been a big stumbling block for many firms.

Many firms are not there yet

Of course, not every firm has a complete MIS system. And in some firms that do, managers don't know how to use what's there. A major problem is that many managers are used to doing it the old way—and they don't think through what information they need.

One sales manager thought he was progressive when he asked his assistant for a report listing each sales rep's sales for the previous month and the current month. The assistant quickly found the relevant information on the firm's intranet, put it into an Excel spreadsheet, and printed out the report. Later, however, she was surprised to see the sales manager working on the list with a calculator. He was figuring the percentage change in sales for the month and ranking the reps from largest increase in sales to smallest. The spreadsheet software could have done all of that—instantly—but the sales manager got what he *asked for*, not what he really needed. An MIS can provide information—but only the marketing manager knows what problem needs solving. It's the job of the manager—not the computer or the MIS specialist—to ask for the right information in the right form.

MIS use is growing rapidly

Some people think that only large firms can develop an effective MIS. In fact, just the opposite may be true. Big firms with complicated marketing programs often face a challenge trying to develop an MIS from scratch. And once a large firm has a system in place it may be very costly to switch to something better. It can be easier for small firms because they are often more focused. They can get started with a simple system and then expand it as needs expand. There is a lot of opportunity in this area for students who are able and willing to apply computer skills to solve real marketing problems.[4]

New questions require new answers

MIS systems tend to focus on recurring information needs. Routinely analyzing such information can be valuable to marketing managers. But it shouldn't be their only source of information for decision making. They must try to satisfy ever-changing needs in dynamic markets. So marketing research must be used—to supplement data already available and accessible through the MIS.

What Is Marketing Research?

Research provides a bridge to customers

The marketing concept says that marketing managers should meet the needs of customers. Yet today, many marketing managers are isolated in company offices—far from potential customers.

This means marketing managers have to rely on help from **marketing research**—procedures to develop and analyze new information to help marketing managers make decisions. One of the important jobs of a marketing researcher is to get the "facts" that are not currently available in the MIS.

Who does the work?

Most large companies have a separate marketing research department to plan and carry out research projects. These departments often use outside specialists—including interviewing and tabulating services—to handle technical assignments. Further, they may call in specialized marketing consultants and marketing research organizations to take charge of a research project.

Small companies (those with less than $4 or $5 million in sales) usually don't have separate marketing research departments. They often depend on their sales people or managers to conduct what research they do.

Some nonprofit organizations have begun to use marketing research—usually with the help of outside specialists. For example, many politicians rely on research firms to conduct surveys of voter attitudes.[5]

Ethical issues in marketing research

The basic reason for doing marketing research is to get information that people can trust in making decisions. But as you will see in this chapter, research often involves many hidden details. A person who wants to misuse marketing research to pursue a personal agenda can often do so.

Perhaps the most common ethical issues concern decisions to withhold certain information about the research. For example, a manager might selectively share only those results that support his or her viewpoint. Others involved in a decision might never know that they are getting only partial truths. Or during a set of interviews, a researcher may discover that consumers are interpreting a poorly worded question many different ways. If the researcher doesn't admit the problem, an unknowing manager may rely on meaningless results.

Another problem involves more blatant abuses. It is unethical for a firm to contact consumers under the pretense of doing research when the real purpose is to sell something. For example, some political organizations have been criticized for surveying consumers to find out their attitudes about various political candidates and

Developments in information technology are making it easier to gather information about customers, but marketers need to be sensitive to concerns that some consumers and critics have about privacy. Zero-Knowledge, the Canadian company featured here, positions itself as the "consumer's advocate on privacy."

issues. Then, armed with that information, someone else calls back to solicit donations. Legitimate marketing researchers don't do this!

The relationship between the researcher and the manager sometimes creates an ethical conflict. Managers must be careful not to send a signal that the only acceptable results from a research project are ones that confirm their existing viewpoints. Researchers are supposed to be objective, but that objectivity may be swayed if future jobs depend on getting the "right" results.[6]

Effective research usually requires cooperation

Good marketing research requires cooperation between researchers and marketing managers. Researchers must be sure their research focuses on real problems.

Marketing managers must be able to explain what their problems are and what kinds of information they need. They should be able to communicate with specialists in the specialists' language. Marketing managers may only be "consumers" of research. But they should be informed consumers—able to explain exactly what they want from the research. They should also know about some of the basic decisions made during the research process so they know the limitations of the findings.

For this reason, our discussion of marketing research won't emphasize mechanics but rather how to plan and evaluate the work of marketing researchers.[7]

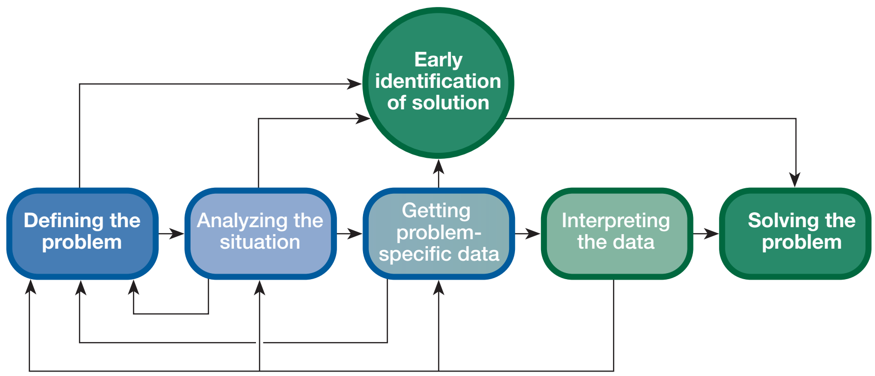
The Scientific Method and Marketing Research

The scientific method—combined with the strategy planning framework we discussed in Chapter 2—can help marketing managers make better decisions.

The **scientific method** is a decision-making approach that focuses on being objective and orderly in *testing* ideas before accepting them. With the scientific method, managers don't just *assume* that their intuition is correct. Instead, they use their intuition and observations to develop **hypotheses**—educated guesses about the relationships between things or about what will happen in the future. Then they test their hypotheses before making final decisions.

A manager who relies only on intuition might introduce a new product without testing consumer response. But a manager who uses the scientific method might say, "I think (hypothesize) that consumers currently using the most popular brand will prefer our new product. Let's run some consumer tests. If at least 60 percent of the

Exhibit 8-2
Five-Step Scientific Approach to Marketing Research Process



consumers prefer our product, we can introduce it in a regional test market. If it doesn't pass the consumer test there, we can make some changes and try again."

The scientific method forces an orderly research process. Some managers don't carefully specify what information they need. They blindly move ahead—hoping that research will provide "the answer." Other managers may have a clearly defined problem or question but lose their way after that. These hit-or-miss approaches waste both time and money.

Five-Step Approach to Marketing Research

The **marketing research process** is a five-step application of the scientific method that includes:

1. Defining the problem.
2. Analyzing the situation.
3. Getting problem-specific data.
4. Interpreting the data.
5. Solving the problem.

Exhibit 8-2 shows the five steps in the process. Note that the process may lead to a solution before all of the steps are completed. Or as the feedback arrows show, researchers may return to an earlier step if needed. For example, the interpreting step may point to a new question—or reveal the need for additional information—before a final decision can be made.

Defining the Problem—Step 1

Defining the problem is often the most difficult step in the marketing research process. But it's important for the objectives of the research to be clearly defined. The best research job on the wrong problem is wasted effort.

Finding the right problem level almost solves the problem

The strategy planning framework introduced in Chapter 2 can be useful here. It can help the researcher identify the real problem area and what information is needed. Do we really know enough about our target markets to work out all of the four Ps? Do we know enough to decide what celebrity to use in an ad or how to handle a price war in New York City or Tokyo? If not, we may want to do research rather than rely on intuition.

The importance of understanding the problem—and then trying to solve it—can be seen in the introduction of Fab One Shot, a laundry product developed to clean, soften, and reduce static cling all in one step. Marketing managers were sure that Fab One Shot was going to appeal to heavy users—especially working women with large families. Research showed that 80 percent of these women used three different laundry products for the family wash, but they were looking for more convenience.

When marketing managers found that other firms were testing similar products, they rushed Fab One Shot into distribution. To encourage first-time purchases, they offered introductory price discounts, coupons, and rebates. And they supported the sales promotion with heavy advertising on TV programs that research showed the heavy users watched.

However, research never addressed the problem of how the heavy user target market would react. After the introductory price-off deals were dropped, sales dropped off too. While the product was convenient, heavy users weren't willing to pay the price—about 25 cents for each washload. For the heavy users, price was a qualifying dimension. And these consumers didn't like Fab's premeasured packets because they had no control over how much detergent they could put in. The competing firms recognized these problems at the research stage and decided not to introduce their products.

After the fact, it was clear that Fab One Shot was most popular with college students, singles, and people living in small apartments. They didn't use much—so the convenience benefit offset the higher price. But the company never targeted those segments. It just assumed that it would be profitable to target the big market of heavy users.[8]

The moral of this story is that our strategy planning framework is useful for guiding the problem definition step—as well as the whole marketing research process. First, a marketing manager should understand the target market and what needs the firm can satisfy. Then the manager can focus on lower-level problems—namely, how sensitive the target market is to a change in one or more of the marketing mix ingredients. Without such a framework, marketing researchers can waste time, and money, working on the wrong problem.

Don't confuse problems with symptoms

The problem definition step sounds simple—and that's the danger. It's easy to confuse symptoms with the problem. Suppose a firm's MIS shows that the company's sales are decreasing in certain territories while expenses are remaining the same—resulting in a decline in profits. Will it help to define the problem by asking: How can we stop the sales decline? Probably not. This would be like fitting a hearing-impaired patient with a hearing aid without first trying to find out *why* the patient was having trouble hearing.

It's easy to fall into the trap of mistaking symptoms for the problem. When this happens, the research objectives are not clear, and researchers may ignore relevant questions—while analyzing unimportant questions in expensive detail.

Setting research objectives may require more understanding

Sometimes the research objectives are very clear. A manager wants to know if the targeted households have tried a new product and what percent of them bought it a second time. But research objectives aren't always so simple. The manager might also want to know *why* some didn't buy or whether they had even heard of the product. Companies rarely have enough time and money to study everything. A manager must narrow the research objectives. One good way is to develop a list of research questions that includes all the possible problem areas. Then the manager can consider the items on the list more completely—in the situation analysis step—before narrowing down to final research objectives.

Analyzing the Situation—Step 2

What information do we already have?

When the marketing manager thinks the real problem has begun to surface, a situation analysis is useful. A **situation analysis** is an informal study of what information is already available in the problem area. It can help define the problem and specify what additional information, if any, is needed.

Pick the brains around you

The situation analysis usually involves informal talks with informed people. Informed people can be others in the firm, a few good middlemen who have close contact with customers, or others knowledgeable about the industry. In industrial markets—where relationships with customers are close—researchers may even call the customers themselves.

Situation analysis helps educate a researcher

The situation analysis is especially important if the researcher is a research specialist who doesn't know much about the management decisions to be made or if the marketing manager is dealing with unfamiliar areas. They both must be sure they understand the problem area—including the nature of the target market, the marketing mix, competition, and other external factors. Otherwise, the researcher may rush ahead and make costly mistakes or simply discover facts that management already knows. The following case illustrates this danger.

A marketing manager at the home office of a large retail chain hired a research firm to do in-store interviews to learn what customers liked most, and least, about some of its stores in other cities. Interviewers diligently filled out their questionnaires. When the results came in, it was apparent that neither the marketing manager nor the researcher had done their homework. No one had even talked with the local store managers! Several of the stores were in the middle of some messy remodeling—so all the customers' responses concerned the noise and dust from the construction. The research was a waste of money.

Secondary data may provide the answers—or some background

The situation analysis should also find relevant **secondary data**—information that has been collected or published already. Later, in Step 3, we will cover **primary data**—information specifically collected to solve a current problem. Too often researchers rush to gather primary data when much relevant secondary information is already available—at little or no cost! See Exhibit 8-3.

Much secondary data is available

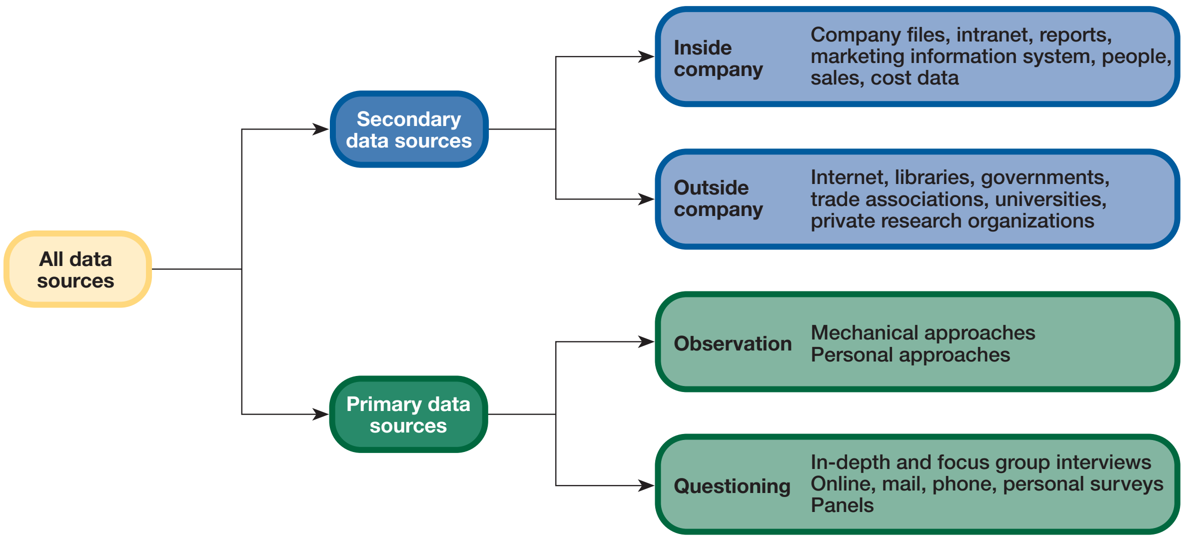
Ideally, much secondary data is already available from the firm's MIS. Data that has not been organized in an MIS may be available from the company's files and reports. Secondary data also is available from libraries, trade associations, government agencies, and private research organizations; increasingly, these organizations are putting their information online. So one of the first places a researcher should look for secondary data is on the Internet.

Search engines find information on the Internet

Although much information relevant to your situation analysis may be on the Internet, it won't do you much good if you can't find it. Fortunately, there are a number of good tools for searching on the Internet and reference books that explain the details of the different tools. However, the basic idea is simple. And, usually, the best way to start is to use a search engine.

Most popular Internet browsers, like Netscape Navigator and Microsoft Internet Explorer, have a menu selection or button to activate an Internet search. In addition, there are hundreds of more specialized search engines. In general a user specifies words or a phrase to find and the search engine produces a list of hyperlinks to websites where that search string is found. Usually all you do is type in the search string, click on search, wait while the reference list of links is assembled, and

Exhibit 8-3 Sources of Secondary and Primary Data



then click on the hyperlink of interest. Then the browser shows the relevant page for that hyperlink on screen. If you want, you can go back to the list and check out another hyperlink.

One of the most popular and useful search engines is at the website for Yahoo (www.yahoo.com). It is especially good at searching for web pages. Another very useful search engine is at the AltaVista website (www.altavista.digital.com); it does a good job of classifying online documents that include the search string. A search engine that is particularly useful for locating specific people or businesses is at www.hotbot.lycos.com. The Northern Light search engine (www.northernlight.com) is very good at identifying published articles on the search topic. Keep in mind, however, that these are just a few of the popular search engines. In fact, if you want to get an idea of how many are available—and how they are different—go to www.yahoo.com and do a search on the term *search engine*.[9]

Most computerized database and index services are now available over the Internet. Some of these are provided by libraries and private firms. For instance, for a fee a user can use Dow Jones' interactive news retrieval system (www.djnr.com) to search the full text of hundreds of publications, including newspapers from around the world. ProQuest Direct, at www.proquest.com, is another valuable research tool. It provides access to one of the world's largest collections of information, including summaries of articles from over 5,000 publications. Many articles are available in full text, full image format.

Internet

Internet Exercise Assume that your boss has asked you to do a customer satisfaction survey. As part of a situation analysis, you want to get ideas about what others have done in this area. Go to the website for the Yahoo search engine (www.yahoo.com). In the dialogue box type 'customer satisfaction survey' (include the single quote marks) and click on search. Look at some of the websites identified. How helpful is this? How could it be improved?

The Internet is dramatically changing how marketing managers get both primary and secondary data.

Government data is inexpensive

Federal and state governments publish data on many subjects. Government data is often useful in estimating the size of markets. In Chapter 5 we gave a number of examples of the different types of data that are available and suggested websites. Distribution of government data is not limited to the Internet, however. Almost all government data is available in inexpensive publications. Much of it is also available in computer form ready for further analysis.

Sometimes it's more practical to use summary publications for leads to more detailed reports. For the U.S. market, one of the most useful summary references is the *Statistical Abstract of the United States*. Like an almanac, it is issued in print form each year and gives 1,500 summary tables from more than 200 published sources. Detailed footnotes guide readers to more specific information on a topic. The abstract and much of the source material on which it is based are available online at www.census.gov. Similarly, the *United Nations Statistical Yearbook* is one of the finest summaries of worldwide data; like many other international statistical references, it is available on CD-ROM and online (www.un.org/depts/unsd).

Secondary data is very limited on some international markets. However, most countries with advanced economies have government agencies that help researchers get the data they need. For example, Statistics Canada (www.statcan.ca) compiles a great deal of information on the Canadian market. Eurostat (europa.eu.int/comm/eurostat), the statistical office for the European Union countries, and the Organization for Economic Cooperation (in Paris) offer many publications packed with data on Europe. In the United States, the Department of Commerce (www.doc.gov) distributes statistics compiled by all other federal departments. Some city and state governments have similar agencies for local data. The Yahoo website (www.yahoo.com) provides an index to a large amount of information about different governments.

Private sources are useful too

Many private research organizations—as well as advertising agencies, newspapers, and magazines—regularly compile and publish data. A good business library is valuable for sources such as *Sales & Marketing Management*, *Advertising Age*, *Journal of Global Marketing*, and the publications of the National Industrial Conference Board.

The *Encyclopedia of Associations* lists 75,000 U.S. and international trade and professional associations that can be a good source of information. For example, the American Marketing Association (www.ama.org) has an information center with many marketing publications.

Much of the information that a marketing manager needs to solve a problem may already be available, if the manager knows where to look. Specialized research firms, like Intelligence Data, can help in that search.

Most trade associations compile data from and for their members. Some also publish magazines that focus on important topics in the industry. *Chain Store Age*, for example, has much information on retailing (www.chainstoreage.com).

Standard & Poor's Industry Surveys is another source of information on whole industries. And the local telephone company or your library usually has copies of the Yellow Pages for many cities; Yellow Page listings are also available on the Internet. Similarly, a number of firms sell computer CD-ROMs that include all of the businesses in the country. Resources such as these may be a big help in estimating the amount of competition in certain lines of business and where it is located.[10]

Situation analysis yields a lot—for very little

The virtue of a good situation analysis is that it can be very informative but takes little time. And it's inexpensive compared with more formal research efforts—like a large-scale survey. Situation analysis can help focus further research or even eliminate the need for it entirely. The situation analyst is really trying to determine the exact nature of the situation and the problem.

Determine what else is needed

At the end of the situation analysis, you can see which research questions—from the list developed during the problem definition step—remain unanswered. Then you have to decide exactly what information you need to answer those questions and how to get it.

This may require discussion between technical experts and the marketing manager. Often companies use a written **research proposal**—a plan that specifies what information will be obtained and how—to be sure no misunderstandings occur later. The research plan may include information about costs, what data will be collected, how it will be collected, who will analyze it and how, and how long the process will take. Then the marketing manager must decide if the time and costs involved are worthwhile. It's foolish to pay $100,000 for information to solve a $50,000 problem!

Getting Problem-Specific Data—Step 3

Gathering primary data

The next step is to plan a formal research project to gather primary data. There are different methods for collecting primary data. Which approach to use depends on the nature of the problem and how much time and money are available.

In most primary data collection, the researcher tries to learn what customers think about some topic or how they behave under some conditions. There are two basic methods for obtaining information about customers: *questioning* and *observing*. Questioning can range from qualitative to quantitative research. And many kinds of observing are possible.

When John Deere does focus group research for its bulldozer line, customers have a chance to see and discuss what's different about Deere's product.

Qualitative questioning—open-ended with a hidden purpose

Qualitative research seeks in-depth, open-ended responses, not yes or no answers. The researcher tries to get people to share their thoughts on a topic—without giving them many directions or guidelines about what to say.

A researcher might ask different consumers, "What do you think about when you decide where to shop for food?" One person may talk about convenient location, another about service, and others about the quality of the fresh produce. The real advantage of this approach is *depth*. Each person can be asked follow-up questions so the researcher really understands what *that* respondent is thinking. The depth of the qualitative approach gets at the details—even if the researcher needs a lot of judgment to summarize it all.

Some types of qualitative research don't use specific questions. For example, a consumer might simply be shown a product or an ad and be asked to comment.

Focus groups stimulate discussion

The most widely used form of qualitative questioning in marketing research is the **focus group interview,** which involves interviewing 6 to 10 people in an informal group setting. The focus group also uses open-ended questions, but here the interviewer wants to get group interaction—to stimulate thinking and get immediate reactions.

A skilled focus group leader can learn a lot from this approach. A typical session may last an hour, so participants can cover a lot of ground. Sessions are often videotaped (or broadcast over the Internet or by satellite) so different managers can form their own impressions of what happened. Some research firms create electronic focus groups in which participants log onto a specified website and with others participate in a chat session; each person types in comments that are shared on the computer screen of each of the other participants. What they type is the record of the session.[11]

Regardless of how a focus group is conducted, conclusions reached from a session usually vary depending on who watches it. A typical problem—and serious limitation—with qualitative research is that it's hard to measure the results objectively. The results seem to depend so much on the viewpoint of the researcher. In addition, people willing to participate in a focus group—especially those who talk the most—may not be representative of the broader target market.

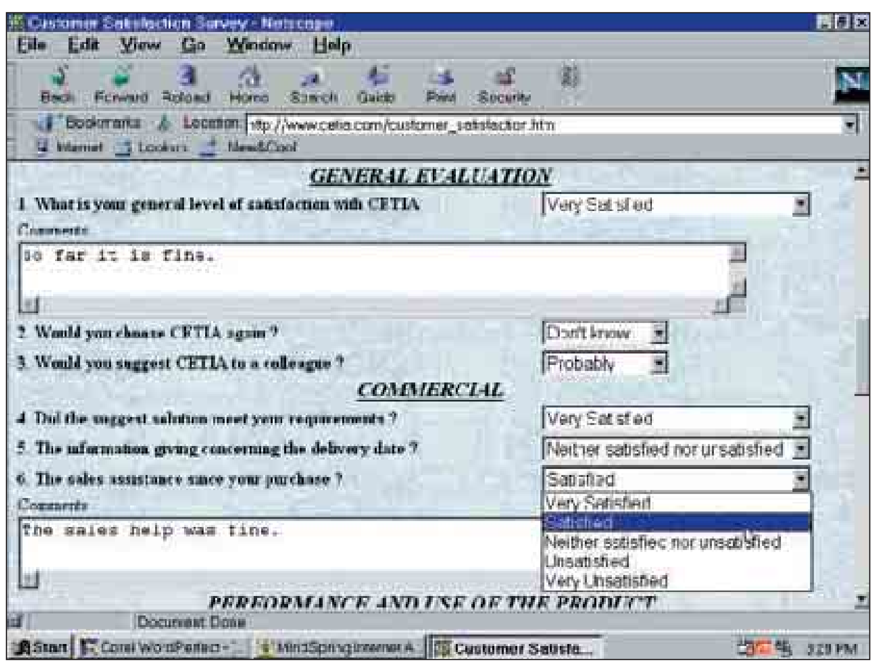
Focus groups can be conducted quickly and at relatively low cost—an average of about $3,500 each. This is part of their appeal. But focus groups are probably being overused. It's easy to fall into the trap of treating an idea arising from a focus group as a "fact" that applies to a broad target market. For example, it's trendy for food product firms in Japan to do focus groups with teenage girls. The logic is that girls will be brutally honest about what they think and that they are good at predicting what will be a hit. So based on a girl's comments in a focus group, Meiji Milk Products substituted oolong tea for fruit juice in a new drink it was developing. The suggested change might or might not be a good one. But there's no way to know if one girl's point of view is representative.[12]

To avoid this trap, some researchers use qualitative research to prepare for quantitative research. For example, the Jacksonville Symphony Orchestra wanted to broaden its base of support and increase ticket sales. It hired a marketing research firm to conduct focus group interviews. These interviews helped the marketing managers refine their ideas about what these target "customers" liked and did not like about the orchestra. The ideas were then tested with a larger, more representative sample. Interviewers telephoned 500 people and asked them how interested they would be in various orchestra programs, event locations, and guest artists. Then they planned their promotion and the orchestra's program for the year based on the research. Ticket sales nearly doubled.[13]

As this example suggests, qualitative research can provide good ideas—hypotheses. But we need other approaches—perhaps based on more representative samples and objective measures—to *test* the hypotheses.

Structured questioning gives more objective results

When researchers use identical questions and response alternatives, they can summarize the information quantitatively. Samples can be larger and more representative, and various statistics can be used to draw conclusions. For these reasons, most survey research is **quantitative research**—which seeks structured responses that can be summarized in numbers, like percentages, averages, or other statistics. For example, a marketing researcher might calculate what percentage of respondents have tried a new product and then figure an average score for how satisfied they were.



CETIA is a European manufacturer of minicomputers. When it delivers a product, it asks the customer to complete this interactive customer satisfaction survey, which is located at CETIA's Internet website. The survey uses a combination of fixed response questions and open-ended comments.

Fixed responses speed answering and analysis

Survey questionnaires usually provide fixed responses to questions to simplify analysis of the replies. This multiple-choice approach also makes it easier and faster for respondents to reply. Simple fill-in-a-number questions are also widely used in quantitative research. Fixed responses are also more convenient for computer analysis, which is how most surveys are analyzed.

Quantitative measures of attitudes too

One common approach to measuring consumers' attitudes and opinions is to have respondents indicate how much they agree or disagree with a questionnaire statement. A researcher interested in what target consumers think about frozen pizzas, for example, might include a statement like "I add extra topppings when I prepare frozen pizza." The respondent might check off a response such as (1) strongly disagree, (2) disagree, (3) agree, or (4) strongly agree.

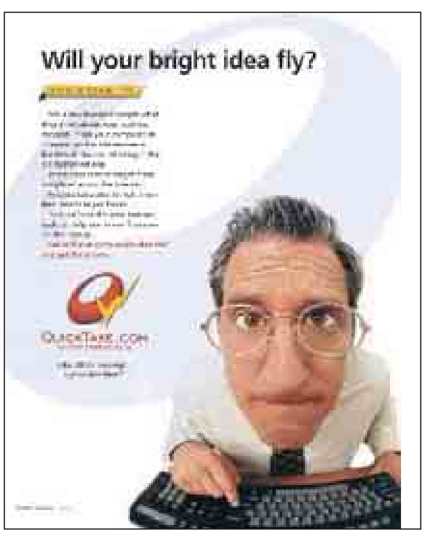
Another approach is to have respondents *rate* a product, feature, or store. For example, a questionnaire might ask consumers to rate the taste of a pizza as *excellent, good, fair,* or *poor.*

Surveys come in many forms

Decisions about what specific questions to ask and how to ask them are usually related to how respondents will be contacted—by mail (or electronic mail), via a website, on the phone, or in person. What question and response approach is used may also affect the survey. There are many possibilities. For example, whether the survey is self-administered or handled by an interviewer, the questionnaire may be on paper or in an interactive computer format (perhaps distributed on a CD or disk or displayed on a website). The computer can be programmed to skip certain questions, depending on answers given. Computerized questionnaires also allow the research to show pictures or play audio/video clips (for example, to get reactions to an advertising jingle). In an automated telephone interview, questions may be prerecorded on an audio tape or computer and the subject responds by pushing touch-tone buttons on the phone.

Mail and online surveys are common and convenient

A questionnaire distributed by mail, e-mail, or online is useful when extensive questioning is necessary. Respondents can complete the questions at their convenience. They may be more willing to provide personal information—since a



Online surveys provide fast feedback and often at a lower cost than the old-fashioned way. Of course, as always, the manager needs to be certain that the sample used is representative.

questionnaire can be completed anonymously. But the questions must be simple and easy to follow since no interviewer is there to help. If the respondent is likely to be a computer user, it may be possible to send the questionnaire on a disk (or put it on a website) and include a help feature with additional directions for people who need them.

A big problem with questionnaires is that many people don't complete them. The **response rate**—the percentage of people contacted who complete the questionnaire—is often low and respondents may not be representative. There is particular concern about the representativeness of people who complete computer-based or online questionnaires. The response rates tend to be even lower than by mail. In addition, online respondents may be younger, better educated, or different in other ways that impact how they answer. Mail, e-mail, and online surveys are economical if a large number of people respond. But they may be quite expensive if the response rate is low. The cost of the research may be wasted if the respondents are not representative; worse, the results may be misleading.

Distributing questionnaires by e-mail, or at a website, is rapidly growing in popularity. The main reason is that it is almost instantaneous—and the responses come back in computer form. Surveys sent by regular mail usually take a lot longer; pencil-and-paper responses also need to be computerized. In business markets, the time to deliver questionnaires can sometimes be reduced by faxing them.

Regardless of how quickly a questionnaire is distributed, people may take a long time to respond. For example, with a mail survey, it often takes a month or more to get the data back, which is too slow for some decisions. Moreover, it is difficult to get respondents to expand on particular points. In markets where illiteracy is a problem, it may not be possible to get any response. In spite of these limitations, the convenience and economy of self-administered surveys makes them popular for collecting primary data.

Internet

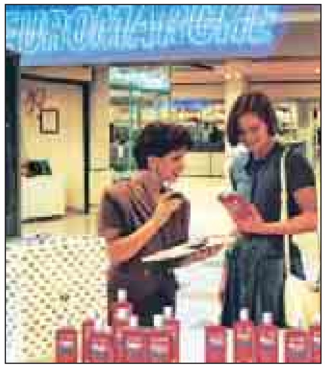
Internet Exercise Perseus Development Corporation sells software that allows a user to create online questionnaires that can be distributed by e-mail or used on the Internet. To see samples of online questions, go to the Perseus website (www.perseus.com) and then click on *Sample Surveys*. Do you think that it's more convenient for a consumer to complete a survey online or with pencil and paper?

Telephone surveys—fast and effective

Telephone interviews are popular. They are effective for getting quick answers to simple questions. Telephone interviews allow the interviewer to probe and really learn what the respondent is thinking. In addition, with computer-aided telephone interviewing, answers are immediately recorded on a computer, resulting in fast data analysis. On the other hand, some consumers find calls intrusive—and about a third refuse to answer any questions. Moreover, the telephone is usually not a very good contact method if the interviewer is trying to get confidential personal information—such as details of family income. Respondents are not certain who is calling or how such personal information might be used.

Personal interview surveys—can be in-depth

A personal interview survey is usually much more expensive per interview than e-mail, mail, or telephone surveys. But it's easier to get and keep the respondent's attention when the interviewer is right there. The interviewer can also help explain complicated directions and perhaps get better responses. For these reasons, personal interviews are commonly used for research on business customers. To reduce the



cost of locating consumer respondents, interviews are sometimes done at a store or shopping mall. This is called a mall intercept interview because the interviewer stops a shopper and asks for responses to the survey.

Researchers have to be careful that having an interviewer involved doesn't affect the respondent's answers. Sometimes people won't give an answer they consider embarrassing. Or they may try to impress or please the interviewer. Further, in some cultures people don't want to give any information. For example, many people in Africa, Latin America, and Eastern Europe are reluctant to be interviewed. This is also a problem in many low-income, inner-city areas in the United States; even Census Bureau interviewers have trouble getting cooperation.[14]

Sometimes questioning has limitations. Then observing may be more accurate or economical.

Observing—what you see is what you get

Observing—as a method of collecting data—focuses on a well-defined problem. Here we are not talking about the casual observations that may stimulate ideas in the early steps of a research project. With the observation method, researchers try to see or record what the subject does naturally. They don't want the observing to *influence* the subject's behavior.

A museum director wanted to know which of the many exhibits was most popular. A survey didn't help. Visitors seemed to want to please the interviewer and usually said that all of the exhibits were interesting. Putting observers near exhibits—to record how long visitors spent at each one—didn't help either. The curious visitors stood around to see what the observer was recording, and that messed up the measures. Finally, the museum floors were waxed to a glossy shine. Several weeks later, the floors around the exhibits were inspected. It was easy to tell which exhibits were most popular—based on how much wax had worn off the floor!

In some situations, consumers are recorded on videotape. Later, researchers can study the tape by running the film at very slow speed or actually analyzing each frame. Researchers use this technique to study the routes consumers follow through a grocery store or how they select products in a department store. Similarly, firms that have online shopping services on the Internet can use software to "watch" how consumers use the website, how much time they spend at each display, and the like.

Similarly, many franchise companies use the observation method—to check how well a franchisee is performing. KFC hires people to go to different KFC stores and act like normal customers. Then these "secret shoppers" report back to KFC on how they were treated, the quality of the service and food, and the cleanliness of the store.

Observing is common in advertising research

Observation methods are common in advertising research. For example, Nielsen Media Research (www.nielsenmedia.com) uses a device called the "people meter" that adapts the observation method to television audience research. This machine is attached to the TV set in the homes of selected families. It records when the set is on and what station is tuned in.

Checkout scanners see a lot

Computerized scanners at retail checkout counters, a major breakthrough in observing, help researchers collect very specific, and useful, information. Often this type of data feeds directly into a firm's MIS. Managers of a large chain of stores can

Whirlpool Heats Up Sales with Marketing Research

Marketing managers at Whirlpool want to satisfy customers. So they do a lot of research to find out how satisfied customers really are. For example, Whirlpool participates in a survey that results in the American Satisfaction Index. This survey of 50,000 consumers allows Whirlpool to benchmark what customers think about its quality with ratings for other firms, including competitors. The ratings published in 2000, for example, put Whirlpool among the top companies studied, and its rating was up 2 points from the year before. But the research doesn't stop there. Each year Whirlpool sends an appliance satisfaction survey to 180,000 households. Respondents rate all of their appliances on dozens of dimensions. When a competing product scores higher, Whirlpool engineers take it apart to see why and build the best ideas into their new models. However, they don't just wait for competitors to figure things out first.

A recently introduced oven, now one of Whirlpool's hottest sellers, illustrates their approach. A survey showed that consumers wanted an oven with easy-to-clean controls. That didn't seem consistent with previous sales patterns; the firm's MIS showed that models with knobs consistently outsold models with easier-to-clean push buttons. Rather than disregard the survey, Whirlpool designed a range with touch pad controls by listening to consumers at every step along the way. Consumers who played with computer simulations of the touch pad explained what they liked and didn't like. Videotapes of consumers who tried prototype models in mall intercept interviews provided ideas to further refine the design. The result is a touch pad control that is easy to clean and so easy to use that consumers don't even need to read the manual.

Consumer research has been an even more important factor in Whirlpool's growth overseas. For example, until recently only about one-third of European households had a microwave oven. Whirlpool researchers learned that more people would buy a microwave oven if it could crisp food as it heated the food. Whirlpool designed a microwave with a broiler coil and other innovations. The result is an oven that is popular in Britain for frying bacon and eggs and in Italy for crisping pizza crusts.[15]

www.mhhe.com/fourps

see exactly what products have sold each day and how much money each department in each store has earned. But the scanner also has wider applications for marketing research.

Information Resources, Inc. (www.infores.com), and ACNielsen (acnielsen.com) use **consumer panels**—a group of consumers who provide information on a continuing basis. Whenever a panel member shops for groceries, he or she gives an ID number to the clerk, who keys in the number. Then the scanner records every purchase—including brands, sizes, prices, and any coupons used. In a variation of this approach, consumers use a hand-held scanner to record purchases once they get home. For a fee, clients can evaluate actual customer purchase patterns and answer

Data from electronic scanners helps retailers decide what brands they will sell and helps their suppliers plan so that products arrive at the store in time to prevent stock-outs.

Simmons' ad agency used an experiment to improve a new print ad for the Beautyrest mattress. Groups of consumers saw two different ads. The ads were the same, except that one featured a father holding a baby and the other featured a mother. The ad with the father earned higher recall scores.

questions about the effectiveness of their discount coupons. Did the coupons draw new customers, or did current customers simply use them to stock up? If consumers switched from another brand, did they go back to their old brand the next time? The answers to such questions are important in planning marketing strategies—and scanners can help marketing managers get the answers.

Some members of the consumer panel are also tied into a special TV cable system. With this system, a company can direct advertisements to some houses and not others. Then researchers can evaluate the effect of the ads by comparing the purchases of consumers who saw the ads with those who didn't.

The use of scanners to "observe" what customers actually do is changing consumer research methods. Companies can turn to firms like Information Resources as a *single source* of complete information about customers' attitudes, shopping behavior, and media habits.

Data captured by electronic scanners is equally important to e-commerce in business-to-business markets. Increasingly, firms mark their shipping cartons and packages with computer-readable bar codes that make it fast and easy to track inventory, shipments, orders, and the like. As information about product sales or shipments becomes available, it is instantly included in the MIS and accessible over the Internet. That way, a manager can access any detailed piece of information or do an analysis to summarize trends and patterns. Here, as with scanner data on consumers, the information available is so detailed that the possibilities are limited more by imagination—and money—than by technology.[16]

Experimental method controls conditions

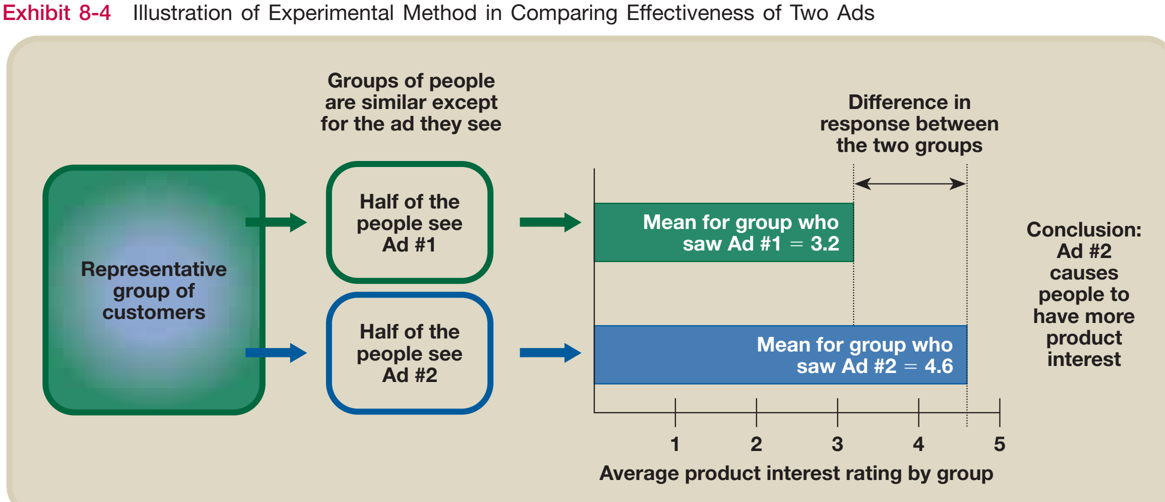
A marketing manager can get a different kind of information—with either questioning or observing—using the experimental method. With the **experimental method,** researchers compare the responses of two (or more) groups that are similar except on the characteristic being tested. Researchers want to learn if the specific characteristic—which varies among groups—*causes* differences in some response among the groups. For example, a researcher might be interested in comparing responses of consumers who had seen an ad for a new product with consumers who had not seen the ad. The "response" might be an observed behavior—like the

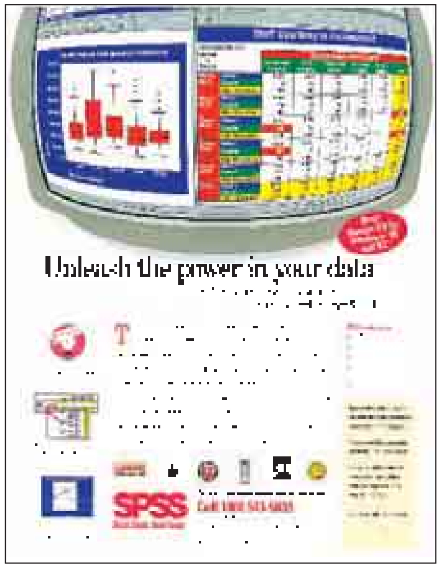
A firm's own data on customers' past purchases, if properly analyzed, can be an important source of information for evaluating new opportunities.

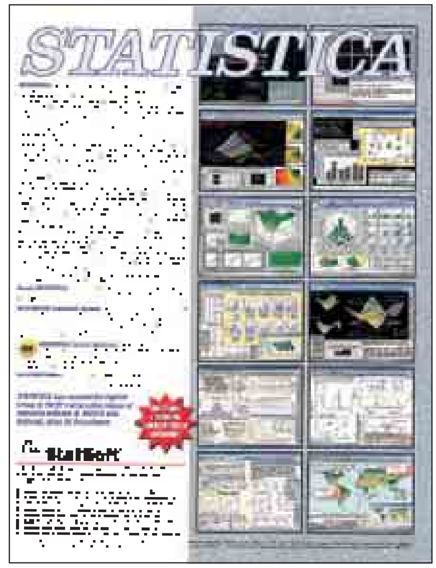
purchase of a product—or the answer to a specific question—like "How interested are you in this new product?" See Exhibit 8-4.

Marketing managers for Mars—the company that makes Snickers candy bars—used the experimental method to help solve a problem. They wanted to know if making their candy bar bigger would increase sales enough to offset the higher cost. To decide, they conducted a marketing experiment in which the company carefully varied the size of candy bars sold in *different* markets. Otherwise, the marketing mix stayed the same. Then researchers tracked sales in each market area to see the effect of the different sizes. They saw a big difference immediately: The added sales more than offset the cost of a bigger candy bar.

Exhibit 8-4 Illustration of Experimental Method in Comparing Effectiveness of Two Ads







SPSS and StatSoft are statistical packages that make it easy to summarize and graph marketing research data.

Test-marketing of new products is another type of marketing experiment. In a typical approach, a company tries variations on its planned marketing mix in a few geographic market areas. The results of the tests help to identify problems or refine the marketing mix—before the decision is made to go to broader distribution. However, alert competitors may disrupt such tests—perhaps by increasing promotion or offering retailers extra discounts. To avoid these problems, some small firms conduct some of their tests in foreign markets.

Researchers don't use the experimental method as often as surveys and focus groups. Many managers don't understand the valuable information they can get from this method. Further, they don't like the idea of some researcher "experimenting" with their business.[17]

Syndicated research shares data collection costs

Some private research firms specialize in collecting data and supplying it to managers in many different client firms. Often the marketing manager subscribes to the research service and gets regular updates.

Marketing managers from many different firms may have to make the same kinds of decisions and may need the same type of data. The most economical approach in a situation like this is for one specialist firm to collect the data and distribute it to the different users, who share the cost. This is how Information Resources, Inc., and ACNielsen operate.

Many other firms collect and distribute specialized types of data. For example, Market Facts (www.marketfacts.com) sells access to its surveys on home appliances and electronics, retail banking and insurance, and other product categories. Simmons Market Research Bureau (www.smrb.com) does extensive research on consumer media habits and then sells its data to many advertising agencies and producers of consumer products who want to find out about their particular target markets. Many different auto producers use J. D. Power's (www.jdpa.com) surveys of customer satisfaction—often as the basis for advertising claims. Subscription data services are available for numerous different industries—ranging from food service to prescription drugs to micro electronic devices.[18]

Interpreting the Data—Step 4

What does it really mean?

After someone collects the data, it has to be analyzed to decide what it all means. In quantitative research, this step usually involves statistics. **Statistical packages**—easy-to-use computer programs that analyze data—have made this step easier. As we noted earlier, some firms provide *decision support systems* so managers can use a statistical package to interpret data themselves. More often, however, technical specialists are involved at the interpretation step.

Cross-tabulation is one of the most frequently used approaches for analyzing and interpreting marketing research data. It shows the relationship of answers to two different questions. Exhibit 8-5 is an example. The cross-tab analysis showed that customers who had moved in the last year were much more likely than nonmovers to have adopted "Caller ID" on their phones at home.

There are many other approaches for statistical analysis—the best one depends on the situation. The details of statistical analysis are beyond the scope of this book. But a good manager should know enough to understand what a research project can and can't do.[19]

Is your sample really representative?

It's usually impossible for marketing managers to collect all the information they want about everyone in a **population**—the total group they are interested in. Marketing researchers typically study only a **sample,** a part of the relevant population. How well a sample *represents* the total population affects the results. Results from a sample that is not representative may not give a true picture.

The manager of a retail store might want a phone survey to learn what consumers think about the store's hours. If interviewers make all of the calls during the day, the sample will not be representative. Consumers who work outside the home during the day won't have an equal chance of being included. Those interviewed might say the limited store hours are "satisfactory." Yet it would be a mistake to assume that *all* consumers are satisfied.

Random samples tend to be representative

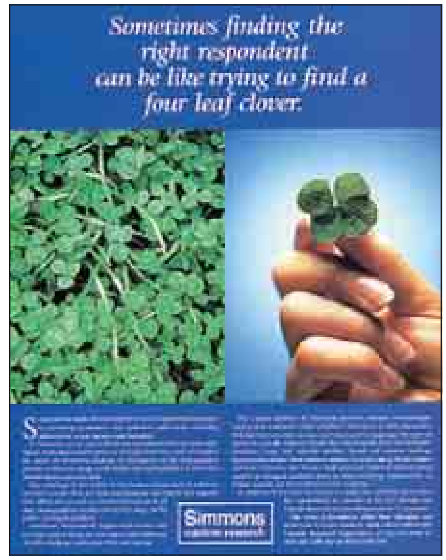
You can see that getting a representative sample is very important. One method of doing so is **random sampling,** where each member of the population has the same chance of being included in the sample. Great care must be used to ensure that sampling is really random, not just haphazard.

If a random sample is chosen from a population, it will tend to have the same characteristics and be representative of the population. "Tend to" is important because it is only a tendency—the sample is not exactly the same as the population.

Exhibit 8-5 Cross-Tabulation Breakdown of Responses to a Phone Company Consumer Survey

		Have You Moved in the Last Year?		
	Answers:	No	Yes	Total
Do you have "Caller ID" on your phone at home?	*Yes*	10.2%	23.4%	15.5%
	No	89.8	76.6	84.5
	Total	100.0%	100.0%	100.0%

Interpretation: 15.5 percent of people in the survey said that they had "Caller ID" on their phone at home. However, the percentage was much higher (23.4%) among people who had moved in the last year, and lower (10.2%) among people who had not moved.



Survey Sampling, Inc., and Simmons Custom Research help marketing researchers develop samples that are really representative of the target market.

Much marketing research is based on nonrandom sampling because of the high cost and difficulty of obtaining a truly random sample. Sometimes nonrandom samples give very good results—especially in industrial markets where the number of customers may be relatively small and fairly similar. But results from nonrandom samples must be interpreted, and used, with care.

Research results are not exact

An estimate from a sample, even a representative one, usually varies somewhat from the true value for a total population. Managers sometimes forget this. They assume that survey results are exact. Instead, when interpreting sample estimates, managers should think of them as *suggesting* the approximate value.

If random selection is used to develop the sample, researchers can use various methods to help determine the likely accuracy of the sample value. This is done in terms of **confidence intervals**—the range on either side of an estimate that is likely to contain the true value for the whole population. Some managers are surprised to learn how wide that range can be.

Consider a wholesaler who has 1,000 retail customers and wants to learn how many of these retailers carry a product from a competing supplier. If the wholesaler randomly samples 100 retailers and 20 say yes, then the sample estimate is 20 percent. But with that information the wholesaler can only be 95 percent confident that the percentage of all retailers is in the confidence interval between 12 and 28 percent.[20]

The larger the sample size, the greater the accuracy of estimates from a random sample. With a larger sample, a few unusual responses are less likely to make a big difference.

Validity problems can destroy research

Even if the sampling is carefully planned, it is also important to evaluate the quality of the research data itself.

Managers and researchers should be sure that research data really measures what it is supposed to measure. Many of the variables marketing managers are interested in are difficult to measure accurately. Questionnaires may let us assign numbers to consumer responses, but that still doesn't mean that the result is precise. An interviewer might ask “How much did you spend on soft drinks last week?” A respondent may be perfectly willing to cooperate—and be part of the representative sample—but just not be able to remember.

Validity concerns the extent to which data measures what it is intended to measure. Validity problems are important in marketing research because many people will try to answer even when they don't know what they're talking about. Further, a poorly worded question can mean different things to different people and invalidate the results. Often, one or more pretests of a research project are required to evaluate the quality of the questions and measures and to ensure that potential problems have been identified. Managers must be sure that they only pay for research results that are representative and valid.

Poor interpretation can destroy research

Besides sampling and validity problems, a marketing manager must consider whether the analysis of the data supports the *conclusions* drawn in the interpretation step. Sometimes technical specialists pick the right statistical procedure—their calculations are exact—but they misinterpret the data because they don't understand the management problem. In one survey, car buyers were asked to rank five cars in order from "most preferred" to "least preferred." One car was ranked first by slightly more respondents than any other car so the researcher reported it as the "most liked car." That interpretation, however, ignored the fact that 70 percent of the respondents ranked the car *last*!

Interpretation problems like this can be subtle but crucial. Some people draw misleading conclusions on purpose to get the results they want. Marketing managers must decide whether *all* of the results support the interpretation and are relevant to their problem.

Marketing manager and researcher should work together

Marketing research involves many technical details. But you can see that the marketing researcher and the marketing manager must work together to be sure that they really do solve the problem facing the firm. If the whole research process has been a joint effort, then the interpretation step can move quickly to decision making—and solving the problem.

Solving the Problem—Step 5

The last step is solving the problem

In the problem solution step, managers use the research results to make marketing decisions.

Some researchers, and some managers, are fascinated by the interesting tidbits of information that come from the research process. They are excited if the research reveals something they didn't know before. But if research doesn't have action implications, it has little value and suggests poor planning by the researcher and the manager.

When the research process is finished, the marketing manager should be able to apply the findings in marketing strategy planning—the choice of a target market or the mix of the four Ps. If the research doesn't provide information to help guide these decisions, the company has wasted research time and money.

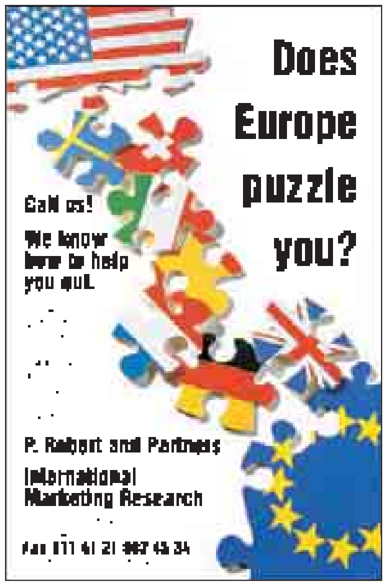
We emphasize this step because it is the reason for and logical conclusion to the whole research process. This final step must be anticipated at each of the earlier steps.

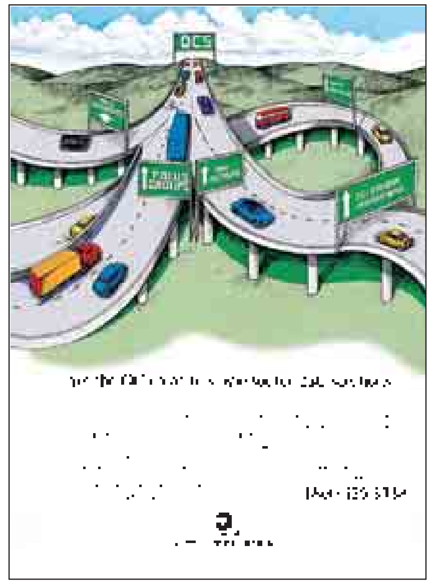
International Marketing Research

Research contributes to international success

Marketing research on overseas markets is often a major contributor toward international marketing success. Conversely, export failures are often due to a lack of home office management expertise concerning customer interests, needs, and other

There are a large number of international marketing research firms that offer specialized services to marketing managers.





segmenting dimensions as well as environmental factors such as competitors' prices and products. Effective marketing research can help to overcome these problems.

Avoid mistakes with local researchers

Whether a firm is small and entering overseas markets for the first time or already large and well established internationally, there are often advantages to working with local market research firms. These research suppliers know the local situation and are less likely to make mistakes based on misunderstanding the customs, language, or circumstances of the customers they study.

Many large research firms have a network of local offices around the world to help with such efforts. Similarly, multinational or local advertising agencies and middlemen can often provide leads on identifying the best research suppliers.

Some coordination and standardization makes sense

When a firm is doing similar research projects in different markets around the world, it makes sense for the marketing manager to coordinate the efforts. If the manager doesn't establish some basic guidelines at the outset, the different research projects may all vary so much that the results can't be compared from one market area to another. Such comparisons give a home office manager a better chance of understanding how the markets are similar and how they differ.

Multinational companies with operations in various countries often attempt to centralize some market research functions. One reason is to reduce costs or achieve research economies of scale. The centralized approach also improves the firm's ability to transfer experience and know-how from one market area or project to another. For example, one of Eastman Kodak's International Divisions appointed a market research specialist in each subsidiary company throughout the Asian region. The specialists report to local marketing managers but also receive research direction from expert research managers in the head office in the U.S.

There is even greater opportunity and need to standardize and coordinate elements of a marketing information system in an international marketing operation. Computer databases and information systems are most useful when they are designed to include the same variables organized consistently over time. Without this, it is impossible for the manager to go into much depth in comparing and contrasting data from different markets.[21]

How Much Information Do You Need?

Information is costly—but reduces risk

We have been talking about the benefits of good marketing information, but dependable information can be expensive. A big company may spend millions developing an information system. A large-scale survey can cost from $20,000 to $100,000—or even more. The continuing research available from companies such as Information Resources, Inc., can cost a company well over $100,000 a year. And a market test for 6 to 12 months may cost $200,000 to $500,000 per test market!

Companies that are willing and able to pay the cost often find that marketing information pays for itself. They are more likely to select the right target market and marketing mix—or they might see a potential problem before it becomes a costly crisis.

What is the value of information?

The high cost of good information must be balanced against its probable value to management. Managers never get all the information they would like to have. Very detailed surveys or experiments may be "too good" or "too expensive" or "too late" if all the company needs is a rough sampling of retailer attitudes toward a new pricing plan by tomorrow. Money is wasted if research shows that a manager's guesses are wrong and the manager ignores the facts.

Marketing managers must take risks because of incomplete information. That's part of their job and always will be. But they must weigh the cost of getting more data against its likely value. If the risk is not too great, the cost of getting more information may be greater than the potential loss from a poor decision. A decision to expand into a new territory with the present marketing mix, for example, might be made with more confidence after a $25,000 survey. But just sending a sales rep into the territory for a few weeks to try to sell potential customers would be a lot cheaper. And, if successful, the answer is in and so are some sales.[22]

Conclusion

Marketing managers face difficult decisions in selecting target markets and managing marketing mixes. And managers rarely have all the information they would like to have. This problem is usually worse for managers who work with international markets. But they don't have to rely only on intuition. They can usually obtain good information to improve the quality of their decisions.

Computers and computer networks, like the Internet, are helping marketing managers become full-fledged members of the information age. Both large and small firms are setting up intranets and marketing information systems (MIS)—to be certain that routinely needed data is available and accessible quickly.

Marketing managers deal with rapidly changing environments. Available data is not always adequate to answer the detailed questions that arise. Then a marketing research project may be required to gather new information.

Marketing research should be guided by the scientific method. The scientific approach to solving marketing problems involves five steps: defining the problem, analyzing the situation, obtaining data, interpreting data, and solving the problem. This objective and organized approach helps to keep research on target—reducing the risk of doing costly research that isn't necessary or doesn't solve the problem.

Our strategy planning framework can be helpful in finding the real problem. By finding and focusing on the real problem, the researcher and marketing manager may be able to move quickly to a useful solution—without the cost and risks of gathering primary data in a formal research project. With imagination, they may even be able to find the answers in their MIS or in other readily available secondary data.

Questions and Problems

1. Discuss the concept of a marketing information system and why it is important for marketing managers to be involved in planning the system.
2. In your own words, explain why a decision support system (DSS) can add to the value of a marketing information system. Give an example of how a decision support system might help.
3. If a firm's intranet and marketing decision support system do not include a search engine, would they still be useful to a marketing manager? Why?
4. Discuss how output from a marketing information system (MIS) might differ from the output of a typical marketing research department.
5. Discuss some of the likely problems facing the marketing manager in a small firm that has just purchased a personal computer with a cable modem to search the Internet for information on competitors' marketing plans.
6. Explain the key characteristics of the scientific method and show why these are important to managers concerned with research.
7. How is the situation analysis different from the data collection step? Can both these steps be done at the same time to obtain answers sooner? Is this wise?
8. Distinguish between primary data and secondary data and illustrate your answer.
9. With so much secondary information now available free or at low cost over the Internet, why would a firm ever want to spend the money to do primary research?
10. If a firm were interested in estimating the distribution of income in the state of California, how could it proceed? Be specific.
11. If a firm were interested in estimating sand and clay production in Georgia, how could it proceed? Be specific.
12. Go to the library (or get on the Internet) and find (in some government publication or website) three marketing-oriented "facts" on international markets that you did not know existed or were available. Record on one page and show sources.
13. Explain why a company might want to do focus group interviews rather than individual interviews with the same people.
14. Distinguish between qualitative and quantitative approaches to research—and give some of the key advantages and limitations of each approach.
15. Define response rate and discuss why a marketing manager might be concerned about the response rate achieved in a particular survey. Give an example.
16. Prepare a table that summarizes some of the key advantages and limitations of mail, e-mail, telephone, and personal interview approaches for administering questionnaires.
17. Would a firm want to subscribe to a shared cost data service if the same data were going to be available to competitors? Discuss your reasoning.
18. Explain how you might use different types of research (focus groups, observation, survey, and experiment) to forecast market reaction to a new kind of disposable baby diaper, which is to receive no promotion other than what the retailer will give it. Further, assume that the new diaper's name will not be associated with other known products. The product will be offered at competitive prices.
19. Marketing research involves expense—sometimes considerable expense. Why does the text recommend the use of marketing research even though a highly experienced marketing executive is available?
20. A marketing manager is considering opportunities to export her firm's current consumer products to several different countries. She is interested in getting secondary data that will help her narrow down choices to countries that offer the best potential. The manager then plans to do more detailed primary research with consumers in those markets. What suggestions would you give her about how to proceed?
21. Discuss the concept that some information may be too expensive to obtain in relation to its value. Illustrate.

Suggested Cases

8. Sophia's Ristorante
9. SleepyTime Motel

Computer-Aided Problem

8. **Marketing Research**

Texmac, Inc., has an idea for a new type of weaving machine that could replace the machines now used by many textile manufacturers. Texmac has done a telephone survey to estimate how many of the old-style machines are now in use. Respondents using the present machines were also asked if they would buy the improved machine at a price of $10,000.

Texmac researchers identified a population of about 5,000 textile factories as potential customers. A sample of these were surveyed, and Texmac received 500 responses. Researchers think the total potential market is about 10 times larger than the sample of respondents. Two hundred twenty of the respondents indicated that their firms used old machines like the one the new machine was intended to replace. Forty percent of those firms said that they would be interested in buying the new Texmac machine.

Texmac thinks the sample respondents are representative of the total population, but the marketing manager realizes that estimates based on a sample may not be exact when applied to the whole population. He wants to see how sampling error would affect profit estimates. Data for this problem appears in the spreadsheet. Quantity estimates for the whole market are computed from the sample estimates. These quantity estimates are used in computing likely sales, costs, and profit contribution.

a. *An article in a trade magazine reports that there are about 5,200 textile factories that use the old-style machine. If the total market is really 5,200 customers—not 5,000 as Texmac originally thought—how does that affect the total quantity estimate and profit contribution?*

b. *Some of the people who responded to the survey didn't know much about different types of machines. If the actual number of old machines in the market is really 200 per 500 firms—not 220 as estimated from survey responses—how much would this affect the expected profit contribution (for 5,200 factories)?*

c. *The marketing manager knows that the percentage of textile factories that would actually buy the new machine might be different from the 40 percent who said they would in the survey. He estimates that the proportion that will replace the old machine might be as low as 36 and as high as 44 percent—depending on business conditions. Use the analysis feature to prepare a table that shows how expected quantity and profit contribution change when the sample percent varies between a minimum of 36 and a maximum of 44 percent. What does this analysis suggest about the use of estimates from marketing research samples? (Note: Use 5,200 for the number of potential customers and use 220 as the estimate of the number of old machines in the sample.)*

For additional questions related to this problem, see Exercise 8-3 in the *Learning Aid for Use with Basic Marketing*, 14th edition.

When You Finish This Chapter, You Should

1. Understand what "Product" really means.

2. Know the key differences between goods and services.

3. Know the differences among the various consumer and business product classes.

4. Understand how the product classes can help a marketing manager plan marketing strategies.

5. Understand what branding is and how to use it in strategy planning.

6. Understand the importance of packaging in strategy planning.

7. Understand the role of warranties in strategy planning.

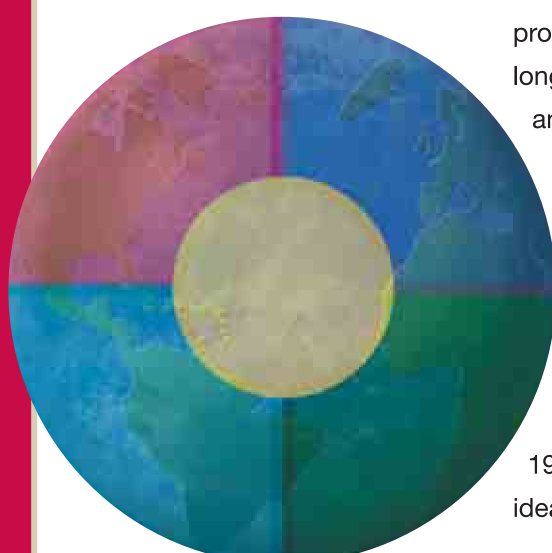
8. Understand the important new terms (shown in red).

Chapter Nine

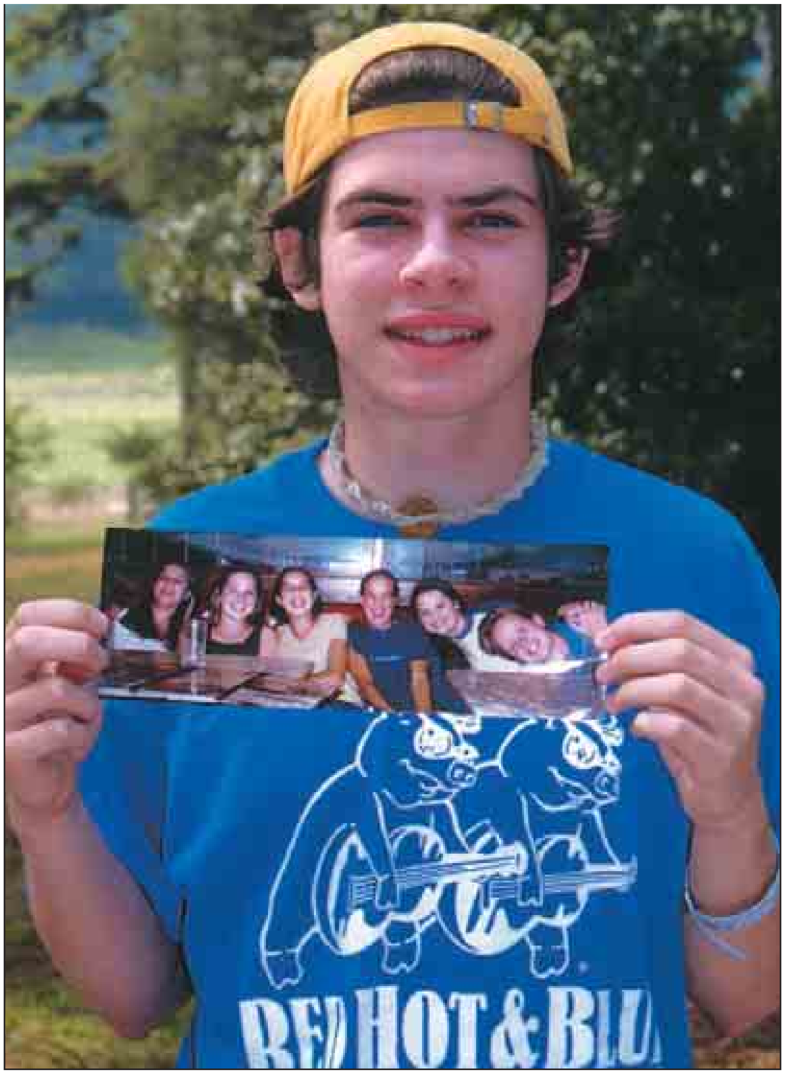
Elements of Product Planning for Goods and Services

For decades, 35mm cameras have been the photographic standard. The technical quality of the films is excellent. They capture subtle colors and offer sharp resolution. And there's a lot of choice among cameras for serious photographers who study all of the details. Unfortunately, this isn't enough to satisfy most amateur photographers. For them, one camera seems pretty much like another. Their snapshots often come out botched because of errors loading the film or the wrong light. Sometimes the shape of the picture just doesn't fit the subject. Or if there's one great picture and someone wants a reprint, the negative can't be found. These problems have been around for a long time. So to address them—and get new sales of films and cameras—Kodak and its four global rivals agreed on a new photo standard, the Advanced Photo System (APS).

When Kodak was ready to introduce its new Advantix brand APS film and cameras in 1996, it looked like a winning idea. A new film cartridge made it



place price promotion produc



easy to load the film. Photos could be shot in any of three sizes, including an extrawide format. The film adjusted for differences in light. And developed film came back protected in the cartridge. Reprints were easy to order too because a numbered proof sheet came with each set of prints. Customers liked these benefits. What they really wanted was good snapshots—so Advantix seemed worth the 15 percent higher price.

However, in its rush to beat rivals to market, Kodak ran into production problems. It could not get enough cameras to retailers. So the big ad campaign to build familiarity with the Advantix brand of film and cameras was wasted. Worse, because of a confusing package, many people bought Advantix film expecting it to work in a 35mm camera; it wouldn't. Initially, getting Advantix pictures developed was also a hassle. Retailers were slow to put money into new equipment to develop Advantix film; they waited to see if customers wanted it. And it added to consumer confusion that Fuji, Minolta, and other firms each had their own brand names for APS products.

By 1998, these problems were smoothing out. But sales were slow because too few consumers knew about Advantix. So Kodak relaunched the product. Kodak stuck with the Advantix name but used a new package design. Ads directly pitted Advantix against the problems with 35mm pictures, even though that risked eating into Kodak's 35mm sales. Camera giveaway promotions on the Kodak website (www.kodak.com) stirred interest too. And price-off discounts on three-roll packages got consumers to take more pictures. As demand grew, retailers also gave

Advantix more attention. For example, Wal-Mart put Kodak's $50 camera on special display. And many photo labs offered consumers a money-back guarantee on any Advantix prints that were not completely satisfactory.

For many customers in the target market, Kodak's Advantix line offers new benefits that they couldn't get before. But it involves new products that are basically incremental to what Kodak was already selling and what customers were already buying. Digital cameras and pictures are a more revolutionary type of new product. Consumers who adopt them will change their picture-taking behavior, and, as Kodak knows, they'll certainly change their film-buying and film-processing behavior too. It won't happen overnight, but digital cameras will make traditional cameras obsolete. And in the process the competition that Kodak faces has already changed, in some cases dramatically. Take, for example, HP's DeskJet brand color printers. If you buy a digital camera, the odds are that you'll print out the pictures on a DeskJet, not on a Kodak printer. So just as Kodak is fighting for shelf space against low-price Fuji and dealer brands in the mature market for 35mm film, it is fighting new and very different competitors in the fast-growing market related to digital photography.[1]

The Product Area Involves Many Strategy Decisions

The Kodak case highlights some important topics we'll discuss in this chapter and the next. Here we'll start by looking at how customers see a firm's product. Then we'll talk about product classes to help you better understand marketing strategy planning. We'll also talk about branding, packaging, and warranties. In summary, as shown in Exhibit 9-1, there are many strategy decisions related to the Product area.

What Is a Product?

Customers buy satisfaction, not parts

When Volkswagen sells a new Beetle, is it just selling a certain number of nuts and bolts, some sheet metal, an engine, and four wheels?

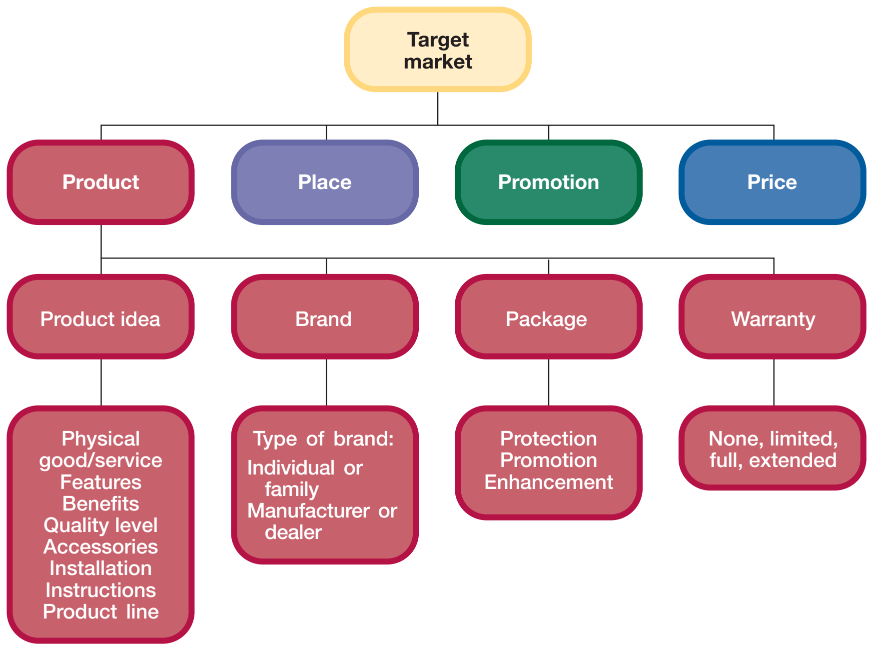
When Air Jamaica sells a ticket for a flight to the Caribbean, is it just selling so much wear and tear on an airplane and so much pilot fatigue?

The answer to these questions is *no*. Instead, what these companies are really selling is the satisfaction, use, or benefit the customer wants.

All consumers care about is that their new Beetles look cute and keep running. And when they take a trip on Air Jamaica, they really don't care how hard it is on the plane or the crew. They just want a safe, comfortable trip. In the same way, when producers and middlemen buy a product, they're interested in the profit they can make from its purchase—through use or resale.

Product means the need-satisfying offering of a firm. The idea of "Product" as potential customer satisfaction or benefits is very important. Many business managers get wrapped up in the technical details involved in producing a product. But that's not how most customers view the product. Most customers think about a product in terms of the total satisfaction it provides. That satisfaction may require a "total" product offering that is really a combination of excellent service, a physical

Exhibit 9-1
Strategy Planning for Product

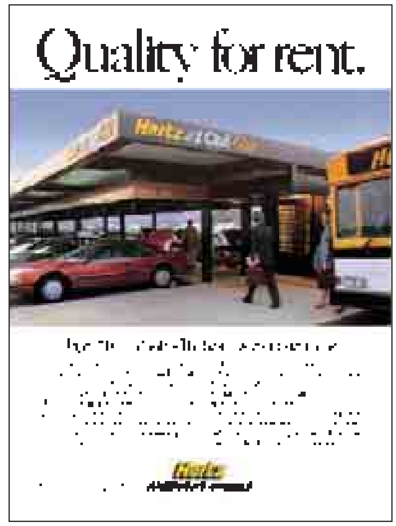


good with the right features, useful instructions, a convenient package, a trustworthy warranty, and perhaps even a familiar name that has satisfied the consumer in the past.

Product quality and customer needs

Product quality should also be determined by how customers view the product. From a marketing perspective, **quality** means a product's ability to satisfy a customer's needs or requirements. This definition focuses on the customer—and how the customer thinks a product will fit some purpose. For example, the "best" satellite TV service may not be the one with the highest number of channels but the one that includes a local channel that a consumer wants to watch. Similarly, the best-quality clothing for casual wear on campus may be a pair of jeans, not a pair of dress slacks made of a higher-grade fabric.

To better satisfy its customers' needs and make traveling more enjoyable, this French railroad's service includes door-to-door delivery of the passenger's luggage. The ad says "your luggage is old enough to travel by itself. It's up to us to ensure you'd rather go by train."



Because customers buy satisfaction, not just parts, marketing managers must be constantly concerned with the product quality of their goods and services.

Among different types of jeans, the one with the strongest stitching and the most comfortable or durable fabric might be thought of as having the highest grade or *relative quality* for its product type. Marketing managers often focus on relative quality when comparing their products to competitors' offerings. However, a product with better features is not a high-quality product if the features aren't what the target market wants.

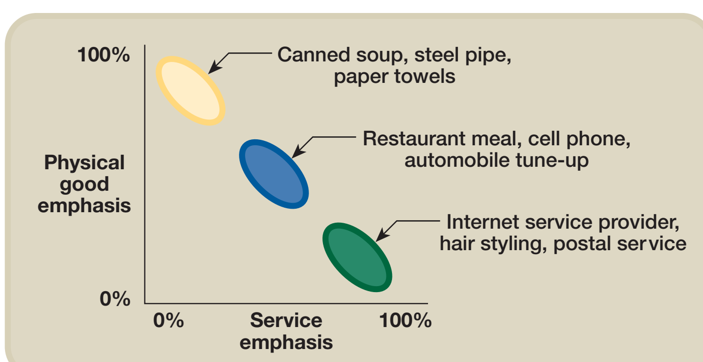
Quality and satisfaction depend on the total product offering. If potato chips get stale on the shelf because of poor packaging, the consumer will be dissatisfied. A broken button on a shirt will disappoint the customer—even if the laundry did a nice job cleaning and pressing the collar. A full-featured TiVo digital video recorder is a poor-quality product if it's hard for a consumer to program a recording session.[2]

Goods and/or services are the product

You already know that a product may be a physical *good* or a *service* or a *blend* of both. Yet, it's too easy to slip into a limited, physical-product point of view. We want to think of a product in terms of the needs it satisfies. If a firm's objective is to satisfy customer needs, service can be part of its product—or service alone may *be* the product—and must be provided as part of a total marketing mix.

Exhibit 9-2 shows this bigger view of Product. It shows that a product can range from a 100 percent emphasis on physical goods—for commodities like steel pipe—to a 100 percent emphasis on service, like dial-up Internet access from EarthLink. Regardless of the emphasis involved, the marketing manager must

Exhibit 9-2
Examples of Possible Blends of Physical Goods and Services in a Product



consider most of the same elements in planning products and marketing mixes. Given this, we usually won't make a distinction between goods and services but will call all of them *Products*. Sometimes, however, understanding the differences in goods and services can help fine tune marketing strategy planning. So let's look at some of these differences next.

Differences in Goods and Services

How tangible is the Product?

Because a good is a physical thing, it can be seen and touched. You can try on a pair of Timberland shoes, thumb through the latest issue of *Rolling Stone* magazine, or smell Colombian coffee as it brews. A good is a *tangible* item. When you buy it, you own it. And it's usually pretty easy to see exactly what you'll get.

On the other hand, a **service** is a deed performed by one party for another. When you provide a customer with a service, the customer can't keep it. Rather, a service is experienced, used, or consumed. You go see a DreamWorks Pictures movie, but afterward all you have is a memory. You ride on a ski lift in the Alps, but you don't own the equipment. Services are not physical—they are *intangible*. You can't "hold" a service. And it may be hard to know exactly what you'll get when you buy it.

Most products are a combination of tangible and intangible elements. Shell gas and the credit card to buy it are tangible—the credit the card grants is not. A Domino's pizza is tangible, but the fast home delivery is not.

Is the product produced before it's sold?

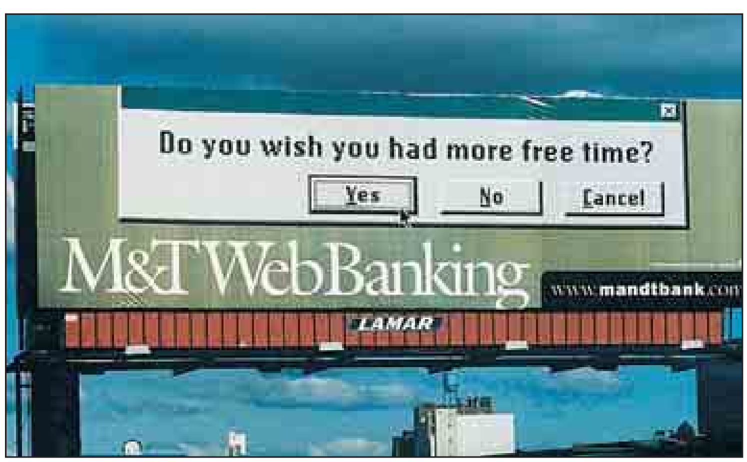
Goods are usually produced in a factory and then sold. A Magnavox TV may be stored in a warehouse or store waiting for a buyer. By contrast, services are often sold first, then produced. And they're produced and consumed in the same time frame. Thus, goods producers may be far away from the customer, but service providers often work in the customer's presence.

A worker in a Magnavox TV factory can be in a bad mood—and customers will never know. But a rude bank teller can drive customers away.

Services can't be stored or transported

Services are perishable—they can't be stored. This makes it harder to balance supply and demand. An example explains the problem.

MCI sells long-distance telephone services. Even when demand is high—during peak business hours or on Mother's Day—customers expect the service to be available. They don't want to hear "Sorry, all lines are busy." So MCI must have enough equipment and employees to deal with peak demand times. But when customers aren't making many calls, MCI's facilities are idle. MCI might be able to save money



Providing consistent, high-quality service is a challenge, so many firms are using technology to make it easier and quicker for customers to get the services they want by themselves.

At companies like 3M, managers must develop marketing plans for individual products that are consistent with the marketing program for the whole product assortment.

with less capacity (equipment and people), but then it will sometimes have to face dissatisfied customers.

It's often difficult to have economies of scale when the product emphasis is on service. Services can't be produced in large, economical quantities and then transported to customers. In addition, *services often have to be produced in the presence of the customer.* So service suppliers often need duplicate equipment and staff at places where the service is actually provided. Merrill Lynch sells investment advice along with financial products worldwide. That advice could, perhaps, be produced more economically in a single building in New York City and made available only on its website. But Merrill Lynch has offices all over the world. Many customers want a personal touch from the stockbroker telling them how to invest their money.[3]

Think about the whole Product

Providing the right product—when and where and how the customer wants it—is a challenge. This is true whether the product is primarily a service, primarily a good, or as is usually the case, a blend of both. Marketing managers must think about the "whole" Product they provide, and then make sure that all of the elements fit together and work with the rest of the marketing strategy. Sometimes a single product isn't enough to meet the needs of target customers. Then assortments of different products may be required.

Whole Product Lines Must Be Developed Too

A **product assortment** is the set of all product lines and individual products that a firm sells. A **product line** is a set of individual products that are closely related. The seller may see the products in a line as related because they're produced and/or operate in a similar way, sold to the same target market, sold through the same types of outlets, or priced at about the same level. Sara Lee, for example, has many product lines in its product assortment—including coffee, tea, luncheon meats, desserts, snacks, hosiery, sportswear, lingerie, and shoe polish. But Enterprise has one product line—different types of vehicles to rent. An **individual product** is a particular product within a product line. It usually is differentiated by brand, level of service offered, price, or some other characteristic. For example, each size and flavor of a

Some items in Bridgestone's line of tire products sell as consumer products, others sell as business products, and some are both. However, when different target markets are involved the rest of the marketing mix may also need to be different.

brand of soap is an individual product. Middlemen usually think of each separate product as a stock-keeping unit (sku) and assign it a unique sku number.

Each individual product and target market may require a separate strategy. For example, Sara Lee's strategy for selling tea in England is different from its strategy for selling men's underwear in the United States. We'll focus mainly on developing one marketing strategy at a time. But remember that a marketing manager may have to plan *several* strategies to develop an effective marketing program for a whole company.

Product Classes Help Plan Marketing Strategies

You don't have to treat *every* product as unique when planning strategies. Some product classes require similar marketing mixes. These product classes are a useful starting point for developing marketing mixes for new products and evaluating present mixes.

Product classes start with type of customer

All products fit into one of two broad groups—based on the type of customer that will use them. **Consumer products** are products meant for the final consumer. **Business products** are products meant for use in producing other products. The same product—like Bertolli Olive Oil—*might* be in both groups. Consumers buy it to use in their own kitchens, but food processing companies and restaurants buy it in large quantities as an ingredient in the products they sell. Selling the same product to both final consumers and business customers requires (at least) two different strategies.

There are product classes within each group. Consumer product classes are based on *how consumers think about and shop for products*. Business product classes are based on *how buyers think about products and how they'll be used*.

Consumer Product Classes

Consumer product classes divide into four groups: (1) convenience, (2) shopping, (3) specialty, and (4) unsought. *Each class is based on the way people buy products*. See Exhibit 9-3 for a summary of how these product classes relate to marketing mixes.[4]

Convenience products—purchased quickly with little effort

Convenience products are products a consumer needs but isn't willing to spend much time or effort shopping for. These products are bought often, require little service or selling, don't cost much, and may even be bought by habit. A convenience product may be a staple, impulse product, or emergency product.

Exhibit 9-3 Consumer Product Classes and Marketing Mix Planning

Consumer Product Class	Marketing Mix Considerations	Consumer Behavior
Convenience products		
Staples	Maximum exposure with widespread, low-cost distribution; mass selling by producer; usually low price; branding is important.	Routinized (habitual), low effort, frequent purchases; low involvement.
Impulse	Widespread distribution with display at point of purchase	Unplanned purchases bought quickly.
Emergency	Need widespread distribution near probable point of need; price sensitivity low.	Purchase made with time pressure when a need is great.
Shopping products		
Homogeneous	Need enough exposure to facilitate price comparison; price sensitivity high.	Customers see little difference among alternatives, seek lowest price.
Heterogeneous	Need distribution near similar products; promotion (including personal selling) to highlight product advantages; less price sensitivity.	Extensive problem solving; consumer may need help in making a decision (salesperson, website, etc.).
Specialty products	Price sensitivity is likely to be low; limited distribution may be acceptable, but should be treated as a convenience or shopping product (in whichever category product would typically be included) to reach persons not yet sold on its specialty product status.	Willing to expend effort to get specific product, even if not necessary; strong preferences make it an important purchase; Internet becoming important information source.
Unsought products		
New unsought	Must be available in places where similar (or related) products are sought; needs attention-getting promotion.	Need for product not strongly felt; unaware of benefits or not yet gone through adoption process.
Regularly unsought	Requires very aggressive promotion, usually personal selling.	Aware of product but not interested; attitude toward product may even be negative.

Staples are products that are bought often, routinely, and without much thought—like breakfast cereal, canned soup, and most other packaged foods used almost every day in almost every household.

Impulse products are products that are bought quickly—as *unplanned* purchases—because of a strongly felt need. True impulse products are items that the customer hadn't planned to buy, decides to buy on sight, may have bought the same way many times before, and wants right now. If the buyer doesn't see an impulse product at the right time, the sale may be lost.[5]

Emergency products are products that are purchased immediately when the need is great. The customer doesn't have time to shop around when a traffic accident occurs, a thunderstorm begins, or an impromptu party starts. The price of the ambulance service, raincoat, or ice cubes won't be important.

Shopping products—are compared

Shopping products are products that a customer feels are worth the time and effort to compare with competing products. Shopping products can be divided into two types, depending on what customers are comparing: (1) homogeneous or (2) heterogeneous shopping products.

Homogeneous shopping products are shopping products the customer sees as basically the same and wants at the lowest price. Some consumers feel that certain sizes and types of computers, television sets, washing machines, and even cars are very similar. So they shop for the best price. For some products, the Internet has become a way to do that quickly.

Many consumers shop for plates and other tableware as if they were homogeneous products, but Crate & Barrel wants customers to see its distinctive offerings as heterogeneous shopping products, or perhaps even specialty items.

Firms may try to emphasize and promote their product differences to avoid head-to-head price competition. For example, EarthLink says that with its dial-up Internet service you get fewer busy signals and lost connections. But if consumers don't think the differences are real or important in terms of the value they seek, they'll just look at price.

Heterogeneous shopping products are shopping products the customer sees as different and wants to inspect for quality and suitability. Furniture, clothing, and membership in a spa are good examples. Often the consumer expects help from a knowledgeable salesperson. Quality and style matter more than price. In fact, once the customer finds the right product, price may not matter at all—as long as it's reasonable. For example, you may have asked a friend to recommend a good dentist without even asking what the dentist charges.

Branding may be less important for heterogeneous shopping products. The more consumers compare price and quality, the less they rely on brand names or labels. Some retailers carry competing brands so consumers won't go to a competitor to compare items.

Specialty products—no substitutes please!

Specialty products are consumer products that the customer really wants and makes a special effort to find. Shopping for a specialty product doesn't mean comparing—the buyer wants that special product and is willing to search for it. It's the customer's *willingness to search*—not the extent of searching—that makes it a specialty product.

Any branded product that consumers insist on by name is a specialty product. Marketing managers want customers to see their products as specialty products and ask for them over and over again. Building that kind of relationship isn't easy. It means satisfying the customer every time. However, that's easier and a lot less costly than trying to win back dissatisfied customers or attract new customers who are not seeking the product at all.

Unsought products—need promotion

Unsought products are products that potential customers don't yet want or know they can buy. So they don't search for them at all. In fact, consumers probably won't buy these products if they see them—unless Promotion can show their value.

There are two types of unsought products. **New unsought products** are products offering really new ideas that potential customers don't know about yet. Informative promotion can help convince customers to accept the product, ending its unsought status. Dannon's yogurt, Litton's microwave ovens, and Netscape's browser are all popular items now, but initially they were new unsought products.

Regularly unsought products are products—like gravestones, life insurance, and encyclopedias—that stay unsought but not unbought forever. There may be a need, but potential customers aren't motivated to satisfy it. For this kind of product, personal selling is *very* important.

Many nonprofit organizations try to "sell" their unsought products. For example, the Red Cross regularly holds blood drives to remind prospective donors of how important it is to give blood.

One product may be seen several ways

We've been looking at product classes one at a time. But the same product might be seen in different ways by different target markets at the same time. For example, a product viewed as a staple by most consumers in the United States, Canada, or some similar affluent country might be seen as a heterogeneous shopping product by consumers in another country. The price might be much higher when considered as a proportion of the consumer's budget, and the available choices might be very different. Similarly, a convenient place to shop often means very different things in different countries. In Japan, for example, retail stores tend to be much smaller and carry smaller selections of products.

Business Products Are Different

Business product classes are also useful for developing marketing mixes—since business firms use a system of buying related to these product classes.

Before looking at business product differences, however, we'll note some important similarities that affect marketing strategy planning.

One demand derived from another

The big difference in the business products market is **derived demand**—the demand for business products derives from the demand for final consumer products. For example, car manufacturers buy about one-fifth of all steel products. But if demand for cars drops, they'll buy less steel. Then even the steel supplier with the best marketing mix is likely to lose sales.[6]

Price increases might not reduce quantity purchased

Total *industry* demand for business products is fairly inelastic. Business firms must buy what they need to produce their own products. Even if the cost of basic silicon doubles, for example, Intel needs it to make computer chips. The increased cost of the silicon won't have much effect on the price of the final computer or on the number of computers consumers demand. Sharp business buyers try to buy as economically as possible. So the demand facing *individual sellers* may be extremely elastic—if similar products are available at a lower price.

Tax treatment affects buying too

How a firm's accountants—and the tax laws—treat a purchase is also important to business customers. An **expense item** is a product whose total cost is treated as a

Businesses buy the goods and services they need to produce products for their own customers, so the demand for GE's special plastic resins, used to make lightweight and impact-resistant body panels, is derived from consumer demand for VW's unique car.

business expense in the year it's purchased. A **capital item** is a long-lasting product that can be used and depreciated for many years. Often it's very expensive. Customers pay for the capital item when they buy it, but for tax purposes the cost is spread over a number of years. This may reduce the cash available for other purchases.

Business Product Classes—How They Are Defined

Business product classes are based on how buyers see products and how the products will be used. The classes of business products are (1) installations, (2) accessories, (3) raw materials, (4) components, (5) supplies, and (6) professional services. Exhibit 9-4 relates these product classes to marketing mix planning.

Installations—a boom-or-bust business

Installations—such as buildings, land rights, and major equipment—are important capital items. One-of-a-kind installations—like office buildings and custom-made machines—generally require special negotiations for each sale. Standardized major equipment is treated more routinely. Even so, negotiations for installations often involve top management and can stretch over months or even years.

Installations are a boom-or-bust business. When sales are high, businesses want to expand capacity rapidly. And if the potential return on a new investment is very attractive, firms may accept any reasonable price. But during a downswing, buyers have little or no need for new installations and sales fall off sharply.[7]

Exhibit 9-4 Business Product Classes and Marketing Mix Planning

Business Product Classes	Marketing Mix Considerations	Buying Behavior
Installations	Usually requires skillful personal selling by producer, including technical contacts, and/or understanding of applications; leasing and specialized support services may be required.	Multiple buying influence (including top management) and new-task buying are common; infrequent purchase, long decision period, and boom-or-bust demand are typical.
Accessory equipment	Need fairly widespread distribution and numerous contacts by experienced and sometimes technically trained personnel; price competition is often intense, but quality is important.	Purchasing and operating personnel typically make decisions; shorter decision period than for installations; Internet sourcing.
Raw materials	Grading is important, and transportation and storing can be crucial because of seasonal production and/or perishable products; markets tend to be very competitive.	Long-term contract may be required to ensure supply; online auctions.
Component parts and materials	Product quality and delivery reliability are usually extremely important; negotiation and technical selling typical on less-standardized items; replacement after market may require different strategies.	Multiple buying influence is common; online competitive bids used to encourage competitive pricing.
Maintenance, repair, and operating (MRO) supplies	Typically require widespread distribution or fast delivery (repair items); arrangements with appropriate middlemen may be crucial.	Often handled as straight rebuys, except important operating supplies may be treated much more seriously and involve multiple buying influence.
Professional services	Services customized to buyer's need; personal selling very important; inelastic demand often supports high prices.	Customer may compare outside service with what internal people could provide; needs may be very specialized.

Business customers usually want a convenient and low-cost way to buy standard equipment and supplies, so many are now turning to vendors who sell over the Internet.

Specialized services are needed as part of the product

Suppliers sometimes include special services with an installation at no extra cost. A firm that sells (or leases) equipment to dentists, for example, may install it and help the dentist learn to use it.

Accessories—important but short-lived capital items

Accessories are short-lived capital items—tools and equipment used in production or office activities—like Canon's small copy machines, Rockwell's portable drills, and Steelcase's filing cabinets.

Since these products cost less and last a shorter time than installations, multiple buying influence is less important. Operating people and purchasing agents, rather than top managers, may make the purchase decision. As with installations, some customers may wish to lease or rent—to expense the cost.

Accessories are more standardized than installations. And they're usually needed by more customers. For example, IBM sells its robotics systems, which can cost over $2 million, as custom installations to large manufacturers. But IBM's Thinkpad computers are accessory equipment for just about every type of modern business all around the world.

Raw materials become part of a physical good

Raw materials are unprocessed expense items—such as logs, iron ore, wheat, and cotton—that are moved to the next production process with little handling. Unlike installations and accessories, *raw materials become part of a physical good and are expense items*.

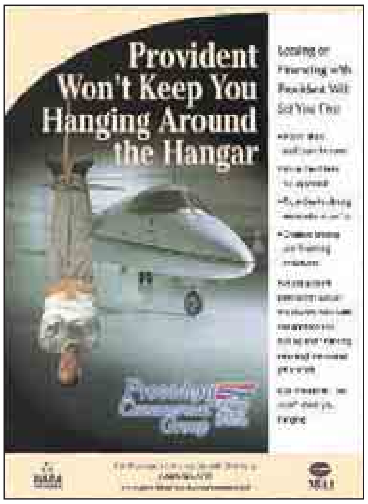
We can break raw materials into two types: (1) farm products and (2) natural products. **Farm products** are grown by farmers—examples are oranges, wheat, sugar cane, cattle, poultry, eggs, and milk. **Natural products** are products that occur in nature—such as fish and game, timber and maple syrup, and copper, zinc, iron ore, oil, and coal.

The need for grading is one of the important differences between raw materials and other business products. Nature produces what it will—and someone must sort and grade raw materials to satisfy various market segments. Top-graded fruits and vegetables may find their way into the consumer products market. Lower grades, which are treated as business products, are used in juices, sauces, and soups.

Most buyers of raw materials want ample supplies in the right grades for specific uses—fresh vegetables for Green Giant's production lines or logs for Weyerhaeuser's paper mills. To ensure steady quantities, raw materials customers often sign long-term contracts, sometimes at guaranteed prices.

Component parts and materials must meet specifications

Components are processed expense items that become part of a finished product. Component *parts* are finished (or nearly finished) items that are ready for assembly into the final product. ATI's graphics cards included in personal computers, TRW's



The ability to arrange a lease or good financial terms is often important in the purchase of a business aircraft or other capital installation. By contrast, component parts become part of a firm's product and are paid for when the expense occurs.

air bags in cars, and Briggs and Stratton's engines for lawn mowers are examples. Component *materials* are items such as wire, plastic, textiles, or cement. They have already been processed but must be processed further before becoming part of the final product. Since components become part of the firm's own product, quality is extremely important.

Components are often produced in large quantity to meet standard specifications. However, some components are custom-made. Then teamwork between the buyer and seller may be needed to arrive at the right specifications. So a buyer may find it attractive to develop a close partnership with a dependable supplier. And top management may be involved if the price is high or the component is extremely important to the final product. In contrast, standardized component materials are more likely to be purchased online using a competitive bidding system.

Since component parts go into finished products, a replacement market often develops. This *after market* can be both large and very profitable. Car tires and batteries are two examples of components originally sold in the *OEM (original equipment market)* that become consumer products in the after market. The target markets are different—and different marketing mixes are usually necessary.[8]

Supplies for maintenance, repair, and operations

Supplies are expense items that do not become part of a finished product. Buyers may treat these items less seriously. When a firm cuts its budget, orders for supplies may be the first to go. Supplies can be divided into three types: (1) maintenance, (2) repair, and (3) operating supplies—giving them their common name: MRO supplies.

Maintenance and small operating supplies are like convenience products. The item will be ordered because it is needed—but buyers won't spend much time on it. Branding may become important because it makes buying easier for such "nuisance" purchases. Breadth of assortment and the seller's dependability are also important. Middlemen usually handle the many supply items, and now they are often purchased via online catalog sites.[9]

If operating supplies are needed regularly, and in large amounts, they receive special treatment. Many companies buy coal and fuel oil in railroad-car quantities. Usually there are several sources for such commodity products—and large volumes may be purchased at global exchanges on the Internet.

Professional services—pay to get it done

Professional services are specialized services that support a firm's operations. They are usually expense items. Engineering or management consulting services can improve the plant layout or the company's efficiency. Information technology services can maintain a company's networks and websites. Design services can suggest a new look for products or promotion materials. Advertising agencies can help promote the firm's products. And food services can improve morale.

Here the *service* part of the product is emphasized. Goods may be supplied—as coffee and doughnuts are with food service—but the customer is primarily interested in the service.

Managers compare the cost of buying professional services outside the firm ("outsourcing") to the cost of having company people do them. For special skills needed only occasionally, an outsider can be the best source. Further, during the last decade, many firms have tried to cut costs by downsizing the number of people that they employ; in many cases, work that was previously done by an employee is now provided as a service by an independent supplier. Clearly, the number of service specialists is growing in our complex economy.

Branding Needs a Strategy Decision Too

There are so many brands—and we're so used to seeing them—that we take them for granted. But branding is an important decision area, so we will treat it in some detail.

What is branding?

Branding means the use of a name, term, symbol, or design—or a combination of these—to identify a product. It includes the use of brand names, trademarks, and practically all other means of product identification.

Brand name has a narrower meaning. A **brand name** is a word, letter, or a group of words or letters. Examples include America Online (AOL), WD-40, 3M Post-its, and PT Cruiser.

Trademark is a legal term. A **trademark** includes only those words, symbols, or marks that are legally registered for use by a single company. A **service mark** is the same as a trademark except that it refers to a service offering.

The word *Buick* can be used to explain these differences. The Buick car is branded under the brand name Buick (whether it's spoken or printed in any manner). When "Buick" is printed in a certain kind of script, however, it becomes a trademark. A trademark need not be attached to the product. It need not even be a word—it can be a symbol. Exhibit 9-5 shows some common trademarks.

These differences may seem technical. But they are very important to business firms that spend a lot of money to protect and promote their brands.

Brands meet needs

Well-recognized brands make shopping easier. Think of trying to buy groceries, for example, if you had to evaluate the advantages and disadvantages of each of 25,000 items every time you went to a supermarket. Many customers are willing to buy new things—but having gambled and won, they like to buy a sure thing the next time.

Brand promotion has advantages for branders as well as customers. A good brand reduces the marketer's selling time and effort. And sometimes a firm's brand name is the only element in its marketing mix that a competitor can't copy. Also, good brands can improve the company's image—speeding acceptance of new products marketed under the same name. For example, many consumers quickly tried

Exhibit 9-5
Recognized Trademarks and Symbols Help in Promotion

Starbucks' coffee-flavored Frappuccino beverage when it appeared on grocery store shelves because they already knew they liked Starbucks' coffee.[10]

Conditions Favorable to Branding

Can you recall a brand name for file folders, bed frames, electric extension cords, or nails? As these examples suggest, it's not always easy to establish a respected brand.

The following conditions are favorable to successful branding:

1. The product is easy to identify by brand or trademark.
2. The product quality is the best value for the price and the quality is easy to maintain.
3. Dependable and widespread availability is possible. When customers start using a brand, they want to be able to continue using it.
4. Demand is strong enough that the market price can be high enough to make the branding effort profitable.
5. There are economies of scale. If the branding is really successful, costs should drop and profits should increase.
6. Favorable shelf locations or display space in stores will help. This is something retailers can control when they brand their own products. Producers must use aggressive salespeople to get favorable positions.

In general, these conditions are less common in less-developed economies, and that may explain why efforts to build brands in less-developed nations often fail.

Achieving Brand Familiarity Is Not Easy

The earliest and most aggressive brand promoters in America were the patent medicine companies. They were joined by the food manufacturers, who grew in size after the Civil War. Some of the brands started in the 1860s and 1870s (and still

It takes time and money to build brand awareness, so sometimes brands can be extended. Both Bounce and Mr. Clean have recently introduced new products that benefit from their well-recognized brand names.

going strong) are Borden's Condensed Milk, Quaker Oats, Pillsbury's Best Flour, and Ivory Soap. Today, familiar brands exist for most product categories, ranging from crayons (Crayola) to real estate services (Century 21). However, what brand is familiar often varies from one country to another.

Brand acceptance must be earned with a good product and regular promotion. **Brand familiarity** means how well customers recognize and accept a company's brand. The degree of brand familiarity affects the planning for the rest of the marketing mix—especially where the product should be offered and what promotion is needed.

Five levels of brand familiarity

Five levels of brand familiarity are useful for strategy planning: (1) rejection, (2) nonrecognition, (3) recognition, (4) preference, and (5) insistence.

Some brands have been tried and found wanting. **Brand rejection** means that potential customers won't buy a brand unless its image is changed. Rejection may suggest a change in the product or perhaps only a shift to target customers who have a better image of the brand. Overcoming a negative image is difficult and can be very expensive.

Brand rejection is a big concern for service-oriented businesses because it's hard to control the quality of service. A business traveler who gets a dirty room in a Hilton Hotel in Caracas, Venezuela, might not return to a Hilton anywhere. Yet it's difficult for Hilton to ensure that every maid does a good job every time.

Some products are seen as basically the same. **Brand nonrecognition** means final consumers don't recognize a brand at all—even though middlemen may use the brand name for identification and inventory control. Examples include school supplies, inexpensive dinnerware, many of the items that you'd find in a hardware store, and thousands of dot-coms on the Internet.

Brand recognition means that customers remember the brand. This may not seem like much, but it can be a big advantage if there are many "nothing" brands on the market. Even if consumers can't recall the brand without help, they may be reminded when they see it in a store among other less familiar brands.

Most branders would like to win **brand preference**—which means that target customers usually choose the brand over other brands, perhaps because of habit or favorable past experience.

Brand insistence means customers insist on a firm's branded product and are willing to search for it. This is an objective of many target marketers.

Exhibit 9-6 Characteristics of a Good Brand Name

- Short and simple
- Easy to spell and read
- Easy to recognize and remember
- Easy to pronounce
- Can be pronounced in only one way
- Can be pronounced in all languages (for international markets)
- Suggestive of product benefits
- Adaptable to packaging/labeling needs
- No undesirable imagery
- Always timely (does not go out-of-date)
- Adaptable to any advertising medium
- Legally available for use (not in use by another firm)

The right brand name can help

A good brand name can help build brand familiarity. It can help tell something important about the company or its product. Exhibit 9-6 lists some characteristics of a good brand name. Some successful brand names seem to break all these rules, but many of them got started when there was less competition.

Companies that compete in international markets face a special problem in selecting brand names. A name that conveys a positive image in one language may be meaningless in another. Or, worse, it may have unintended meanings. GM's Nova car is a classic example. GM stuck with the Nova name when it introduced the car in South America. It seemed like a sensible decision because *nova* is the Spanish word for star. However, Nova also sounds the same as the Spanish words for "no go." Consumers weren't interested in a no-go car, and sales didn't pick up until GM changed the name.[11]

A respected name builds brand equity

Because it's costly to build brand recognition, some firms prefer to acquire established brands rather than try to build their own. The value of a brand to its current owner or to a firm that wants to buy it is sometimes called **brand equity**—the value of a brand's overall strength in the market. For example, brand equity is likely to be higher if many satisfied customers insist on buying the brand and if retailers are eager to stock it. That almost guarantees ongoing profits.

Traditional financial statements don't show brand equity or the future profit potential of having close relationships with a large base of satisfied customers. Perhaps they should. Having that information would prompt a lot of narrow-thinking finance managers to view marketing efforts as an investment, not just as an expense.

The financial value of the Yahoo brand name illustrates this point. In 1994, Yahoo was just a tiny start-up trying to make it with a directory site on the Internet. Most people had never heard the name, and for that matter few even knew what the Internet was or why you'd need a directory site. As interest in the Internet grew, Yahoo promoted its brand name, not just on the Internet but in traditional media like TV and magazines. It was often the only website name that newcomers to the web knew, so for many it was a good place from which to start their surfing. When they found the Yahoo site useful, they'd tell their friends—and that generated more familiarity with the name and more hits on the site. Within a few years—even before the Internet really took off—Yahoo was attracting 30 million different people a month and 95 million web page views a day. Since Yahoo's original marketing plan was to make money by charging fees to advertisers eager to reach the hordes of people who visit Yahoo's web pages, the familiarity of its brand translated directly into ad revenues. Because it attracted traffic and ad revenue, it could offer users more specialized content, better search capability, free e-mail, community offerings, and e-commerce. And now, in less than a decade, it's become one of the best known brands not only in cyberspace but in the world.[12]

www.mhhe.com/fourps

How to Blow Out a Relationship with Customers

There are few brand names that are more familiar to U.S. consumers than Firestone and Ford Explorer. Yet in the aftermath of tread separations on tires that resulted in many rollovers and tragic deaths, the reputations of these once lofty brand names are seriously tarnished. There are millions of consumers who say that they will never again buy any tire with the Firestone name on it. The Firestone brand may not survive. The plant where many of the unsafe tires were produced has already been shut down. What automaker would buy from that plant and risk its own image and sales. Tire retailers who sell replacement tires in the consumer market face similar reactions. It's easier for them to just sell Michelins, a brand that positions itself on safety benefits.

In part to protect its customers, Ford recalled millions of Firestone tires, including many designs that Firestone says are not a problem. Who should pay the cost? Unlike most of the components used in building a car, the tires are covered by a Firestone warranty, not by Ford's warranty. Responsibility is clearer in government recalls. But staff shortages at the National Highway Traffic Safety Administration contributed to delays in figuring out who was really at fault.

The long-standing relationship between Ford and Firestone is severed. Imagine how you would feel if you were Bill Ford, chairman of Ford. Firestone was his grandfather. That aside, questions about rollovers have eroded the brand equity of one of the best sellers in Ford's whole product line. Rebuilding profits won't be easy. With all the bad publicity customers are very concerned about rollover hazards of the Explorer. Even if a complete redesign would help reassure them, that's not an option. The new-product development process for a big change in the Explorer will take years.[13]

Protecting Brand Names and Trademarks

U.S. common law and civil law protect the rights of trademark and brand name owners. The **Lanham Act** (of 1946) spells out what kinds of marks (including brand names) can be protected and the exact method of protecting them. The law applies to goods shipped in interstate or foreign commerce.

The Lanham Act does not force registration. But registering under the Lanham Act is often a first step toward protecting a trademark to be used in international markets. That's because some nations require that a trademark be registered in its home country before they will register or protect it.

You must protect your own

A brand can be a real asset to a company. Each firm should try to see that its brand doesn't become a common descriptive term for its kind of product. When this happens, the brand name or trademark becomes public property—and the owner loses all rights to it. This happened with the names cellophane, aspirin, shredded wheat, and kerosene.[14]

Counterfeiting is accepted in some cultures

Even when products are properly registered, counterfeiters may make unauthorized copies. Many well-known brands—ranging from Levi's jeans to Rolex watches to Zantax ulcer medicine—face this problem. Counterfeiting is especially common in developing nations. In China, most videotapes and CDs are bootleg copies. Counterfeiting is big business in some countries, so efforts to stop it may meet with limited success. There are also differences in cultural values. In South Korea, for example, many people don't see counterfeiting as unethical.[15]

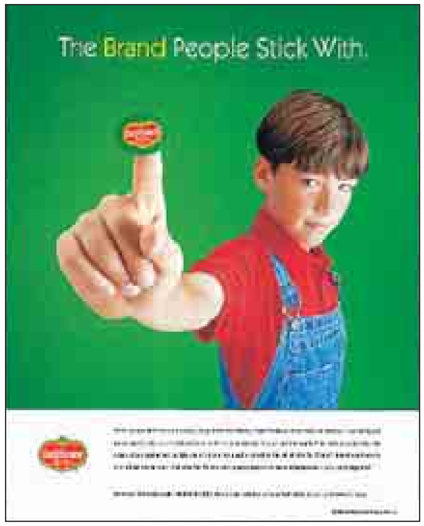
What Kind of Brand to Use?

Keep it in the family

Branders of more than one product must decide whether they are going to use a **family brand**—the same brand name for several products—or individual brands for each product. Examples of family brands are Keebler snack food products and Sears' Kenmore appliances.

The use of the same brand for many products makes sense if all are similar in type and quality. The main benefit is that the goodwill attached to one or two

As these trade ads suggest, both Del Monte and GE want retailers to remember that many consumers already know and trust their brand names.



products may help the others. Money spent to promote the brand name benefits more than one product, which cuts promotion costs for each product.

A special kind of family brand is a **licensed brand**—a well-known brand that sellers pay a fee to use. For example, the familiar Sunkist brand name has been licensed to many companies for use on more than 400 products in 30 countries.[16]

Individual brands for outside and inside competition

A company uses **individual brands**—separate brand names for each product—when it's important for the products to each have a separate identity, as when products vary in quality or type.

If the products are really different, such as Elmer's glue and Borden's ice cream, individual brands can avoid confusion. Some firms use individual brands with similar products to make segmentation and positioning efforts easier. Unilever, for example, markets Aim, Close-Up, and Pepsodent toothpastes, but each involves different positioning efforts.

Internet

Internet Exercise Go to the Procter & Gamble website (www.pg.com) and click on *Product List and Info* and then on *Beauty Care.* Find out the brand names of the different shampoos that P&G makes. How are the different brands positioned, and what target markets do they appeal to?

Sometimes firms use individual brands to encourage competition within the company. Each brand is managed by a different group within the firm. They argue that if anyone is going to take business away from their firm, it ought to be their own brand. However, many firms that once used this approach have reorganized. Faced with slower market growth, they found they had plenty of competitive pressure from other firms. The internal competition just made it more difficult to coordinate different marketing strategies.[17]

Generic "brands"

Products that some consumers see as commodities may be difficult or expensive to brand. Some manufacturers and middlemen have responded to this problem with **generic products**—products that have no brand at all other than identification of their contents and the manufacturer or middleman. Generic products are usually offered in plain packages at lower prices. They are quite common in less-developed nations.[18]

Who Should Do the Branding?

Manufacturer brands versus dealer brands

Manufacturer brands are brands created by producers. These are sometimes called *national brands* because the brand is promoted all across the country or in large regions. Note, however, that many manufacturer brands are now distributed globally. Such brands include Nabisco, Campbell's, Whirlpool, Ford, and IBM. Many creators of service-oriented firms—like McDonald's, Orkin Pest Control, and Midas Muffler—promote their brands this way too.

Dealer brands, also called **private brands,** are brands created by middlemen. Examples of dealer brands include the brands of Kroger, Ace Hardware, Radio Shack, Wal-Mart, and Sears. Some of these are advertised and distributed more widely than many national brands. For example, national TV ads have helped Original Arizona Jeans (by JCPenney) and Canyon River Blues (by Sears) compete with Levi's and Wrangler.

From the middleman's perspective, the major advantage of selling a popular manufacturer brand is that the product is already presold to some target customers. Such products may bring in new customers and can encourage higher turnover with reduced selling cost. The major disadvantage is that manufacturers normally offer lower gross margins than the middleman might be able to earn with a dealer brand. In addition, the manufacturer maintains control of the brand and may withdraw it from a middleman at any time. Customers, loyal to the brand rather than to the retailer or wholesaler, may go elsewhere if the brand is not available.

Dealer branders take on more responsibility. They must promote their own product. They must be able to arrange a dependable source of supply and usually have to buy in fairly large quantities. This increases their risk and cost of carrying inventory. However, these problems are easier to overcome if the middleman deals in a large sales volume, as is the case with many large retail chains.

Who's winning the battle of the brands?

The **battle of the brands,** the competition between dealer brands and manufacturer brands, is just a question of whose brands will be more popular and who will be in control.

At one time, manufacturer brands were much more popular than dealer brands. Now sales of both kinds of brands are about equal—but sales of dealer brands are expected to continue growing. Middlemen have some advantages in this battle. With the number of large wholesalers and retail chains growing, they are better able to arrange reliable sources of supply at low cost. They can also control the point of sale and give the dealer brand special shelf position or promotion.

Innovative packaging turns Yoplait Go-Gurt into an on-the-go yogurt snack for kids and makes Colombo yogurt more convenient (with its spoon-in-lid feature).

Exhibit 9-7 Some Ways Packaging Benefits Consumers and Marketers

Opportunity to Add Value	Some Decision Factors	Examples
Promotion	Link product to promotion	The bunny on the Energizer battery package is a reminder that it "keeps going and going."
	Branding at point of purchase or consumption	Coke's logo greets almost everyone each time the refrigerator is opened.
	Product information	Kraft's nutrition label helps consumers decide which cheese to buy, and a UPC code reduces checkout time and errors.
Protection	For shipping and storing	Sony's MP3 player is kept safe by Styrofoam inserts.
	From spoiling	Tylenol's safety seal prevents tampering.
	From shoplifting	Cardboard hang-tag on Gillette razor blades is too large to hide in hand.
Enhance product	The environment	Tide detergent bottle can be recycled.
	Convenience in use	Squeezable tube of Yoplait Go-Gurt is easy to eat on the go and in new situations.
	Added product functions	Plastic tub is useful for refrigerator leftovers after the Cool Whip is gone.

Consumers benefit from the battle. Competition has already narrowed price differences between manufacturer brands and well-known dealer brands. And big retailers like Wal-Mart are constantly pushing manufacturers to lower prices—because national brands at low prices bring in even more customers than store brands.[19]

The Strategic Importance of Packaging

Packaging involves promoting, protecting, and enhancing the product. Packaging can be important to both sellers and customers. See Exhibit 9-7. It can make a product more convenient to use or store. It can prevent spoiling or damage. Good packaging makes products easier to identify and promotes the brand at the point of purchase and even in use.

Packaging can enhance the product

A new package can make *the* important difference in a new marketing strategy—by meeting customers' needs better. Sometimes a new package makes the product easier or safer to use. For example, Quaker State oil comes with a twist-off top and pouring spout to make it more convenient for customers at self-service gas stations. And most drug and food products now have special seals to prevent product tampering.

Clever packaging is an important part of an effort by Dean's Foods to pump new life into an old product—milk. Just as Bird's Eye did with frozen vegetables, Dean wants to make milk something more than a cheap commodity. Dean is selling six-packs of chocolate-flavored milk in bottles called chugs—lightweight plastic bottles designed like old-fashioned milk bottles with a wide mouth, but with resealable twist-off caps. The shape of the new package also helps

Dean get distribution in convenience stores and vending machines. Of course, storing milk for long or shipping it large distances is still a problem because milk is perishable. But Dean is working on packaging technology that will keep milk fresh for 60 days. For now, Dean is introducing a blue-ice freezer pack that keeps a six-pack of milk cold so people can take it to work or school. The package is also the focus of an ad campaign that positions the new product as hip. The ad shows a chug of milk in a back jeans pocket with the tagline, "Milk where you want it."[20]

Packaging sends a message

Packaging can tie the product to the rest of the marketing strategy. Packaging for Energizer batteries features the pink bunny seen in attention-getting TV ads and reminds consumers that the batteries are durable. A good package sometimes gives a firm more promotion effect than it could get with advertising. Customers see the package in stores, when they're actually buying.

Packaging may lower distribution costs

Better protective packaging is very important to manufacturers and wholesalers. They sometimes have to pay the cost of goods damaged in shipment. Retailers need protective packaging too. It can reduce storing costs by cutting breakage, spoilage, and theft. Good packages save space and are easier to handle and display.[21]

Universal product codes speed handling

To speed handling of fast-selling products, government and industry representatives have developed a **universal product code (UPC)** that identifies each product with marks readable by electronic scanners. A computer then matches each code to the product and its price. Supermarkets and other high-volume retailers have been eager to use these codes. They speed the checkout process and reduce the need to mark the price on every item. They also reduce errors by cashiers and make it easy to control inventory and track sales of specific products.[22]

What Is Socially Responsible Packaging?

Laws reduce confusion and clutter

In the United States, consumer criticism finally led to the passage of the **Federal Fair Packaging and Labeling Act** (of 1966)—which requires that consumer goods be clearly labeled in easy-to-understand terms—to give consumers more information. The law also calls on industry to try to reduce the number of package sizes and make labels more useful. Since then there have been further guidelines. The most far-reaching are based on the Nutrition Labeling and Education Act of 1990. It requires food manufacturers to use a uniform format and disclose what is in their products. The idea was to allow consumers to compare the nutritional value of different products. That could be a plus, and may even lead to healthier diets. However, the Food and Drug Administration estimated that the total cost to change 250,000 food labels in the U.S. marketplace was over $1.4 billion. Ultimately, all consumers shared the cost of those changes, whether they use the information or not.[23]

Internet

Internet Exercise The FDA's website has a page on the food label requirements that proclaims "grocery store aisles have become avenues to greater nutritional knowledge." Go to that page at Internet address (www.fda.gov/opacom/backgrounders/foodlabel/newlabel.html) and review the actual label requirements. Do you use this information in deciding what products to buy?

Current laws also offer more guidance on environmental issues. Some states require a consumer to pay a deposit on bottles and cans until they're returned. These laws mean well, but they can cause problems. Channels of distribution are usually set up to distribute products, not return empty packages.[24]

Ethical decisions remain

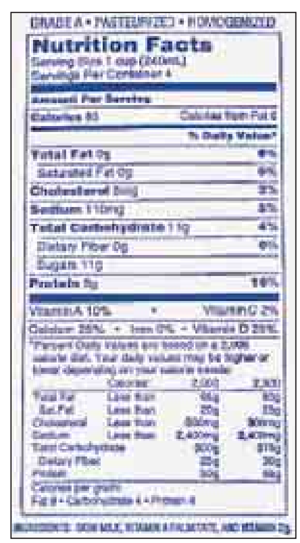
Although various laws provide guidance on many packaging issues, many areas still require marketing managers to make ethical choices. For example, some firms have been criticized for designing packages that conceal a downsized product, giving consumers less for the money. Similarly, some retailers design packages and labels for their private-label products that look just like, and are easily confused with, manufacturer brands. Are efforts such as these unethical, or are they simply an attempt to make packaging a more effective part of a marketing mix? Different people will answer differently.

Some marketing managers promote environmentally friendly packaging on some products while simultaneously increasing the use of problematic packages on others. Empty packages now litter our streets, and some plastic packages will lie in a city dump for decades. But some consumers like the convenience that accompanies these problems. Is it unethical for a marketing manager to give consumers with different preferences a choice? Some critics argue that it is; others praise firms that give consumers a choice.

Many critics feel that labeling information is too often incomplete or misleading. Do consumers really understand the nutritional information required by law? Further, some consumers want information that is difficult, perhaps even impossible, to provide. For example, how can a label accurately describe a product's taste or texture? But the ethical issues usually focus on how far a marketing manager should go in putting potentially negative information on a package. For example, should Häagen-Dazs affix a label that says "this product will clog your arteries"? That sounds extreme, but what type of information *is* appropriate?[25]

Unit-pricing is a possible help

Some retailers, especially large supermarket chains, make it easier for consumers to compare packages with different weights or volumes. They use **unit-pricing**—which involves placing the price per ounce (or some other standard measure) on or near the product. This makes price comparison easier.[26]



Food label requirements help some consumers make healthier purchases, but many consumers don't understand or use the information.

Warranty Policies Are a Part of Strategy Planning

Warranty puts promises in writing

A **warranty** explains what the seller promises about its product. A marketing manager should decide whether to offer a specific warranty, and if so what the warranty will cover and how it will be communicated to target customers. This is an area where the legal environment—as well as customer needs and competitive offerings—must be considered.

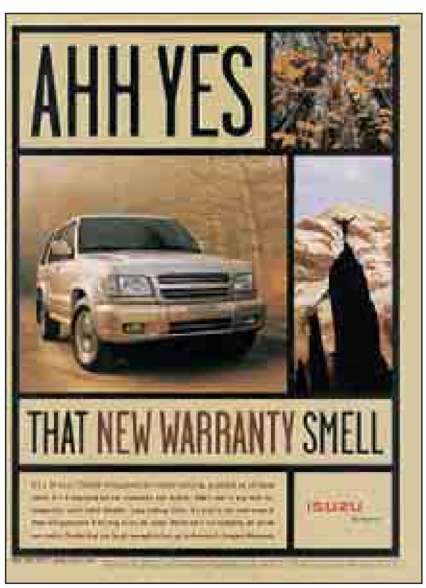
U.S. common law says that producers must stand behind their products—even if they don't offer a specific warranty. A written warranty provided by the seller may promise more than the common law provides. However, it may actually *reduce* the responsibility a producer would have under common law.

The federal **Magnuson-Moss Act** (of 1975) says that producers must provide a clearly written warranty if they choose to offer any warranty. The warranty does not have to be strong. However, Federal Trade Commission (FTC) guidelines try to ensure that warranties are clear and definite and not deceptive or unfair. A warranty must also be available for inspection before the purchase.

Some firms used to say their products were fully warranted or absolutely guaranteed. However, they didn't state the time period or spell out the meaning of the warranty. Now a company has to make clear whether it's offering a full or limited warranty—and the law defines what *full* means. Most firms offer a limited warranty, if they offer one at all.

Warranty may improve the marketing mix

Some firms use warranties to improve the appeal of their marketing mix. They design more quality into their goods or services and offer refunds or replacement, not just repair, if there is a problem. Xerox Corp. uses this approach with its copy machines. Its three-year warranty says that a customer who is not satisfied with a copier—for *any* reason—can trade it for another model. This type of warranty sends a strong signal. A buyer doesn't have to worry about whether the copier will work as expected, service calls will be prompt, or even that the Xerox salesperson or dealer has recommended the appropriate model.



In a competitive market, a product warranty or a service guarantee can be a very important part of the marketing mix.

Service guarantees

Customer service guarantees are becoming more common as a way to attract, and keep, customers. Pizza Hut guarantees a luncheon pizza in five minutes or it's free. General Motors set up a fast-oil-change guarantee to compete with fast-lube specialists who were taking customers away from dealers. If the dealer doesn't get the job done in 29 minutes or less, the next oil change is free. The Hampton Inn motel chain guarantees "100% satisfaction." All employees, even the cleaning crews, are empowered to offer an unhappy customer a discount or refund on the spot.

There's more risk in offering a service guarantee than a warranty on a physical product. An apathetic employee or a service breakdown can create a big expense. However, without the guarantee, dissatisfied customers may just go away mad without ever complaining. When customers collect on a guarantee, the company can clearly identify the problem. Then the problem can be addressed.

Warranty support can be costly

The cost of warranty support ultimately must be covered by the price that consumers pay. This has led some firms to offer warranty choices. The basic price for a product may include a warranty that covers a short time period or that covers parts but not labor. Consumers who want more or better protection pay extra for an extended warranty or a service contract.[27]

Conclusion

In this chapter, we looked at Product very broadly. A product may not be a physical good at all. It may be a service or it may be some combination of goods and services—like a meal at a restaurant. Most important, we saw that a firm's Product is *what satisfies the needs of its target market*.

We introduced consumer product and business product classes and showed their affect on planning marketing mixes. Consumer product classes are based on consumers' buying behavior. Business product classes are based on how buyers see the products and how they are used. Knowing these product classes—and learning how marketers handle specific products within these classes—will help you develop your marketing sense.

The fact that different people may see the same product in different product classes helps explain why seeming competitors may succeed with very different marketing mixes.

Branding and packaging can create new and more satisfying products. Packaging offers special opportunities to promote the product and inform customers. Variations in packaging can make a product attractive to different target markets. A specific package may have to be developed for each strategy.

Customers see brands as a guarantee of quality, and this leads to repeat purchasing. For marketers, such routine buying means lower promotion costs and higher sales.

Should companies stress branding? The decision depends on whether the costs of brand promotion and honoring the brand guarantee can be more than covered by a higher price or more rapid turnover, or both. The cost of branding may reduce pressure on the other three Ps.

Branding gives marketing managers a choice. They can add brands and use individual or family brands. In the end, however, customers express their approval or disapproval of the whole Product (including the brand). The degree of brand familiarity is a measure of the marketing manager's ability to carve out a separate market. And brand familiarity affects Place, Price, and Promotion decisions.

Warranties are also important in strategy planning. A warranty need not be strong—it just has to be clearly stated. But some customers find strong warranties attractive.

Product is concerned with much more than physical goods and services. To succeed in our increasingly competitive markets, the marketing manager must also be concerned about packaging, branding, and warranties.

Questions and Problems

1. Define, in your own words, what a Product is.
2. Discuss several ways in which physical goods are different from pure services. Give an example of a good and then an example of a service that illustrates each of the differences.
3. What products are being offered by a shop that specializes in bicycles? By a travel agent? By a supermarket? By a new car dealer?
4. What kinds of consumer products are the following: *(a)* watches, *(b)* automobiles, and *(c)* toothpastes? Explain your reasoning.
5. Consumer services tend to be intangible, and goods tend to be tangible. Use an example to explain how the lack of a physical good in a pure service might affect efforts to promote the service.
6. How would the marketing mix for a staple convenience product differ from the one for a homogeneous shopping product? How would the mix for a specialty product differ from the mix for a heterogeneous shopping product? Use examples.
7. Give an example of a product that is a *new* unsought product for most people. Briefly explain why it is an unsought product.
8. In what types of stores would you expect to find *(a)* convenience products, *(b)* shopping products, *(c)* specialty products, and *(d)* unsought products?
9. Cite two examples of business products that require a substantial amount of service in order to be useful.
10. Explain why a new law office might want to lease furniture rather than buy it.
11. Would you expect to find any wholesalers selling the various types of business products? Are retail stores required (or something like retail stores)?
12. What kinds of business products are the following: *(a)* lubricating oil, *(b)* electric motors, and *(c)* a firm that provides landscaping and grass mowing for an apartment complex? Explain your reasoning.
13. How do raw materials differ from other business products? Do the differences have any impact on their marketing mixes? If so, what specifically?
14. For the kinds of business products described in this chapter, complete the following table (use one or a few well-chosen words).
    1. *Kind of distribution facility(ies) needed and functions they will provide.*
    2. *Caliber of salespeople required.*
    3. *Kind of advertising required.*

Products	1	2	3
Installations			
Buildings and land rights			
Major equipment			
Standard			
Custom-made			
Accessories			
Raw materials			
Farm products			
Natural products			
Components			
Supplies			
Maintenance and small operating supplies			
Operating supplies			
Professional services			

15. Is there any difference between a brand name and a trademark? If so, why is this difference important?
16. Is a well-known brand valuable only to the owner of the brand?
17. Suggest an example of a product and a competitive situation where it would *not* be profitable for a firm to spend large sums of money to establish a brand.
18. List five brand names and indicate what product is associated with the brand name. Evaluate the strengths and weaknesses of the brand name.
19. Explain family brands. Should Toys "R" Us carry its own dealer brands to compete with some of the popular manufacturer brands it carries? Explain your reasons.
20. In the past, Sears emphasized its own dealer brands. Now it is carrying more well-known manufacturer brands. What are the benefits to Sears of carrying more manufacturer brands?
21. What does the degree of brand familiarity imply about previous and future promotion efforts? How does the degree of brand familiarity affect the Place and Price variables?

22. You operate a small hardware store with emphasis on manufacturer brands and have barely been breaking even. Evaluate the proposal of a large wholesaler who offers a full line of dealer-branded hardware items at substantially lower prices. Specify any assumptions necessary to obtain a definite answer.
23. Give an example where packaging costs probably *(a)* lower total distribution costs and *(b)* raise total distribution costs.
24. Is it more difficult to support a warranty for a service than for a physical good? Explain your reasons.

Suggested Cases

1. McDonald's "Seniors" Restaurant
13. Paper Supplies Corporation

Computer-Aided Problem

9. **Branding Decision**

Wholesteen Dairy, Inc., produces and sells Wholesteen brand condensed milk to grocery retailers. The overall market for condensed milk is fairly flat, and there's sharp competition among dairies for retailers' business. Wholesteen's regular price to retailers is $8.88 a case (24 cans). FoodWorld—a fast-growing supermarket chain and Wholesteen's largest customer—buys 20,000 cases of Wholesteen's condensed milk a year. That's 20 percent of Wholesteen's total sales volume of 100,000 cases per year.

FoodWorld is proposing that Wholesteen produce private label condensed milk to be sold with the FoodWorld brand name. FoodWorld proposes to buy the same total quantity as it does now, but it wants half (10,000 cases) with the Wholesteen brand and half with the FoodWorld brand. FoodWorld wants Wholesteen to reduce costs by using a lower-quality can for the FoodWorld brand. That change will cost Wholesteen $.01 less per can than it costs for the cans that Wholesteen uses for its own brand. FoodWorld will also provide preprinted labels with its brand name—which will save Wholesteen an additional $.02 a can.

Wholesteen spends $70,000 a year on promotion to increase familiarity with the Wholesteen brand. In addition, Wholesteen gives retailers an allowance of $.25 per case for their local advertising, which features the Wholesteen brand. FoodWorld has agreed to give up the advertising allowance for its own brand, but it is only willing to pay $7.40 a case for the milk that will be sold with the FoodWorld brand name. It will continue under the old terms for the rest of its purchases.

Sue Glick, Wholesteen's marketing manager, is considering the FoodWorld proposal. She has entered cost and revenue data on a spreadsheet—so she can see more clearly how the proposal might affect revenue and profits.

a. *Based on the data in the initial spreadsheet, how will Wholesteen profits be affected if Glick accepts the FoodWorld proposal?*
b. *Glick is worried that FoodWorld will find another producer for the FoodWorld private label milk if Wholesteen rejects the proposal. This would immediately reduce Wholesteen's annual sales by 10,000 cases. FoodWorld might even stop buying from Wholesteen altogether. What would happen to profits in these two situations?*
c. *FoodWorld is rapidly opening new stores and sells milk in every store. The FoodWorld buyer says that next year's purchases could be up to 25,000 cases of Wholesteen's condensed milk. But Sue Glick knows that FoodWorld may stop buying the Wholesteen brand and want all 25,000 cases to carry the FoodWorld private label brand. How will this affect profit? (Hint: enter the new quantities in the "proposal" column of the spreadsheet.)*
d. *What should Wholesteen do? Why?*

For additional questions related to this problem, see Exercise 9-5 in the *Learning Aid for Use with Basic Marketing*, 14th edition.

When You Finish This Chapter, You Should

1. Understand how product life cycles affect strategy planning.

2. Know what is involved in designing new products and what "new products" really are.

3. Understand the new-product development process.

4. See why product liability must be considered in screening new products.

5. Understand the need for product or brand managers.

6. Understand the important new terms (shown in red).

Chapter Ten

Product Management and New-Product Development

In today's markets, a few years can bring a lot of changes. When Palm introduced its first personal digital assistant (PDA) in the mid 1990s, it was a really new product concept—even in the eyes of its target market of gadget-loving, on-the-go executives. It didn't do anything radical, but it did a few important things really well. It could store thousands of names and addresses, track expenses, schedule meetings and priorities, and program calculations. And it was easy to use, which helped Palm sell a million units in just the first two years. As sales growth accelerated, Palm introduced new models with more features—like its connected organizer that could "beam" data to another Palm or a computer and even connect to e-mail anywhere anytime.

During those early years, Palm had little direct competition.

price

place

promotion

produc

Customers around the world bought 13 million PDAs in five years, and 75 percent of them were Palms. Business customers were not very price-sensitive, so without much competition Palm also enjoyed great profit margins.

Palm's marketing plan for its new m500 series (www.palm.com) was to improve graphics and power and add modular features like a digital camera and digital notepad for handwritten e-mail. While these were not big changes for the PDA market, they probably looked revolutionary to the marketing managers for DayTimer's pen-and-paper organizers, Timex's DataLink watches, HP's programmable calculators, IBM's Thinkpad laptops, and Motorola's digital pagers. The marketing managers for these products may not have seen the changes to the new m500 or the original PDA as a competitor. Yet when a firm finds a better way to meet customer needs, it disrupts old ways of doing things. And PDAs were taking business from other categories, even digital cameras.

But Palm wasn't immune to the forces of competition either. Its profits, and the growth of the PDA market, attracted rivals. Casio, IBM, Sharp, Psion, HP, and others jumped into the fray. For example, just as Palm was hoping to get growth from sales to students and other price-sensitive consumers, Handspring made big inroads with colorful, low-priced models. Similarly, Compaq's iPaq and other brands chipped away at the high end of the market with units using Microsoft's new Pocket PC operating system. Many users who wanted feature-packed PDAs with more power and better screens thought the Pocket PC had benefits that Palm's system missed. As a weak economy eroded demand, price competition on high-end PDAs wiped out Palm's profit margins. It also didn't help that Palm's new-product development process hit delays. When its new model didn't come out on schedule, even loyal customers looked elsewhere.

Given the fast changes in this market environment, it's hard to know what will happen in the future or how marketing strategies may change. Soon a PDA may just be a promotional giveaway with a subscription to some service—like wireless video teleconferencing over the Internet. Or the really big market may be kids—if PDA makers build in more interactive gaming features.[1]

Managing Products over Their Life Cycles

The life and death cycle seen in our Palm case is being repeated over and over again in product-markets worldwide. Cellular phones are replacing shortwave radios and CBs and also making it possible for people to communicate from places where it was previously impossible. Cellular linkups over the Internet are coming on strong. Cassette tapes replaced vinyl records, and now CDs, digital minidiscs, and even VHS tapes are challenged by DVD and MP3 digital files on miniature electronic memory cards. Switchboard operators in many firms were replaced with answering machines, and then answering machines lost ground to voice mail services. "Video messaging" over the Internet is now beginning to replace voice mail.

These innovations show that products, markets, and competition change over time. This makes marketing management an exciting challenge. Developing new products and managing existing products to meet changing conditions is important to the success of every firm. In this chapter, we will look at some important ideas in these areas.

Revolutionary products create new product-markets. Competitors are always developing and copying new ideas and products—making existing products out-of-date more quickly than ever. Products, like consumers, go through life cycles. So product planning and marketing mix planning are important.

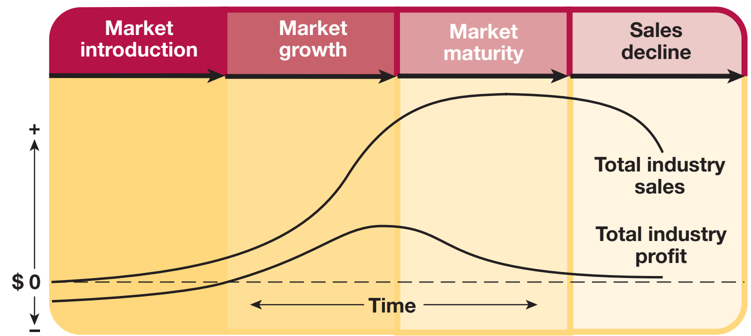
Product life cycle has four major stages

The **product life cycle** describes the stages a really new product idea goes through from beginning to end. The product life cycle is divided into four major stages: (1) market introduction, (2) market growth, (3) market maturity, and (4) sales decline. The product life cycle is concerned with new types (or categories) of product in the market, not just what happens to an individual brand.

A particular firm's marketing mix usually must change during the product life cycle. There are several reasons why. Customers' attitudes and needs may change over the product life cycle. The product may be aimed at entirely different target markets at different stages. And the nature of competition moves toward pure competition or oligopoly.

Further, total sales of the product—by all competitors in the industry—vary in each of its four stages. They move from very low in the market introduction stage to high at market maturity and then back to low in the sales decline stage. More important, the profit picture changes too. These general relationships can be seen in Exhibit 10-1. Note that sales and profits do not move together over time. *Industry profits decline while industry sales are still rising.*[2]

Exhibit 10-1
Typical Life Cycle of a New Product Concept



Market introduction—investing in the future

In the **market introduction** stage, sales are low as a new idea is first introduced to a market. Customers aren't looking for the product. Even if the product offers superior value, customers don't even know about it. Informative promotion is needed to tell potential customers about the advantages and uses of the new product concept.

Even though a firm promotes its new product, it takes time for customers to learn that the product is available. Most companies experience losses during the introduction stage because they spend so much money for Promotion, Product, and Place development. Of course, they invest the money in the hope of future profits.

Market growth—profits go up and down

In the **market growth** stage, industry sales grow fast—but industry profits rise and then start falling. The innovator begins to make big profits as more and more customers buy. But competitors see the opportunity and enter the market. Some just copy the most successful product or try to improve it to compete better. Others try to refine their offerings to do a better job of appealing to some target markets. The new entries result in much product variety. So monopolistic competition—with down-sloping demand curves—is typical of the market growth stage.

This is the time of biggest profits *for the industry*. It is also a time of rapid sales and earnings growth for companies with effective strategies. *But it is toward the end of this stage when industry profits begin to decline* as competition and consumer price sensitivity increase. See Exhibit 10-1.

Some firms make big strategy planning mistakes at this stage by not understanding the product life cycle. They see the big sales and profit opportunities of the early market growth stage but ignore the competition that will soon follow. When they realize their mistake, it may be too late. This happened with many dot-coms during the late 1990s. Marketing managers who understand the cycle and pay attention to competitor analysis are less likely to encounter this problem.

Market maturity—sales level off, profits continue down

The **market maturity** stage occurs when industry sales level off and competition gets tougher. Many aggressive competitors have entered the race for profits—except in oligopoly situations. Industry profits go down throughout the market maturity stage because promotion costs rise and some competitors cut prices to attract business. Less efficient firms can't compete with this pressure—and they drop out of the market. Even in oligopoly situations, there is a long-run downward pressure on prices.

New firms may still enter the market at this stage—increasing competition even more. Note that late entries skip the early life-cycle stages, including the profitable market growth stage. And they must try to take a share of the saturated market from established firms, which is difficult and expensive. The market leaders have a lot at stake, so they usually will fight hard to defend their market share and revenue stream. Satisfied customers who are happy with their current relationship typically won't be interested in switching to a new brand. So late entrants usually have a tough battle.

A new product, like equipment for video conferencing over the Internet, is likely to get to the market growth stage of the product life cycle more quickly if customers see it as being easy to use.

Persuasive promotion becomes more important during the market maturity stage. Products may differ only slightly if at all. Most competitors have discovered the most effective appeals or quickly copied the leaders. Although each firm may still have its own demand curve, the curves become increasingly elastic as the various products become almost the same in the minds of potential consumers. By then, price sensitivity is a real factor.

In the United States, the markets for most cars, boats, television sets, and many household appliances are in market maturity. This stage may continue for many years—until a basically new product idea comes along—even though individual brands or models come and go. For example, high-definition digital TV (HDTV) is coming on now, and over time it will make obsolete not only the old-style TVs but also the broadcast systems on which they rely.[3]

Sales decline—a time of replacement

During the **sales decline** stage, new products replace the old. Price competition from dying products becomes more vigorous—but firms with strong brands may make profits until the end. These firms have down-sloping demand curves because they successfully differentiated their products.

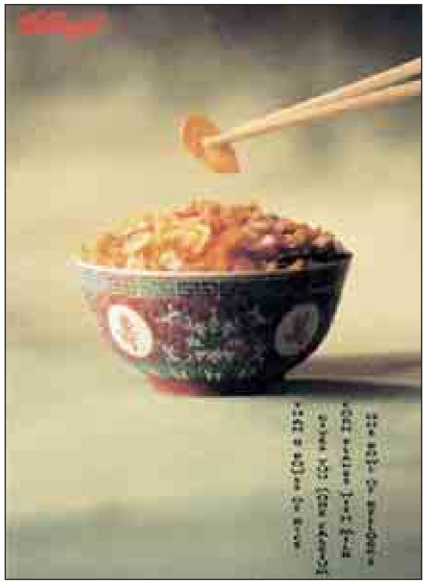
As the new products go through their introduction stage, the old ones may keep some sales by appealing to the most loyal customers or those who are slow to try new ideas. These conservative buyers might switch later—smoothing the sales decline.

Product Life Cycles Should Be Related to Specific Markets

Remember that product life cycles describe industry sales and profits for a *product idea* within a particular product-market. The sales and profits of an individual product or brand may not, and often do not, follow the life-cycle pattern. They may vary up and down throughout the life cycle—sometimes moving in the opposite direction of industry sales and profits. Further, a product idea may be in a different life-cycle stage in different markets.

Individual brands may not follow the pattern

A given firm may introduce or withdraw a specific product during any stage of the product life cycle. A “me-too” brand introduced during the market growth stage,



Marketing managers for Kellogg and Nabisco have found many opportunities for new growth in international markets.

for example, may never get any sales at all and suffer a quick death. Or it may reach its peak and start to decline even before the market maturity stage begins. Market leaders may enjoy high profits during the market maturity stage—even though industry profits are declining. Weaker products, on the other hand, may not earn a profit during any stage of the product life cycle. Sometimes the innovator brand loses so much in the introduction stage that it has to drop out just as others are reaping big profits in the growth stage.

Strategy planners who naively expect sales of an individual product to follow the general product life-cycle pattern are likely to be rudely surprised. In fact, it might be more sensible to think in terms of "product-market life cycles" rather than product life cycles—but we will use the term *product life cycle* because it is commonly accepted and widely used.

Each market should be carefully defined

How we see product life cycles depends on how broadly we define a product-market. For example, about 80 percent of all U.S. households own microwave ovens. Although microwave ovens appear to be at the market maturity stage here, in many other countries they're still early in the growth stage. Even in European countries like Switzerland, Denmark, Italy, and Spain, fewer than 20 percent of all households own microwave ovens.[4] As this example suggests, a firm with a mature product can sometimes turn back the clock by focusing on new growth opportunities in international markets.

How broadly we define the needs of customers in a product-market also affects how we view product life cycles—and who the competitors are. For example, consider the set of consumer needs related to storing and preparing foods. Wax paper sales in the United States started to decline when Dow introduced Saran Wrap. Then sales of Saran Wrap (and other similar products) fell sharply when small plastic storage bags became popular. However, sales picked up again by the end of the decade. The product didn't change, but customers' needs did. Saran Wrap filled a new need—a wrap that would work well in microwave cooking. In the last few years, resealable bags like those from Ziploc have taken over because they can be used in both the freezer and the microwave.

If a market is defined broadly, there may be many competitors—and the market may appear to be in market maturity. On the other hand, if we focus on a narrow

New products that do a better job of meeting the needs of specific target customers are more likely to move quickly and successfully through the introductory stage of the product life cycle.

submarket—and a particular way of satisfying specific needs—then we may see much shorter product life cycles as improved product ideas come along to replace the old.

Product Life Cycles Vary in Length

How long a whole product life cycle takes—and the length of each stage—vary a lot across products. The cycle may vary from 90 days—in the case of toys like the Ghostbusters line—to possibly 100 years for gas-powered cars.

The product life cycle concept does not tell a manager precisely *how long* the cycle will last. But a manager can often make a good guess based on the life cycle for similar products. Sometimes marketing research can help too. However, it is more important to expect and plan for the different stages than to know the precise length of each cycle.

Some products move fast

A new product idea will move through the early stages of the life cycle more quickly when it has certain characteristics. For example, the greater the *comparative advantage* of a new product over those already on the market, the more rapidly its sales will grow. Sales growth is also faster when the product is *easy to use* and if its advantages are *easy to communicate*. If the product *can be tried* on a limited basis—without a lot of risk to the customer—it can usually be introduced more quickly. Finally, if the product is *compatible* with the values and experiences of target customers, they are likely to buy it more quickly.

The fast adoption of the Netscape Navigator browser for the Internet's World Wide Web is a good example. Netscape offered real benefits. The Internet had been around for a while, but it was used by very few people because it was hard to access. Compared to existing ways for computers to communicate on the Internet, Navigator was easy to use and it worked as well with pictures as data. It also offered a simple way to customize to the user's preferences. Free online downloads of the software made it easy for consumers to try the product. And Navigator worked like other Windows software that users already knew, so it was easy to install and learn—and it was compatible with their computers and how they were working. Most of the initial growth, however, was in the U.S. In less-developed countries where personal computers were less common and where there were fewer computer networks, Navigator did not initially have the same comparative advantages.[5]

Internet

Internet Exercise A number of software, hardware, and programming firms are working on products that deliver Internet information via TV. Explore the WebTV website (www.webtv.com) to find out about one aspect of this idea. How does WebTV stack up when you consider the characteristics of an innovation reviewed earlier?

Product life cycles are getting shorter

Although the life of different products varies, in general product life cycles are getting shorter. This is partly due to rapidly changing technology. One new invention may make possible many new products that replace old ones. Tiny electronic microchips led to hundreds of new products—from Texas Instruments calculators and Pulsar digital watches in the early days to microchip-controlled heart valves, color fax machines, and wireless Internet devices such as the Palm now.

Some markets move quickly to market maturity—if there are fast copiers. In the highly competitive grocery products industry, cycles are down to 12 to 18 months for really new ideas. Simple variations of a new idea may have even shorter life cycles. Competitors sometimes copy flavor or packaging changes in a matter of weeks or months.

Patents for a new product may not be much protection in slowing down competitors. Competitors can often find ways to copy the product idea without violating a specific patent. Worse, some firms find out that an unethical competitor simply disregarded the patent protection. Patent violations by foreign competitors are very common. A product's life may be over before a case can get through patent-court bottlenecks. By then, the copycat competitor may even be out of business. These problems are even more severe in international cases because different governments, rules, and court systems are involved. The patent system, in the United States and internationally, needs significant improvement if it is to really protect firms that develop innovative ideas.[6]

Although life cycles are moving faster in the advanced economies, keep in mind that many advances bypass most consumers in less-developed economies. These consumers struggle at the subsistence level, without an effective macro-marketing system to stimulate innovation. However, some of the innovations and economies of scale made possible in the advanced societies do trickle down to benefit these consumers. Inexpensive antibiotics and drought-resistant plants, for example, are making a life-or-death difference.

The early bird usually makes the profits

The increasing speed of the product life cycle means that firms must be developing new products all the time. Further, they must try to have marketing mixes that will make the most of the market growth stage—when profits are highest.

During the growth stage, competitors are likely to rapidly introduce product improvements. Fast changes in marketing strategy may be required here because profits don't necessarily go to the innovator. Sometimes fast copiers of the basic idea will share in the market growth stage. Sony, a pioneer in developing videocassette recorders, was one of the first firms to put VCRs on the market. Other firms quickly followed—and the competition drove down prices and increased demand. As sales of VCRs continued to grow, Sony doggedly stuck to its Beta format VCRs in spite of the fact that most consumers were buying VHS-format machines offered by competitors. Not until a decade later did Sony finally "surrender" and offer a VHS-format machine. However, by then the booming growth in VCR sales had ebbed, and competitors controlled 90 percent of the market. Although Sony was slow to see its mistake, its lost opportunities were minor compared to American producers who sat on the sidelines and watched as foreign producers captured the whole VCR market. Copiers can be even faster than the innovator in adapting to the market's needs. Marketers must be flexible, *but also* they must fully understand the needs and attitudes of their target markets.[7]

A certain color or style may be in fashion one season and outdated the next.

The short happy life of fashions and fads

The sales of some products are influenced by **fashion**—the currently accepted or popular style. Fashion-related products tend to have short life cycles. What is currently popular can shift rapidly. A certain color or style of clothing—baggy jeans, miniskirts, or four-inch-wide ties—may be in fashion one season and outdated the next. Marketing managers who work with fashions often have to make really fast product changes.

How fast is fast enough? Zara, a women's fashion retailer based in Spain, takes only about two weeks to go from a new fashion concept to having items on the racks of its stores. Zara's market-watching designers get a constant flow of new fashion ideas from music videos, what celebrities are wearing, fashion shows and magazines—even trendy restaurants and bars. Zara quickly produces just enough of a design to test the waters and then sends it out for overnight delivery to some of its 449 stores around the world. Stores track consumer preferences every day through point-of-sale computers. Designers may not even wait for online summaries at the end of the day. They are in constant touch with store managers by phone to get an early take on what's selling and where. If an item is hot, more is produced and shipped. Otherwise it's dropped. Stores get deliveries several times a week. With this system items are rarely on the shelves of Zara stores for more than a week or two. As a result, there is almost no inventory—which helps Zara keep prices down relative to many of its fashion competitors.[8]

It's not really clear why a particular fashion becomes popular. Most present fashions are adaptations or revivals of previously popular styles. Designers are always looking for styles that will satisfy fashion innovators who crave distinctiveness. And lower-cost copies of the popular items may catch on with other groups and survive for a while. Yet the speed of change usually increases the cost of producing and marketing products. Companies sustain losses due to trial and error in finding acceptable styles, then producing them on a limited basis because of uncertainty about the length of the cycle. These increased costs are not always charged directly to the consumer since some firms lose their investment and go out of business. But in total, fashion changes cost consumers money. Fashion changes are a luxury that most people in less-developed countries simply can't afford.

A **fad** is an idea that is fashionable only to certain groups who are enthusiastic about it. But these groups are so fickle that a fad is even more short lived than a regular fashion. Many toys—whether it's a Hasbro Planet of the Apes plastic figure or a Toymax Paintball pack—are fads but do well during a short-lived cycle. Some teenagers' music tastes are fads.[9]

Planning for Different Stages of the Product Life Cycle

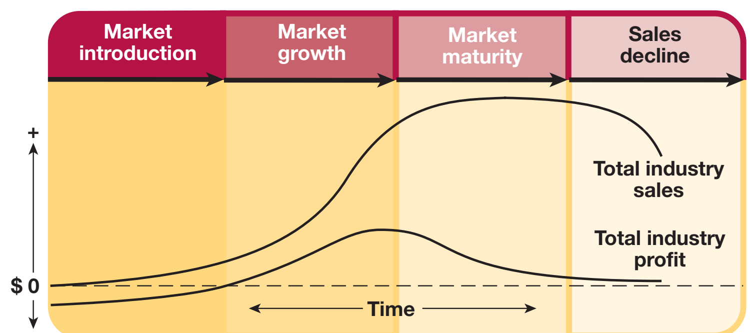
Length of cycle afects strategy planning

Where a product is in its life cycle—and how fast it's moving to the next stage—should affect marketing strategy planning. Marketing managers must make realistic plans for the later stages. Exhibit 10-2 shows the relationship of the product life cycle to the marketing mix variables. The technical terms in this figure are discussed later in the book.

Introducing new products

Exhibit 10-2 shows that a marketing manager has to do a lot of work to introduce a really new product—and this should be reflected in the strategy planning. Money must be spent designing and developing the new product. Even if the product is unique, this doesn't mean that everyone will immediately come running to

Exhibit 10-2
Typical Changes in Marketing Variables over the Product Life Cycle



	Market introduction	Market growth	Market maturity	Sales decline
Competitive situation	Monopoly or monopolistic competition	Monopolistic competition or oligopoly	Monopolistic competition or oligopoly heading toward pure competition →	→
Product	One or few	Variety—try to find best product Build brand familiarity	All "same" Battle of brands	Some drop out
Place	Build channels Maybe selective distribution →		Move toward more intensive distribution →	
Promotion	Build primary demand Pioneering-informing	Build selective demand → Informing/Persuading → Persuading/Reminding (frantically competitive)		
Price	Skimming or penetration	Meet competition (especially in oligopoly) → or Price dealing and price cutting →		

the producer's door. The firm will have to build channels of distribution—perhaps offering special incentives to win cooperation. Promotion is needed to build demand *for the whole idea* not just to sell a specific brand. Because all this is expensive, it may lead the marketing manager to try to "skim" the market—charging a relatively high price to help pay for the introductory costs.

The correct strategy, however, depends on how fast the product life cycle is likely to move—that is, how quickly the new idea will be accepted by customers—and how quickly competitors will follow with their own versions of the product. When the early stages of the cycle will be fast, a low initial (penetration) price may make sense to help develop loyal customers early and keep competitors out.

Pioneer may need help from competitors

Sometimes it's not in the best interest of the market pioneer for competitors to stay out of the market. This may seem odd. But building customer interest in a really new product idea—and obtaining distribution to make the product available—can be too big a job for a single company, especially a small one with limited resources. Two or more companies investing in promotion to build demand may help to stimulate the growth of the whole product-market. Similarly, a new product that is unique may languish if it is not compatible with other products that customers rely on. This is what recently happened with Digital Video Express (Divx) video disks. When Divx came out, many consumer-electronics makers, retailers, and film studios were struggling to launch DVD format products. Divx had a number of advantages over DVD, but it was not compatible with many of the ordinary DVD players that were already on the market. Video rental stores didn't want to stock movies for both DVD and Divx, and consumers didn't want to get stuck with Divx players if movies were not available. So as DVD started to sizzle Divx fizzled.[10]

New product sales may not take off

Not all new product ideas catch on. Customers may conclude that the marketing mix doesn't satisfy their needs, or other new products may meet the same need better. But the success that eludes a firm with its initial strategy can sometimes be achieved by modifying the strategy. Videodisc players illustrate this point. They were a flop during their initial introduction in the home-entertainment market. Consumers didn't see any advantage over cheaper videotape players. But then new opportunities developed. For example, the business market for these systems grew because firms used them for sales presentations and for in-store selling. Customers could shop for products by viewing pictures at a video kiosk. Of course, change marches on. CD-ROM took over much of this market when computer manufacturers added a CD drive as a standard feature. And now DVD has the advantage because it can handle even more video on one disk.[11]

Also relevant is how quickly the firm can change its strategy as the life cycle moves on. Some firms are very flexible. They can compete effectively with larger, less adaptable competitors by adjusting their strategies more frequently.

Managing maturing products

It's important for a firm to have some competitive advantage as it moves into market maturity. Even a small advantage can make a big difference—and some firms do very well by carefully managing their maturing products. They are able to capitalize on a slightly better product or perhaps lower production and/or marketing costs. Or they are simply more successful at promotion—allowing them to differentiate their more or less homogeneous product from competitors. For example, graham crackers were competing in a mature market and sales were flat. Nabisco used the same ingredients to create bite-sized Teddy Grahams and then promoted them heavily. These changes captured new sales and profits for Nabisco. However, competing firms quickly copied this idea with their own brands.[12]

The important point here is that industry profits are declining in market maturity. Top management must see this, or it will continue to expect the attractive

Some companies continue to do well in market maturity by improving their products. Lipton has developed a cold brew tea and Nintendo's Game Boy remains popular with new color features.

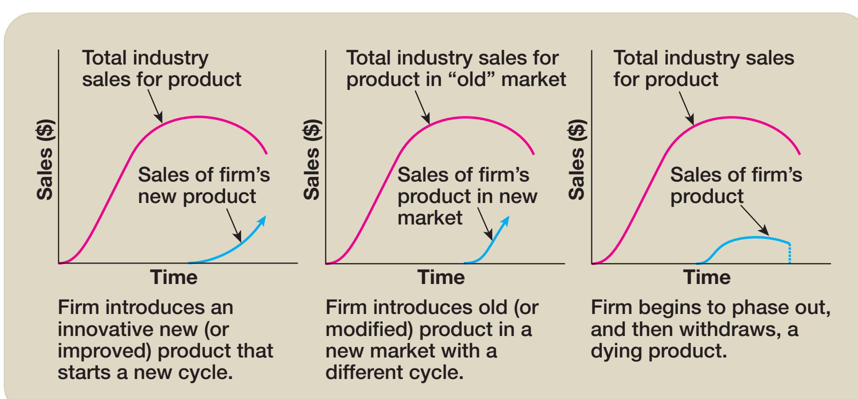
profits of the market growth stage—profits that are no longer possible. If top managers don't understand the situation, they may place impossible burdens on the marketing department—causing marketing managers to think about collusion with competitors, deceptive advertising, or some other desperate attempt to reach impossible objectives.

Product life cycles keep moving. But that doesn't mean a firm should just sit by as its sales decline. There are other choices. A firm can improve its product or develop an innovative new product for the same market. Or it can develop a strategy for its product (perhaps with modifications) targeted at a new market. For example, it might find a market in a country where the life cycle is not so far along, or it might try to serve a new need. Or the firm can withdraw the product before it completes the cycle and refocus on better opportunities. See Exhibit 10-3.

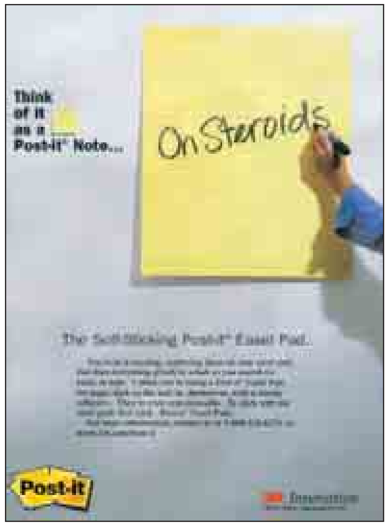
Improve the product or develop a new one

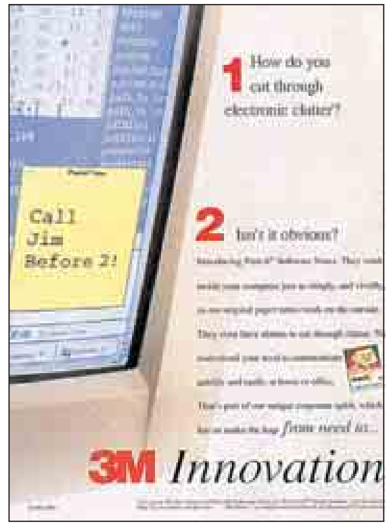
When a firm's product has won loyal customers, it can be successful for a long time—even in a mature or declining market. However, continued improvements may be needed to keep customers satisfied, especially if their needs shift. An outstanding example is Procter & Gamble's Tide. Introduced in 1947, this powdered detergent gave consumers a much cleaner wash than they were able to get before because it did away with soap film. Tide led to a whole new generation of powdered laundry products that cleaned better with fewer suds. The demands on Tide continue to change because of new washing machines and fabrics—so the powdered Tide sold today is much different than the one sold in 1947. In fact, powdered Tide has had at least 55 (sometimes subtle) modifications.

Exhibit 10-3
Examples of Three Marketing Strategy Choices for a Firm in a Mature Product-Market



A new product idea gives birth to lots of new products, so the idea is important.





Do product modifications—like those made with powdered Tide—create a wholly new product that should have its own product life cycle? Or are they technical adjustments of the original product idea? We will take the latter position—focusing on the product idea rather than changes in features. This means that some of these Tide changes were made in the market maturity stage. But this type of product improvement can help to extend the product life cycle.

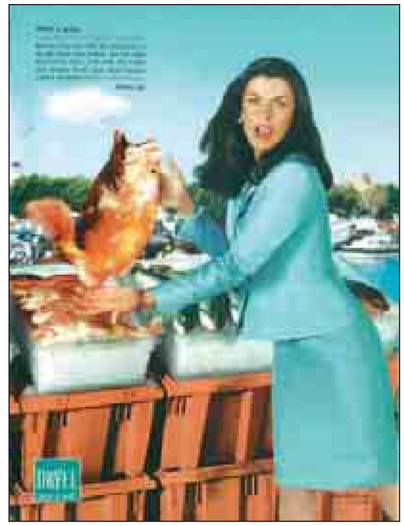
On the other hand, a firm that develops an innovative new product may move to a new product life cycle. For example, by 1985 new liquid detergents like Wisk were moving into the growth stage, and sales of powdered detergents were declining. To share in the growth-stage profits for liquid detergents and to offset the loss of customers from powdered Tide, Procter & Gamble introduced Liquid Tide. Then, in 1997, P&G introduced Tide HE High Efficiency Laundry Detergent. It was the first detergent designed specifically to work with a new type of washing machine that is just now starting to appear in stores. These environmentally friendly front loaders use up to 40 percent less water per wash and over 50 percent less electricity than regular washers. Regular detergents don't work in these washers because they do too much sudsing, but Tide HE is designed to be a low-suds solution. Although P&G used the familiar Tide brand name on both Liquid Tide and Tide HE, they appear to be different product concepts that compete in different product-markets. Traditional liquid detergent is probably now entering the market maturity stage, and Tide HE is probably just starting the growth stage.

Even though regular powdered detergents in general appear to be in the decline stage, traditional powdered Tide continues to sell well because it still does the job for some consumers. But sales growth is likely to come from liquid detergents and the new low-suds detergents.[13]

Develop new strategies for different markets

We already highlighted the fact that the same product may be in different life cycle stages in different markets. That means that a firm may have to pursue very different strategies for a product, at the same time, in different markets.

In a mature market, a firm may be fighting to keep or increase its market share. But if the firm finds a new use for the product, it may need to try to stimulate overall demand. Du Pont's Teflon fluorocarbon resin is a good example. It was developed more than 50 years ago and has enjoyed sales growth as a nonstick coating for cookware, as an insulation for aircraft wiring, and as a lining for chemically resistant equipment. But marketing managers for Teflon are not waiting to be stuck with declining profits in



Tide detergent has been improved many times over the years, and now has a new WearCare formula that helps protect cotton threads from damage. By contrast, Dryel is a completely new type of product and being able to dry clean delicate clothes at home is a new idea.

those mature markets. They are constantly developing strategies for new markets where Teflon will meet needs. For example, Teflon is now selling well as a special coating for the wires used in high-speed communications between computers.[14]

Phasing out dying products

Not all strategies have to be exciting growth strategies. If prospects are poor in some product-market, a phase-out strategy may be needed. The need for phasing out becomes more obvious as the sales decline stage arrives. But even in market maturity, it may be clear that a particular product is not going to be profitable enough to reach the company's objectives using the current strategy. Then the wisest move may be to develop a strategy that helps the firm phase out of the product-market—perhaps over several years.

Marketing plans are implemented as ongoing strategies. Salespeople make calls, inventory moves in the channel, advertising is scheduled for several months into the future, and so on. So the firm usually experiences losses if managers end a plan too abruptly. Because of this, it's sometimes better to phase out the product gradually. Managers order materials more selectively so production can end with a minimum of unused inventory and they shift salespeople to other jobs. They may cancel advertising and other promotion efforts more quickly since there's no point in promoting for the long run. These various actions obviously affect morale within the company—and they may cause middlemen to pull back too. So the company may have to offer price inducements in the channels. Employees should be told that a phase-out strategy is being implemented—and hopefully they can be shifted to other jobs as the plan is completed.

Obviously, there are some difficult implementation problems here. But phase-out is also a *strategy*—and it must be market-oriented to cut losses. In fact, it is possible to milk a dying product for some time if competitors move out more quickly. This situation occurs when there is still ongoing (though declining) demand and some customers are willing to pay attractive prices to get their old favorite.

New-Product Planning

Competition is strong and dynamic in most markets. So it is essential for a firm to keep developing new products, as well as modifying its current products, to meet changing customer needs and competitors' actions. Not having an active new-product development process means that consciously, or subconsciously, the firm has decided to milk its current products and go out of business. New-product planning is not an optional matter. It has to be done just to survive in today's dynamic markets.

What is a new product?

In discussing the introductory stage of product life cycles, we focused on the type of really new product innovations that tend to disrupt old ways of doing things. However, each year firms introduce many products that are basically refinements of existing products. So a **new product** is one that is new *in any way* for the company concerned.

A product can become "new" in many ways. A fresh idea can be turned into a new product and start a new product life cycle. For example, Alza Corporation's time-release skin patches are replacing pills and injections for some medications.

Variations on an existing product idea can also make a product new. Oral B changed its conventional toothbrush to include a strip of colored bristles that fade as you brush; that way you know when it's time for a new brush. Colgate redesigned the toothbrush with a soft handle and angled bristles to do a better job removing tartar. Even small changes in an existing product can make it new.[15]

FTC says product is "new" only six months

A firm can call its product new for only a limited time. Six months is the limit according to the **Federal Trade Commission (FTC)**—the federal government agency that polices antimonopoly laws. To be called new, says the FTC, a product must be entirely new or changed in a "functionally significant or substantial respect." While six months may seem a very short time for production-oriented managers, it may be reasonable, given the fast pace of change for many products.

Ethical issues in new-product planning

New product decisions—and decisions to abandon old products—often involve ethical considerations. For example, some firms (including firms that develop drugs to treat AIDS) have been criticized for holding back important new product innovations until patents run out, or sales slow down, on their existing products.

At the same time, others have been criticized for "planned obsolescence"—releasing new products that the company plans to soon replace with improved new versions. Similarly, wholesalers and middlemen complain that producers too often keep their new-product introduction plans a secret and leave middlemen with dated inventory that they can sell only at a loss.

Companies also face ethical dilemmas when they decide to stop supplying a product or the service and replacement parts to keep it useful. An old model of a Cuisinart food processor, for example, might be in perfect shape except for a crack in the plastic mixing bowl. It's sensible for the company to improve the design if the crack is a frequent problem, but if consumers can't get a replacement part for the model they already own, they're left holding the bag.

Criticisms are also leveled at firms that constantly release minor variations of products that already saturate markets. Consider what happened with disposable diapers. Marketing managers thought that they were serving some customers' needs better when they offered diapers in boys' and girls' versions and in a variety of sizes, shapes, and colors. But many retailers felt that the new products were simply a ploy to get more shelf space. Further, some consumers complained that the bewildering array of choices made it impossible to make an informed decision. Of course, some people would level the same criticism at Huggies Little Swimmers Disposable Swimpants. But unlike other disposables, this new product doesn't swell in the water. They have been a success because they seem to fill a different need.

So, different marketing managers might have very different reactions to such criticisms. However, the fact remains that product management decisions often have a significant effect, one way or another, on customers and middlemen. A marketing manager who is not sensitive to this may find that a too casual decision leads to a negative backlash that affects the firm's strategy or reputation.[16]

An Organized New-Product Development Process Is Critical

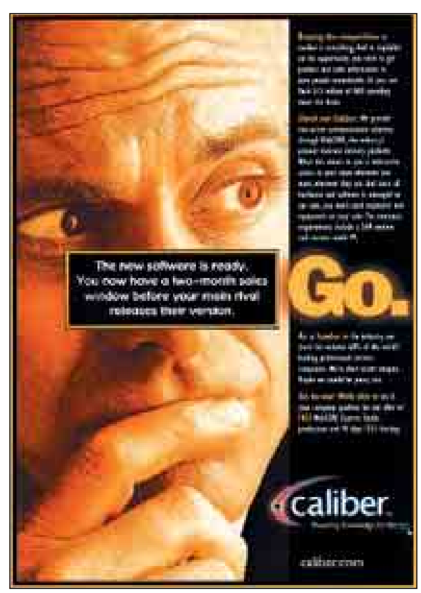
Identifying and developing new-product ideas—and effective strategies to go with them—is often the key to a firm's success and survival. But this isn't easy. New-product development demands effort, time, and talent—and still the risks and costs of failure are high. Experts estimate that consumer packaged-goods companies spend at least $20 million to introduce a new brand—and 70 to 80 percent of these new brands flop. Each year there are over 31,000 new consumer packaged goods in the U.S. alone. So, about 25,000 failed. That's a big expense—and a waste. In the service sector, the front-end cost of a failed effort may not be as high, but it can have a devastating long-term effect if dissatisfied consumers turn elsewhere for help.[17]

Internet

Internet Exercise Marketing Intelligence Service, Ltd., is a U.S.-based firm that tracks new consumer packaged goods—both successes and failures. Enter its website (www.productscan.com) and click on the *What's New* button, then review its selections for new product innovations of the year. Do you think that these products offer customers superior value, or are they just me-too imitations?

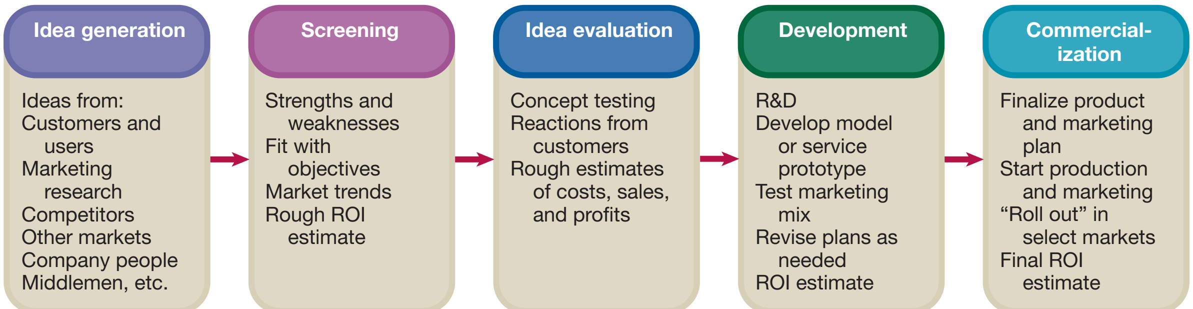
A new product may fail for many reasons. Most often, companies fail to offer a unique benefit or underestimate the competition. Sometimes the idea is good but the company has design problems—or the product costs much more to produce than was expected. Some companies rush to get a product on the market without developing a complete marketing plan.[18]

But moving too slowly can be a problem too. With the fast pace of change for many products, speedy entry into the market can be a key to competitive advantage. Marketing managers at Xerox learned this the hard way. Japanese competitors were taking market share with innovative new models of copiers. It turned out that the competitors were developing new models twice as fast as Xerox and at half the



Generating innovative and profitable new products requires an understanding of customer needs—and an organized new-product development process.

Exhibit 10-4 New-Product Development Process



cost. For Xerox to compete, it had to slash its five-year product development cycle. Many other companies—ranging from manufacturers like Chrysler Corporation and Hewlett-Packard to Internet service firms like E*Trade and Yahoo—are working to speed up the new-product development process.[19]

To move quickly and also avoid expensive new-product failures, many companies follow an organized new-product development process. The following pages describe such a process, which moves logically through five steps: (1) idea generation, (2) screening, (3) idea evaluation, (4) development (of product and marketing mix), and (5) commercialization.[20] See Exhibit 10-4.

The general process is similar for both consumer and business markets—and for both goods and services. There are some significant differences, but we will emphasize the similarities in the following discussion.

Process tries to kill new ideas—economically

An important element in this new-product development process is continued evaluation of a new idea's likely profitability and return on investment. In fact, the hypothesis-testing approach discussed in Chapter 8 works well for new-product development. The hypothesis tested is that the new idea will *not* be profitable. This puts the burden on the new idea—to prove itself or be rejected. Such a process may seem harsh, but experience shows that most new ideas have some flaw that can lead to problems and even substantial losses. Marketers try to discover those flaws early, and either find a remedy or reject the idea completely. Applying this process requires much analysis of the idea, both within and outside the firm, *before* the company spends money to develop and market a product. This is a major departure from the usual production-oriented approach—in which a company develops a product first and then asks sales to "get rid of it."

Of course, the actual new-product success rate varies among industries and companies. But many companies *are* improving the way they develop new products. It's important to see that if a firm doesn't use an organized process like this, it may bring many bad or weak ideas to market—at a big loss.

Step 1: Idea generation

New ideas can come from a company's own sales or production staff, middlemen, competitors, consumer surveys, or other sources such as trade associations, advertising agencies, or government agencies. By analyzing new and different views of the company's markets and studying present consumer behavior, a marketing manager can spot opportunities that have not yet occurred to competitors or even to potential customers. For example, ideas for new service concepts may come directly from analysis of consumer complaints.

No one firm can always be first with the best new ideas. So in their search for ideas, companies should pay attention to what current or potential competitors are doing. Microsoft, for example, had to play catchup with its Internet Explorer browser—and other changes to Windows—when Netscape Navigator became an instant hit. Some firms use what's called reverse engineering. For example, new-product specialists at Ford Motor Company buy other firms' cars as soon as they're available. Then they take the cars apart to look for new ideas or improvements. British Airways talks to travel agents to learn about new services offered by competitors. Many other companies use similar approaches.[21]

Many firms now "shop" in international markets for new ideas. Jamaica Broilers, a poultry producer in the Caribbean, moved into fish farming; it learned that many of the techniques it was using to breed chickens were also successful on fish farms in Israel. In the same vein, food companies in the United States and Europe are experimenting with an innovation recently introduced in Japan—a clear, odorless, natural film for wrapping food. Consumers don't have to unwrap it; when they put the product in boiling water or a microwave, the wrapper vanishes.[22]

Research shows that many new ideas in business markets come from customers who identify a need they have. Then they approach a supplier with the idea and perhaps even with a particular design or specification. These customers become the lead users of the product, but the supplier can pursue the opportunity in other markets.[23]

But finding new product ideas can't be left to chance. Companies need a formal procedure for seeking new ideas. The checkpoints discussed below, as well as the hierarchy of needs and other behavioral elements discussed earlier, should be reviewed regularly to ensure a continual flow of new, and sound, ideas. And companies do need a continual flow so they can spot an opportunity early—while there's still time to do something about it. Although later steps eliminate many ideas, a company must have some that succeed.

Step 2: Screening

Screening involves evaluating the new ideas with the type of S.W.O.T analysis described in Chapter 3 and the product-market screening criteria described in Chapter 4. Recall that these criteria include the combined output of a resource (strengths and weaknesses) analysis, a long-run trends analysis, and a thorough understanding of the company's objectives. See Exhibit 3-1 and Exhibit 4-5. Further, a "good" new idea should eventually lead to a product (and marketing mix) that will give the firm a competitive advantage—hopefully, a lasting one.

Opportunities with better growth potential are likely to be more attractive. We discussed this idea earlier when we introduced the GE planning grid (see Exhibit 4-7). Now, however, you know that the life-cycle stage at which a firm's new product enters the market has a direct bearing on its prospects for growth. Clearly, screening should consider how the strategy for a new product will hold up over the whole product life cycle. In other words, screening should consider how attractive the new product will be both in the short- and long-term.

Some companies screen based on consumer welfare

Screening should also consider how a new product will affect consumers over time. Ideally, the product should increase consumer welfare, not just satisfy a whim. Exhibit 10-5 shows different kinds of new-product opportunities. Obviously, a socially responsible firm tries to find desirable opportunities rather than deficient ones. This may not be as easy as it sounds, however. Some consumers want pleasing products

Exhibit 10-5
Types of New-Product Opportunities

Long-run consumer welfare	Immediate satisfaction: High	Immediate satisfaction: Low
High	Desirable products	Salutary products
Low	Pleasing products	Deficient products

Products that can be regenerated or remanufactured provide both immediate satisfaction and long-run consumer welfare.

instead of desirable ones. They emphasize immediate satisfaction and give little thought to their own long-term welfare. And some competitors willingly offer what consumers want in the short run. Generating socially responsible new-product ideas is a challenge for new-product planners, but consumer groups are helping firms to become more aware.

Safety must be considered

Real acceptance of the marketing concept certainly leads to safe products. But consumers still buy some risky products for the thrills and excitement they provide—for example, bicycles, skis, hang gliders, and bungee jumps. Even so, companies can usually add safety features—and some potential customers want them.

The U.S. **Consumer Product Safety Act** (of 1972) set up the Consumer Product Safety Commission to encourage safety in product design and better quality control. The commission has a great deal of power. It can set safety standards for products. It can order costly repairs or return of unsafe products. And it can back up its orders with fines and jail sentences. The Food and Drug Administration has similar powers for food and drugs.

Product safety complicates strategy planning because not all customers—even those who want better safety features—are willing to pay more for safer products. Some features cost a lot to add and increase prices considerably. These safety concerns must be considered at the screening step because a firm can later be held liable for unsafe products.

Products can turn to liabilities

Product liability means the legal obligation of sellers to pay damages to individuals who are injured by defective or unsafe products. Product liability is a serious matter. Liability settlements may exceed not only a company's insurance coverage but its total assets!

Relative to most other countries, U.S. courts enforce a very strict product liability standard. Producers may be held responsible for injuries related to their products no matter how the items are used or how well they're designed. Riddell—whose football helmets protect the pros—was hit with a $12 million judgment for a high school football player who broke his neck. The jury concluded that Riddell should have put a sticker on the helmet to warn players of the danger of butting into opponents!

Cases and settlements like this are common. In the United States, companies pay over $100 billion a year to lawyers and consumers. Some critics argue that the U.S. rules are so tough that they discourage innovation and economic growth. In contrast, Japan may be too slack. Japan's system discourages consumers from filing complaints because they are required to pay a percentage of any damages they seek as court costs—regardless of whether they win or lose.

Sometimes there is incentive for lawyers to push liability cases to take a share of the payments. Juries sometimes give huge settlements based on an emotional reaction to the case rather than scientific evidence. That seems to have happened in lawsuits over silicon breast implants. On the other hand, until recently tobacco companies' lawyers took just about any step they could to try to discredit scientific evidence of the cancer hazards of smoking.

Product liability is a serious ethical and legal matter. Many countries are attempting to change their laws so that they will be fair to both firms and consumers. But until product liability questions are resolved, marketing managers must be even more sensitive when screening new-product ideas.[24]

ROI is a crucial screening criterion

Getting by the initial screening criteria doesn't guarantee success for the new idea. But it does show that at least the new idea is in the right ballpark *for this firm*. If many ideas pass the screening criteria, a firm must set priorities to determine which ones go on to the next step in the process. This can be done by comparing the ROI (return on investment) for each idea—assuming the firm is ROI-oriented. The most attractive alternatives are pursued first.

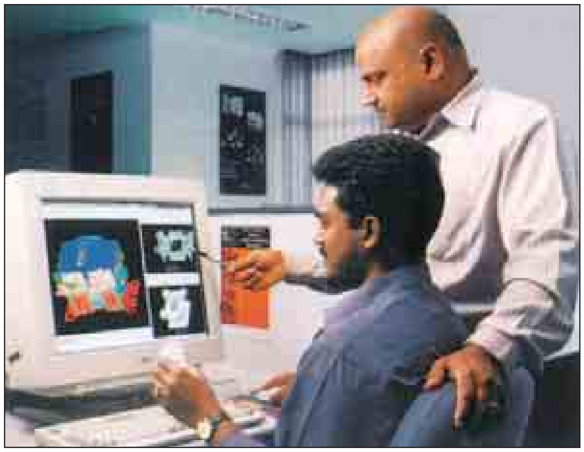
Step 3: Idea evaluation

When an idea moves past the screening step, it is evaluated more carefully. Note that an actual product has not yet been developed—and this can handicap the firm in getting feedback from customers. For help in idea evaluation, firms use **concept testing**—getting reactions from customers about how well a new product idea fits their needs. Concept testing uses market research—ranging from informal focus groups to formal surveys of potential customers.

Companies can often estimate likely costs, revenue, and profitability at this stage. And market research can help identify the size of potential markets. Even informal focus groups are useful—especially if they show that potential users are not excited about the new idea. If results are discouraging, it may be best to kill the idea at this stage. Remember, in this hypothesis-testing process, we're looking for any evidence that an idea is *not* a good opportunity for this firm and should be rejected.

Product planners must think about wholesaler and retailer customers as well as final consumers. Middlemen may have special concerns about handling a proposed product. A Utah ice-cream maker was considering a new line of ice-cream novelty products—and he had visions of a hot market in California. But he had to drop his idea when he learned that grocery store chains wanted payments of $20,000 each just to stock his frozen novelties in their freezers. Without the payment, they didn't want to risk using profitable freezer space on an unproven product. This is not an unusual case. At the idea evaluation stage, companies often find that other members of the distribution channel won't cooperate.[25]

Idea evaluation is often more precise in business markets. Potential customers are more informed—and their needs focus on the economic reasons for buying rather than emotional factors. Further, given the derived nature of demand in business markets, most needs are already being satisfied in some way. So new products just substitute for existing ones. This means that product planners can compare the cost advantages and limitations of a new product with those currently being used. And



GE developed a software system so that its new product design engineers in different parts of the world could collaborate over the Internet in real time—which helps GE bring concepts to market more quickly.

by interviewing well-informed people, they can determine the range of product requirements and decide whether there is an opportunity.

For example, you've probably noticed that most new car designs have switched to low-profile headlights. They allow sleeker styling and better gas mileage. Yet these lights were initially only used on high-priced cars. That's because the GE development team worked with engineers at Ford when they were first developing the bulbs for these headlights. Together they determined that the switch to the new bulb and headlight assembly would add about $200 to the price of a car. That meant that the bulb was initially limited to luxury cars—until economies of scale brought down the costs.[26]

Whatever research methods are used, the idea evaluation step should gather enough information to help decide whether there is an opportunity, whether it fits with the firm's resources, *and* whether there is a basis for developing a competitive advantage. With such information, the firm can estimate likely ROI in the various market segments and decide whether to continue the new-product development process.[27]

Step 4: Development

Product ideas that survive the screening and idea evaluation steps must now be analyzed further. Usually, this involves some research and development (R&D) and engineering to design and develop the physical part of the product. In the case of a new service offering, the firm will work out the details of what training, equipment, staff, and so on will be needed to deliver on the idea. Input from the earlier efforts helps guide this technical work.

New computer-aided design (CAD) systems are sparking a revolution in design work. Designers can develop lifelike 3-D color drawings of packages and products. Then the computer allows the manager to look at the product from different angles and views, just as with a real product. Changes can be made almost instantly. They can be sent by e-mail to managers all over the world for immediate review. They can even be put on a website for marketing research with remote customers. Then once the designs are finalized, they feed directly into computer-controlled manufacturing systems. Companies like Motorola and Timex have found that these systems cut their new-product development time in half—giving them a leg up on many competitors. Most firms are now using variations on these systems.

Even so, it is still good to test models and early versions of the product in the market. This process may have several cycles. A manufacturer may build a model of a physical product or produce limited quantities; a service firm may try to train a small group of service providers. Product tests with customers may lead to revisions—*before* the firm commits to full-scale efforts to produce the good or service.

With actual goods or services, potential customers can react to how well the product meets their needs. Using small focus groups, panels, and larger surveys, marketers can get reactions to specific features and to the whole product idea. Sometimes that reaction kills the idea. For example, Coca-Cola Foods believed it had a great idea with Minute Maid Squeeze-Fresh, frozen orange juice concentrate in a squeeze bottle. Coca-Cola thought consumers would prefer to mix one glass at a time rather than find space for another half-gallon jug in the refrigerator. When actually tested, however, Squeeze-Fresh bombed. Consumers loved the idea but hated the product. It was messy to use, and no one could tell how much concentrate to squeeze in the glass.[28]

In other cases, testing can lead to revision of product specifications for different markets. For example, AMR Corporation had plans for a new reservation system to help travel agents, hotels, and airlines provide better customer service. But tests revealed too many problems, and plans for the service had to be revised. Sometimes a complex series of revisions may be required. Months or even years of research may be necessary to focus on precisely what different market segments will find acceptable. For example, Gillette's Mach3 razor blade took over a decade and $750 million in development and tooling costs, plus another $300 million for introductory promotion.[29]

Firms often use full-scale market testing to get reactions in real market conditions or to test product variations and variations in the marketing mix. For example, a firm may test alternative brands, prices, or advertising copy in different test cities. Note that the firm is testing the whole marketing mix, not just the product. For example, a hotel chain might test a new service offering at one location to see how it goes over.

Test-marketing can be risky because it may give information to competitors. In fact, a company in Chicago—Marketing Intelligence Services—monitors products in test markets and then sells the information to competing firms. Similar firms monitor markets in other countries.

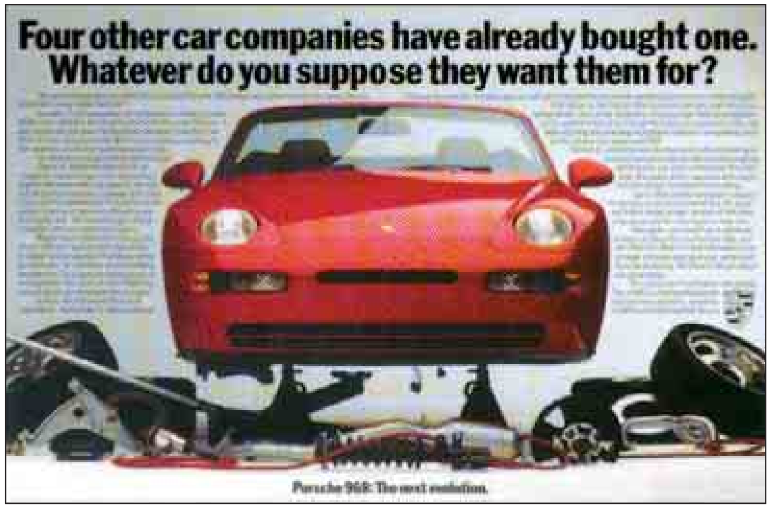
But *not* testing is dangerous too. Frito-Lay was so sure it understood consumers' snack preferences that it introduced a three-item cracker line without market testing. Even with network TV ad support, MaxSnax met with overwhelming consumer indifference. By the time Frito-Lay pulled the product from store shelves, it had lost $52 million. Market tests can be very expensive. Yet they can uncover problems that otherwise might go undetected and destroy the whole strategy.[30]

If a company follows the new-product development process carefully, the market test will provide a lot more information to the firm than to its competitors. Of course, the company must test specific variables rather than just vaguely testing whether a new idea will "sell." After the market test, the firm can estimate likely ROI for various strategies to determine whether the idea moves on to commercialization.

Some companies don't do market tests because they just aren't practical. In fashion markets, for example, speed is extremely important, and products are usually just tried in market. And durable products—which have high fixed production costs and long production lead times—may have to go directly to market. In these cases, it is especially important that the early steps be done carefully to reduce the chances for failure.[31]

Step 5: Commercialization

A product idea that survives this far can finally be placed on the market. First, the new-product people decide exactly which product form or line to sell. Then they complete the marketing mix—really a whole strategic plan. And top management has to approve an ROI estimate for the plan before it is implemented. Finally, the product idea emerges from the new-product development process—but success requires the cooperation of the whole company.



Firms often take apart competitors' products to look for ideas that they can apply or adapt in their own products.

Putting a product on the market is expensive. Manufacturing or service facilities have to be set up. Goods have to be produced to fill the channels of distribution, or people must be hired and trained to provide services. Further, introductory promotion is costly—especially if the company is entering a very competitive market.

Because of the size of the job, some firms introduce their products city by city or region by region—in a gradual "rollout"—until they have complete market coverage. Sprint used this approach in introducing its broadband wireless service that included a rooftop transmission device. Detroit, Phoenix, and San Francisco were targeted first. Rollouts also permit more market testing—although that is not their purpose. Rather, the purpose is to do a good job implementing the marketing plan. But marketing managers also need to pay close attention to control—to ensure that the implementation effort is working and that the strategy is on target.

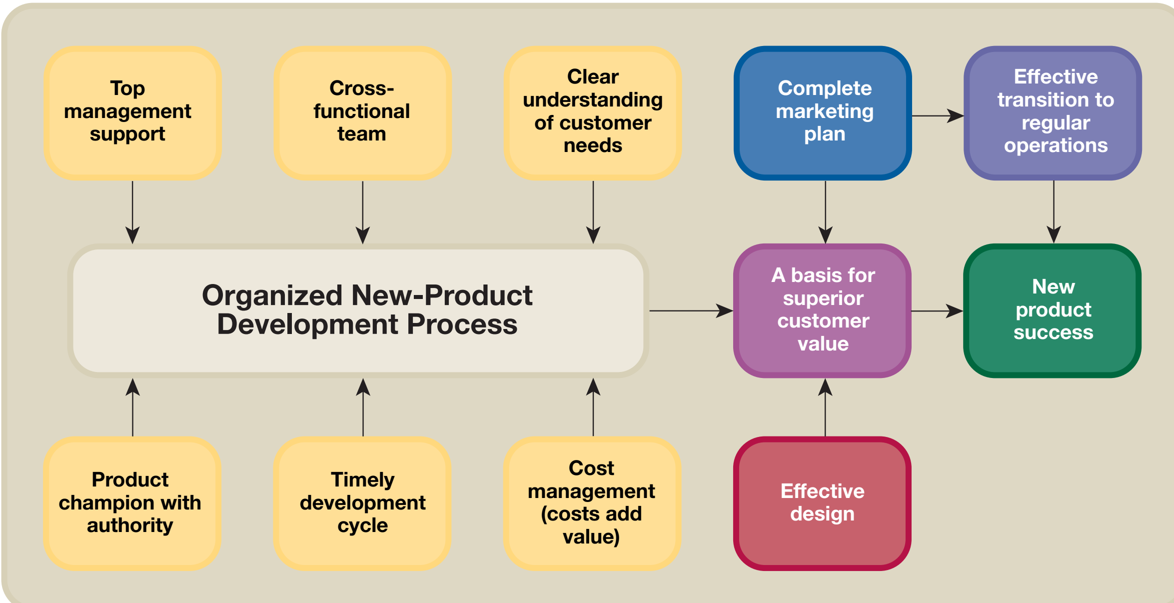
New-Product Development: A Total Company Effort

We've been discussing the steps in a logical, new-product development process. However, as shown in Exhibit 10-6, many factors can impact the success of the effort.

Top-level support is vital

Companies that are particularly successful at developing new goods and services seem to have one trait in common: enthusiastic top-management support for new-product development. New products tend to upset old routines that managers of established products often try in subtle but effective ways to maintain. So someone with top-level support, and authority to get things done, needs to be responsible for new-product development.[32]

Exhibit 10-6 New-Product Development Success Factors



Put someone in charge

In addition, rather than leaving new-product development to someone in engineering, R&D, or sales who happens to be interested in taking the initiative, successful companies put someone in charge. It may be a person, department, or team. But it's not a casual thing. It's a major responsibility of the job.

A new-product development department or team (committee) from different departments may help ensure that new ideas are carefully evaluated and profitable ones quickly brought to market. It's important to choose the right people for the job. Overly conservative managers may kill too many, or even all, new ideas. Or committees may create bureaucratic delays leading to late introduction and giving competitors a head start. A delay of even a few months can make the difference between a product's success or failure.

Market needs guide R&D effort

Many new-product ideas come from scientific discoveries and new technologies. That is why firms often assign specialists to study the technological environment in search of new ways to meet customers' needs. Many firms have their own R&D group that works on developing new products and new-product ideas. Even service firms have technical specialists who help in development work. For example, a bank thinking about offering customers a new set of investment alternatives must be certain that it can deliver on its promises. We've touched on this earlier, but the relationship between marketing and R&D warrants special emphasis.

The R&D effort is usually handled by scientists, engineers, and other specialists who have technical training and skills. Their work can make an important contribution to a firm's competitive advantage—especially if it competes in high-tech markets. However, technical creativity by itself is not enough. The R&D effort must be guided by the type of market-oriented new-product development process we've been discussing.

From the idea generation stage to the commercialization stage, the R&D specialists, the operations people, and the marketing people must work together to evaluate the feasibility of new ideas. They may meet in person, or communicate with e-mail or intranet sites, or perhaps via teleconferencing or some other technology. There are many ways to share ideas. So it isn't sensible for a marketing manager to develop elaborate marketing plans for goods or services that the firm simply can't produce—or produce profitably. It also doesn't make sense for R&D people to develop a technology or product that does not have potential for the firm and its markets. Clearly, a balancing act is involved here. But the critical point is the basic one we've been emphasizing throughout the whole book: marketing-oriented firms seek to satisfy customer needs at a profit with an integrated, whole company effort.

A complicated, integrated effort is needed

Developing new products should be a total company effort. The whole process—involving people in management, research, production, promotion, packaging, and branding—must move in steps from early exploration of ideas to development of the product and marketing mix. Even with a careful development process, many new products do fail—usually because a company skips some steps in the process. Because speed can be important, it's always tempting to skip needed steps when some part of the process seems to indicate that the company has a "really good idea." But the process moves in steps—gathering different kinds of information along the way. By skipping steps, a firm may miss an important aspect that could make a whole strategy less profitable or actually cause it to fail.

Eventually, the new product is no longer new—it becomes just another product. In some firms, at this point the new-product people turn the product over to the regular operating people and go on to developing other new ideas. In other firms, the person who was the new-product champion continues with the product, perhaps taking on the broader responsibility for turning it into a successful business.

Need for Product Managers

Product variety leads to product managers

When a firm has only one or a few related products, everyone is interested in them. But when many new products are being developed, someone should be put in charge of new-product planning to be sure it is not neglected. Similarly, when a firm has products in several different product categories, management may decide to put someone in charge of each category, or each brand, to be sure that attention to these products is not lost in the rush of everyday business. **Product managers** or **brand managers** manage specific products—often taking over the jobs formerly handled by an advertising manager. That gives a clue to what is often their major responsibility—Promotion—since the products have already been developed by the new-product people. However, some brand managers start at the new-product development stage and carry on from there.

Product managers are especially common in large companies that produce many kinds of products. Several product managers may serve under a marketing manager. Sometimes these product managers are responsible for the profitable operation of a particular product's whole marketing effort. Then they have to coordinate their efforts with others—including the sales manager, advertising agencies, production and research people, and even channel members. This is likely to lead to difficulties if product managers have no control over the marketing strategy for other related brands or authority over other functional areas whose efforts they are expected to direct and coordinate.

To avoid these problems, in some companies the product manager serves mainly as a "product champion"—concerned with planning and getting the promotion effort implemented. A higher-level marketing manager with more authority

3M Sticks to Its Focus on Innovation

Minnesota Mining & Manufacturing (3M) is fast and successful in spinning out new products. This isn't just by chance. 3M's top executive set an objective that 30 percent of sales should come from products that didn't exist four years ago. You see the emphasis on innovation in even the quickest visit to 3M's website (www.3m.com). For example, current 3M innovations include radiant light film (for uses ranging from graphical signage to glittery toys), elastomers (which seal in aggressive chemicals in high-temperature settings), and electrostatic fibers (that filter dust out of heating vents). You can see why 3M says, "we are always new."

3M motivates innovation by staying close to customers, rewarding new-product champions, and sharing ideas among divisions. Teams from marketing, operations, and R&D screen new-product concepts for the ones with the highest profit potential. Then everyone works to bring the best ones to market fast. 3M's Scotch-Brite Never Rust Wool Soap Pads show how this approach can succeed. Consumers told 3M marketing researchers that they wanted an improved soap pad. Ordinary steel wool pads leave rust stains on sinks and tiny metal splinters in dishpan hands. 3M screens new products for their environmental impact, so the R&D people developed a pad using plastic fibers from recycled plastic bottles. Experts from 3M's abrasives division figured out how to coat the fibers with fine abrasives and biodegradable soap. Further marketing research refined the shape of the pads, and test markets evaluated details of the marketing plan. For example, tests confirmed that consumers liked the colorful package made from recycled paper and would pay more for Never Rust pads than they did for Brillo.

The managers varied the marketing plan for different countries. In mature markets such as the U.S. and Brazil where steel wool pads already had a large consumer base, the objective was to capture share. In Japan, where steel wool is not commonly used, the objective was to pioneer the market and attract new customers. In a firm renowned for innovation, the launch of Never Rust pads was one of 3M's most profitable ever.

3M is also serious about how its innovations affect consumer welfare. When managers learned that traces of a chemical in 3M's Scotchgard fabric protector might persist in the environment, they didn't wait for scientists to do more tests. They voluntarily pulled the popular product off the market—before they even knew if R&D could find a substitute chemical.[33]

www.mhhe.com/fourps

coordinates the efforts and integrates the marketing strategies for different products into an overall plan.

The activities of product managers vary a lot depending on their experience and aggressiveness and the company's organizational philosophy. Today companies are emphasizing marketing *experience*—because this important job takes more than academic training and enthusiasm. But it is clear that someone must be responsible for developing and implementing product-related plans—especially when a company has many products.[34]

Consumer packaged goods companies, like Nabisco, usually assign brand managers who are responsible for individual products. However, when there are a number of products in the same product category there is often a higher-level manager who ensures that the marketing program for the whole category is effective.

Conclusion

New-product planning is an increasingly important activity in a modern economy because it is no longer very profitable to just sell me-too products in highly competitive markets. Markets, competition, and product life cycles are changing at a fast pace.

The product life cycle concept is especially important to marketing strategy planning. It shows that a firm needs different marketing mixes—and even strategies—as a product moves through its cycle. This is an important point because profits change during the life cycle—with most of the profits going to the innovators or fast copiers.

We pointed out that a product is new to a firm if it is new in any way or to any target market. But the Federal Trade Commission takes a narrower view of what you can call "new."

New products are so important to business survival that firms need some organized process for developing them. We discuss such a process and emphasize that it requires a total company effort to be successful.

The failure rate of new products is high—but it is lower for better-managed firms that recognize product development and management as vital processes. Some firms appoint product managers to manage individual products and new-product teams to ensure that the process is carried out successfully.

Questions and Problems

1. Explain how industry sales and industry profits behave over the product life cycle.
2. Cite two examples of products that you feel are currently in each of the product life-cycle stages. Consider services as well as physical goods.
3. Explain how you might reach different conclusions about the correct product life-cycle stage(s) in the worldwide automobile market.
4. Explain why individual brands may not follow the product life-cycle pattern. Give an example of a new brand that is not entering the life cycle at the market introduction stage.
5. Discuss the life cycle of a product in terms of its probable impact on a manufacturer's marketing mix. Illustrate using personal computers.
6. What characteristics of a new product will help it to move through the early stages of the product life cycle more quickly? Briefly discuss each characteristic—illustrating with a product of your choice. Indicate how each characteristic might be viewed in some other country.
7. What is a new product? Illustrate your answer.
8. Explain the importance of an organized new-product development process and illustrate how it might be used for *(a)* a new hair care product, *(b)* a new children's toy, and *(c)* a new subscribers-only cable television channel.
9. Discuss how you might use the new-product development process if you were thinking about offering some kind of summer service to residents in a beach resort town.
10. Explain the role of product or brand managers. When would it make sense for one of a company's current brand managers to be in charge of the new-product development process? Explain your thinking.
11. If a firm offers one of its brands in a number of different countries, would it make sense for one brand manager to be in charge, or would each country require its own brand manager? Explain your thinking.
12. Discuss the social value of new-product development activities that seem to encourage people to discard products that are not all worn out. Is this an economic waste? How worn out is all worn out? Must a shirt have holes in it? How big?

Suggested Cases

3. Pillsbury's Häagen-Dazs
12. ChemTech
20. Outdoor World, Inc.

Computer-Aided Problem

10. **Growth Stage Competition**

AgriChem, Inc., has introduced an innovative new product—a combination fertilizer, weed killer, and insecticide that makes it much easier for soybean farmers to produce a profitable crop. The product introduction was quite successful, with 1 million units sold in the year of introduction. And AgriChem's profits are increasing. Total market demand is expected to grow at a rate of 200,000 units a year for the next five years. Even so, AgriChem's marketing managers are concerned about what will happen to sales and profits during this period.

Based on past experience with similar situations, they expect one new competitor to enter the market during each of the next five years. They think this competitive pressure will drive prices down about 6 percent a year. Further, although the total market is growing, they know that new competitors will chip away at AgriChem's market share—even with the 10 percent a year increase planned for the promotion budget. In spite of the competitive pressure, the marketing managers are sure that familiarity with AgriChem's brand will help it hold a large share of the total market and give AgriChem greater economies of scale than competitors. In fact, they expect that the ratio of profit to dollar sales for AgriChem should be about 10 percent higher than for competitors.

AgriChem's marketing managers have decided the best way to get a handle on the situation is to organize the data in a spreadsheet. They have set up the spreadsheet so they can change the "years in the future" value and see what is likely to happen to AgriChem and the rest of the industry. The starting spreadsheet shows the current situation with data from the first full year of production.

a. *Compare AgriChem's market share and profit for this year with what is expected next year—given the marketing managers' current assumptions. What are they expecting? (Hint: Set number of years in the future to 1.)*
b. *Prepare a table showing AgriChem's expected profit, and the expected industry revenue and profit, for the current year and the next five years. Briefly explain what happens to industry sales and profits and why. (Hint: Do an analysis to vary the number of years in the future value in the spreadsheet from a minimum of 0—the current year—to a maximum of 5. Display the three values requested.)*
c. *If market demand grows faster than expected—say, at 280,000 units a year—what will happen to AgriChem's profits and the expected industry revenues and profits over the next five years? What are the implications of this analysis?*

For additional questions related to this problem, see Exercise 10-3 in the *Learning Aid for Use with Basic Marketing*, 14th edition.

When You Finish This Chapter, You Should

1. Understand what product classes suggest about Place objectives.

2. Understand why some firms use direct channel systems while others rely on intermediaries and indirect systems.

3. Understand how and why marketing specialists develop to make channel systems more effective.

4. Understand how to develop cooperative relationships and avoid conflict in channel systems.

5. Know how channel members in vertical marketing systems shift and share functions—to meet customer needs.

6. Understand the differences between intensive, selective, and exclusive distribution.

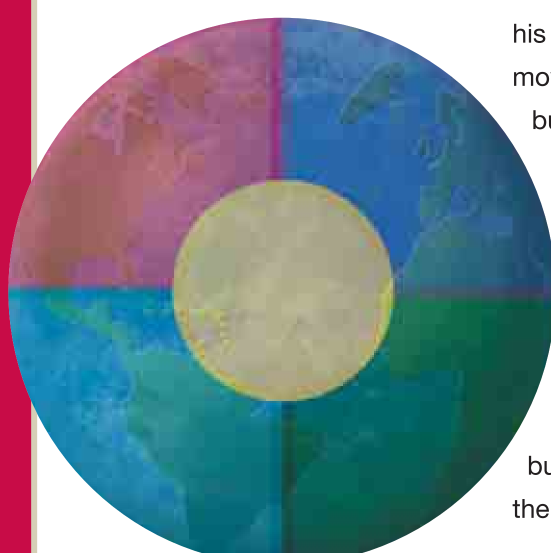
7. Understand the important new terms (shown in red).

Chapter Eleven

Place and Development of Channel Systems

Steve Bollic's small firm creates video game software. In the summer of 2001, he learned that Ingram Book Group, a book wholesaler, had formed an alliance with Valley Media, Inc., a distributor of music and entertainment products. Most people in his product-market would have glossed over that news, but in his previous job Bollic had gotten a taste of what it might mean: tough new competition from game producers whose distribution channels focused on the big retail chains.

Bollic had been a manager for the Intimate Bookshops, a small chain of shops that for decades had been *the* place to buy books in his college-town market. He moved on to start his video game business even before the Intimate had its final clearance sale and closed its doors for good. After all, sales of books through independent bookshops dropped by over 25 percent in the 1990s. Like the Intimate, many went out of business because of changes in the channels of distribution for

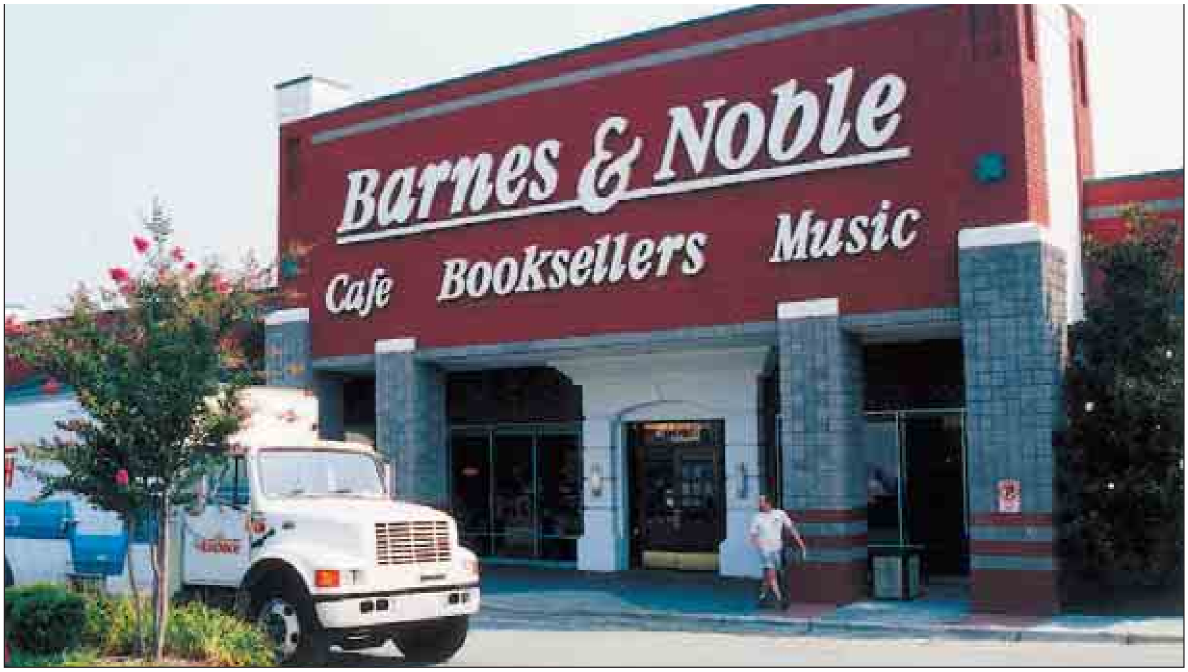


price

place

promotion

produc



books. Many small publishers with whom they worked also had troubles.

At the Intimate, competitors had chipped away at sales over the years. But the coffin nail was not driven by mail-order book clubs, or by the religious book store that opened in town, or even by used textbook brokers who ate into that business. Rather, the bigger issue was the big national chains. They had buying clout with publishers and could demand lower prices for larger quantities. They also had aggressive marketing programs to woo consumers. The Intimate had lost some customers to the frequent-buyer discount and special-order service at Walden Books. Others went to Barnes and Noble for the selection—and the coffee bar. Wal-Mart carried only a few best-sellers, but its low prices turned shoppers into impulse buyers. Some of the Intimate's ex-customers were no longer shopping in any store. Rather, they were ordering books online from Amazon.com.

Operating from its website, Amazon offers consumers an amazing selection of over two million books. As Amazon ads pop up on-screen, web surfers may think the selection is even greater. But Bollic knew that in reality Amazon's warehouse keeps inventory on only a couple thousand of the fastest-selling books. That's because Amazon fills most orders through wholesalers. And that takes us back to Ingram Book Group. It has been the hidden giant behind many big book retailers, including Internet sellers. For example, in 1998 it handled more than 60 percent of Amazon's orders. At the same time it was a major supplier for Barnes and Noble. There are good reasons. Its distribution customer service is hard to match. Orders flow into Ingram's computers electronically, and most are assembled and shipped the same day from its inventory of 500,000 titles. With a half-dozen warehouses spread across the country, Ingram gets 95 percent of its shipments to the retailer within 48 hours. You can see why Barnes and Noble wanted to merge with Ingram; this vertical integration would have made the combined firm even more efficient and powerful.

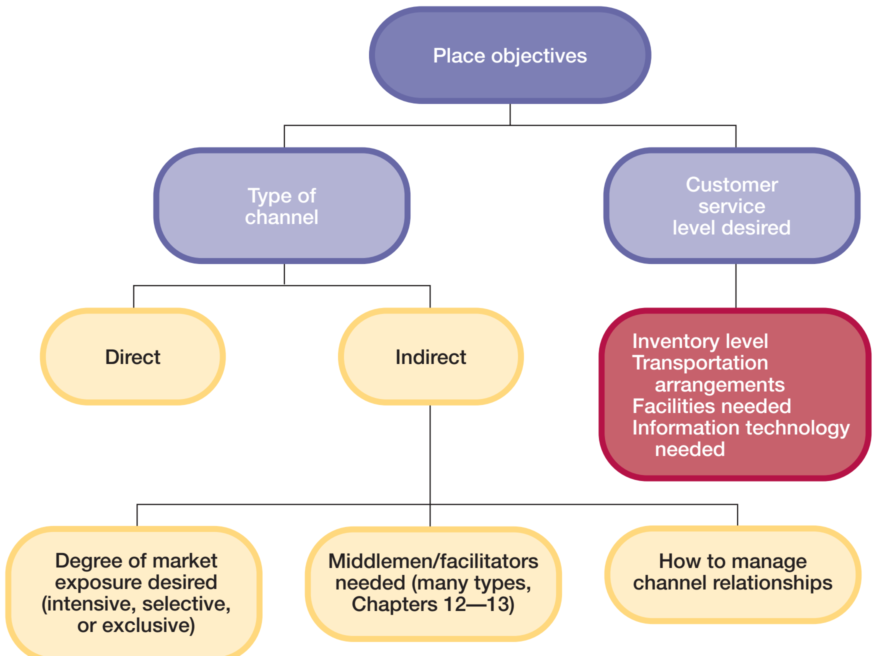
When that merger fell through, Barnes and Noble expanded its own distribution centers, inventory, and logistics systems to become more efficient on its own. Ingram, in turn, is getting new business by offering its retailer-customers new services—like sending books directly to the consumer. But Ingram is also adding music and entertainment products, like video games, to its line. That's because many of the retailer-customers it serves are scrambling their product lines to include the best sellers among these categories. With video games becoming a mature product, it is not a complete surprise that distribution intensity is expanding. But it may mean that Bollic will need to decide whether to join one of these new channel systems or stick with the specialists who helped him get started.[1]

Place Decisions Are an Important Part of Marketing Strategy

As this example shows, offering customers a good product at a reasonable price is important to a successful marketing strategy. But it's not the whole story. Managers must also think about **Place**—making goods and services available in the right quantities and locations—when customers want them. And when different target markets have different needs, a number of Place variations may be required. Our opening case also makes it clear that new Place arrangements can dramatically change the competition in a product-market. This is especially important in business today because many firms are trying to use new information technologies, including websites and aspects of e-commerce, to reach customers directly. Of course, not every consumer (or business customer) wants to buy products online;

To provide solutions to problems faced by more different types of home improvement customers, Home Depot has supplemented its home improvement warehouse stores with Expo Design Centers and smaller Villager's Hardware Stores.

Exhibit 11-1
Strategy Decision Areas in Place



but the numbers are increasing, prompting firms to rethink the ways that they can provide greater value to their target markets.

In the next three chapters, we'll deal with the many important strategy decisions that a marketing manager must make concerning Place. Exhibit 11-1 gives an overview. We'll start in this chapter with a discussion of the type of channel that's needed to meet customers' needs. We'll show why specialists are often involved and how they come together to form a **channel of distribution**—any series of firms or individuals who participate in the flow of products from producer to final user or consumer. We'll also consider how to manage relations among channel members to reduce conflict and improve cooperation.

In Chapter 12, we'll expand our coverage of Place to include decisions that a marketing manager makes to decide what level of distribution service to offer—and why he must coordinate storing and transporting activities—providing the desired service at a reasonable cost. Then, in Chapter 13, we'll take a closer look at the many different types of retailing and wholesaling firms. We'll consider their role in channels as well as the strategy decisions they make to satisfy their own customers.

Place Decisions Are Guided by "Ideal" Place Objectives

All marketing managers want to be sure that their goods and services are available in the right quantities and locations—when customers want them. But customers may have different needs with respect to time, place, and possession utility as they make different purchases.

Product classes suggest Place objectives

You've already seen this with the product classes—which summarize consumers' urgency to have needs satisfied and willingness to seek information, shop, and compare. Now you should be able to use the product classes to handle Place decisions.

Most pet food companies focus on distribution through grocery stores, but Science Diet brand premium pet foods reach consumers in the U.S., Japan, and Italy through a different channel—veterinary offices and pet stores. Because Science Diet has developed cooperative relationships with other members of this channel, Science Diet products often get special promotion support at the point of purchase.

Exhibit 9-3 shows the relationship between consumer product classes and ideal Place objectives. Similarly, Exhibit 9-4 shows the business product classes and how they relate to customer needs. Study these exhibits carefully. They set the framework for making Place decisions. In particular, the product classes help us decide how much market exposure we'll need in each geographic area.

Place system is not automatic

A product may be sold both to final consumers and business customers, and each type of customer may want to purchase in different ways. Further, several different product classes may be involved if different market segments view a product in different ways. Thus, just as there is no automatic classification for a specific product, we can't automatically decide the one best Place arrangement.

However, people in a particular target market should have similar attitudes and therefore should be satisfied with the same Place system. If different target segments view a product in different ways, marketing managers may need to develop several strategies, each with its own Place arrangements.

Place decisions have long-run effects

The marketing manager must also consider Place objectives in relation to the product life cycle; see Exhibit 10-2. Place decisions often have long-run effects. They're usually harder to change than Product, Price, and Promotion decisions. Many firms that thought they could quickly establish effective websites for direct online sales, for example, found that it took several years and millions of dollars to work out the kinks. It can take even longer to develop effective working relationships with others in the channel. Legal contracts with channel partners may also limit changes. And it's hard to move retail stores and wholesale facilities once leases are signed and customer shopping patterns are settled. Yet as products mature, they typically need broader distribution to reach different target customers.

The distribution of premium pet foods followed this pattern. A decade ago, supermarkets wouldn't carry specialized pet foods because there wasn't much demand. So marketing managers for Science Diet products concentrated on getting distribution through pet shops and veterinary offices. These pet professionals were already focused on Science Diet's target market. Science Diet's sales in this channel grew rapidly. What's more, profit margins on the specialty foods were much higher than on traditional fare. Seeing that this market was growing, Purina, Kal Kan, and other producers developed new products and worked with their supermarket channels to set up special "nutrition centers" on the pet food aisle. P&G bought Iams and pushed for distribution in pet superstores, at mass-merchandisers, and online. Perhaps the competition among channels was inevitable. But Science Diet is still doing well in its own channel. It's also using the same approach to expand into other countries. In pet stores in Japan and Italy, for example, Science Diet attracts new customers with special displays, samples, and free literature.[2]

Channel System May Be Direct or Indirect

One of the most basic Place decisions producers must make is whether to handle the whole distribution themselves—perhaps by relying on direct-to-customer e-commerce selling—or use wholesalers, retailers, and other specialists (see Exhibit 11-1). Middlemen, in turn, must select the producers they'll work with.

Why a firm might want to use direct distribution

Many firms prefer to distribute directly to the final customer or consumer. One reason is that they want complete control over the marketing job. They may think that they can serve target customers at a lower cost or do the work more effectively than middlemen. Further, working with independent middlemen with different objectives can be troublesome.

The Internet makes direct distribution easier

Website-based e-commerce systems give many firms direct access to prospects and customers whom it would have been difficult or impossible to reach in the past. Even very small, specialized firms may be able to establish a web page and draw customers from all over the world. Of course, there are limitations. If a customer wants a salesperson to demonstrate a product, then a "virtual store" may not be adequate. However, the concept of distribution over the Internet is still evolving. Some firms now use live camera "feeds" while talking with the customer over an Internet video phone. Other innovations are being tested. Regardless, if it's with the help of technology or by other more traditional means, there often *are* great advantages in selling directly to the final user or consumer.

Direct contact with customers

If a firm is in direct contact with its customers, it is more aware of changes in customer attitudes. It is in a better position to adjust its marketing mix quickly because there is no need to convince other channel members to help. If a product needs an aggressive selling effort or special technical service, the marketing manager can ensure that salespeople receive the necessary training and motivation. In contrast, middlemen often carry products of several competing producers. So they might not give any one item the special emphasis its producer wants.

In the U.S. and many other developed nations, Unilever relies primarily on indirect distribution through a variety of wholesalers and retailers. However, in Spain it delivers frozen foods directly to consumer homes, and in Vietnam a mobile store brings products to local consumers. And now some products are sold direct to consumers from an Internet website.

When Snapple bought SoBe's main wholesaler in New Jersey, other goods wholesalers were not available and SoBe was left with limited distribution. So marketers for SoBe sold directly to retailers. Getting retailer cooperation and good shelf space was easier when SoBe provided its own coolers.

Suitable middlemen are not available

A firm may have to go direct if suitable middlemen are not available or will not cooperate. For example, Apple is again opening its own stores in hopes of getting more in-store promotional emphasis on what's different about its iMac computers.[3]

Middlemen who have the best contacts with the target market may be hesitant to add unproven vendors or new products, especially really new products that don't fit well with their current business. Many new products die because the producer can't find willing middlemen and doesn't have the financial resources to handle direct distribution.

In the United States, the Census Bureau publishes detailed data concerning wholesalers and retailers, including breakdowns by kind of business, product line, and geographic territory. Similar information is available for Canada and many other countries, including most of those in the European Union. Most of this data is available online. It can be very valuable in strategy planning—especially to learn whether potential channel members are serving a target market. You can also learn what sales volume current middlemen are achieving.

Common with business customers and services

Many business products are sold direct-to-customer. Rolm, for example, sells its computerized voice mail systems direct. Alcan sells aluminum to General Motors direct. And Honda sells its motors direct to lawn mower producers. This is understandable since in business markets there are fewer transactions and orders are larger. In addition, customers may be concentrated in a small geographic area, making distribution easier. Further, once relationships are established e-commerce systems can provide an efficient way to handle orders, inventory replenishment, and routine information needs (such as delivery schedules).

Service firms often use direct channels. If the service must be produced in the presence of customers, there may be little need for middlemen. An accounting firm like Arthur Andersen, for example, must deal directly with its customers. However, many firms that produce physical goods turn to middlemen specialists to help provide the services customers expect as part of the product. Maytag may hope that its authorized dealers don't get many repair calls, but the service is available when customers need it. Here the middleman produces the service.[4]

Some consumer products are sold direct

Many companies that produce consumer products have websites where a consumer can place a direct order. But for most consumer products this is still a small part of total sales. Most consumer products are sold through middlemen.

Internet

Internet Exercise Gateway is a computer company that uses direct distribution to its customers in the U.S. Go to the Gateway website (www.gateway.com) and think about how it is organized. Is the website organized well to help Gateway reach different segments of customers in the U.S.?

Of course, some consumer products are sold direct to consumers' homes. Tupperware, Mary Kay and Avon cosmetics, Electrolux vacuum cleaners, Amway household products, and Fuller Brush products are examples. Most of these firms rely on direct selling, which involves personal sales contact between a representative of the company and an individual consumer. However, most of these "salespeople" are *not* company employees. Rather, they usually work as independent middlemen, and the companies that they sell for refer to them as dealers, distributors, agents, or some similar term. So in a strict technical sense, this is not really direct producer-to-consumer distribution. That does not mean, however, that this approach is unimportant. It has grown both in the U.S. and in international markets. In fact, many U.S. firms are finding that it's the best way to crack open international markets. Some of the distribution arrangements might surprise you. For example, Mattel has teamed up with Avon door-to-door representatives to sell its Barbie dolls in China.[5]

Don't be confused by the term *direct marketing*

An increasing number of firms now rely on **direct marketing**—direct communication between a seller and an individual customer using a promotion method other than face-to-face personal selling. Sometimes direct marketing promotion is coupled with direct distribution from a producer to consumers. Park Seed Company, for example, sells the seeds it grows directly to consumers with a mail catalog. However, many firms that use direct marketing promotion distribute their products through middlemen. So the term *direct marketing* is primarily concerned with the Promotion area, not Place decisions. We'll talk about direct marketing promotion in more detail in Chapter 14.[6]

When indirect channels are best

Even if a producer wants to handle the whole distribution job, sometimes it's simply not possible. Customers often have established buying patterns. For example, Square D, a producer of electrical supplies, might want to sell directly to electrical contractors. It can certainly set up a website for online orders or even open sales offices in key markets. But if contractors like to make all of their purchases in one convenient stop—at a local electrical wholesaler—the only practical way to reach them is through a wholesaler.

Consumers want convenience

Similarly, consumers are spread throughout many geographic areas and often prefer to shop for certain products at specific places. Some consumers, for instance, see Sears as *the* place to shop for tires, so they'll only buy the brands that Sears carries. Similarly, a consumer may see a Walgreens drugstore as *the* place to shop for emergency items—because it's conveniently located in the neighborhood. Moreover, if retailers who serve target customers make most of their purchases from specific wholesalers, the producer may have to work with these wholesalers. This is one reason why most firms that produce consumer products rely so heavily on indirect channels (see Exhibit 2-10).[7]

Middlemen may invest in inventory

Direct distribution usually requires a significant investment in facilities, people, and information technology. A new company, one that has limited financial resources, or one that wants to retain flexibility, may want to avoid that investment by working with established middlemen.

Middlemen may further reduce a producer's investment and need for working capital by buying the producer's output and carrying it in inventory until it's sold. If customers want a good "right now," there must be an inventory available to make the sale. And if customers are spread over a large area, it will probably be necessary to have widespread distribution.

Middlemen may reduce credit risk

Some middlemen play a critical role by providing credit to customers at the end of the channel. This financing function may be very important to small business customers; it provides their working capital. Even if the producer could afford to provide credit, a middleman who knows local customers can help reduce credit risks. As sales via the Internet grow, sellers are looking for faster and better ways to check the credit ratings of distant customers. It's an unhappy day when the marketing manager learns that a customer who was shipped goods based on an online order can't pay the invoice.

As these examples suggest, there may be a number of reasons why a producer might want to work with a specific wholesaler or retailer. However, the most important reason for using an indirect channel of distribution is that an intermediary can often help producers serve customer needs better and at lower cost. Remember that we discussed this briefly in Chapter 1 (see Exhibit 1-3). Now we'll go into more detail so you'll be able to plan different kinds of distribution channels.

Channel Specialists May Reduce Discrepancies and Separations

The assortment and quantity of products customers want may be different from the assortment and quantity of products companies produce. Producers are often located far from their customers and may not know how best to reach them. Customers in turn may not know about their choices. Specialists develop to adjust these discrepancies and separations.[8]

Middlemen may supply needed information

Specialists often help provide information to bring buyers and sellers together. For example, most consumers don't know much about the wide variety of home and auto insurance policies available from many different insurance companies. A local independent insurance agent may help them decide which policy, and which insurance company, best fits their needs. In the same vein, a furniture retailer can help a customer find a producer who has a certain style chair with just the right combination of fabric and finish.

Middlemen who are close to their customers are often in a better position to anticipate customer needs and forecast demand more accurately. This information can help reduce inventory costs in the whole channel—and it may help the producer smooth out production.

Most producers seek help from specialists when they first enter international markets. Specialists can provide crucial information about customer needs and insights into differences in the marketing environment.

Discrepancies of quantity and assortment

Discrepancy of quantity means the difference between the quantity of products it is economical for a producer to make and the quantity final users or consumers normally want. For example, most manufacturers of golf balls produce large quantities—perhaps 200,000 to 500,000 in a given time period. The average golfer, however, wants only a few balls at a time. Adjusting for this discrepancy usually requires middlemen—wholesalers and retailers.

Office Depot, a large office supplies chain, accumulates products from many producers at its distribution center and then breaks bulk to provide the convenient assortments that consumers expect to find at individual Office Depot stores.

Producers typically specialize by product—and therefore another discrepancy develops. **Discrepancy of assortment** means the difference between the lines a typical producer makes and the assortment final consumers or users want. Most golfers, for example, need more than golf balls. They want golf shoes, gloves, clubs, a bag, and, of course, a golf course to play on. And they usually don't want to shop for each item separately. So, again, there is a need for wholesalers and retailers to adjust these discrepancies.

In actual practice, bringing products to customers isn't as simple as the golf example. Specializing only in golfing products may not achieve all the economies possible in a channel of distribution. Retailers who specialize in sports products usually carry even wider assortments. And they buy from a variety of wholesalers who specialize by product line. Some of these wholesalers supply other wholesalers. These complications will be discussed later. The important thing to remember is that discrepancies in quantity and assortment cause distribution problems for producers and explain why many specialists develop.

Channel specialists adjust discrepancies with regrouping activities

Regrouping activities adjust the quantities and/or assortments of products handled at each level in a channel of distribution.

There are four regrouping activities: accumulating, bulk-breaking, sorting, and assorting. When one or more of these activities is needed, a marketing specialist may develop to fill this need.

Adjusting quantity discrepancies by accumulating and bulk-breaking

Accumulating involves collecting products from many small producers. Much of the coffee that comes from Colombia is grown on small farms in the mountains. Accumulating the small crops into larger quantities is a way of getting the lowest transporting rate and making it more convenient for distant food processing companies to buy and handle it. Accumulating is especially important in less-developed countries and in other situations, like agricultural markets, where there are many small producers.

Accumulating is also important with professional services because they often involve the combined work of a number of individuals, each of whom is a specialized producer. A hospital makes it easier for patients by accumulating the services of a number of health care specialists, many of whom may not actually work for the hospital.

To reach its place objectives, Sprint sells PCS phones and its wireless services through 12,000 outlets, including retail chains like Staples and its own Sprint PCS Centers.

Many middlemen who operate from Internet websites focus on accumulating. Specialized sites for everything from Chinese art to Dutch flower bulbs bring together the output of many producers.

Bulk-breaking involves dividing larger quantities into smaller quantities as products get closer to the final market. Sometimes this even starts at the producer's level. A golf ball producer may need 25 wholesalers to help sell its output. And the bulk-breaking may involve several levels of middlemen. Wholesalers may sell smaller quantities to other wholesalers or directly to retailers. Retailers continue breaking bulk as they sell individual items to their customers.

Adjusting assortment discrepancies by sorting and assorting

Different types of specialists adjust assortment discrepancies. They perform two types of regrouping activities: sorting and assorting.

Sorting means separating products into grades and qualities desired by different target markets. For example, an investment firm might offer its customers a chance to buy shares in a mutual fund made up only of stocks for certain types of companies—high-growth firms, ones that pay regular dividends, or ones that have good environmental track records.

Similarly, a wholesaler that specializes in serving convenience stores may focus on smaller packages of frequently used products, whereas a wholesaler working with restaurants and hotels might handle only very large institutional sizes.

Sorting is also a very important process for raw materials. Nature produces what it will—and then the products must be sorted to meet the needs of different target markets.

Assorting means putting together a variety of products to give a target market what it wants. This usually is done by those closest to the final consumer or user—retailers or wholesalers who try to supply a wide assortment of products for the convenience of their customers. A grocery store is a good example. But some assortments involve very different products. A wholesaler selling Yazoo tractors and mowers to golf courses might also carry Pennington grass seed, Scott fertilizer, and even golf ball washers or irrigation systems—for its customers' convenience.

Watch for changes

Sometimes these discrepancies are adjusted badly—especially when consumer wants and attitudes shift rapidly. When cellular phones suddenly became popular, an opportunity developed for a new specialist. Cellular phone dealers came on the scene to help customers figure out what type of cellular phone and service would meet their needs. After all, the traditional phone companies didn't initially offer these services. However, it cost the sellers of cellular services about $300 per customer to sell through dealers. As the market grew and the competition for customers

A channel captain can improve the performance of the whole channel—by developing strategies that help everyone in the channel do a better job of meeting the needs of target customers at the end of the channel.

heated up, electronics stores wanted a piece of the action, and they were willing to take a smaller markup. Now that the market is much more established, many cellular service providers are finding it cheaper to sell from a website or use their own salespeople.[9]

Specialists should develop to adjust discrepancies *if they must be adjusted.* But there is no point in having middlemen just because that's the way it's been done in the past. Sometimes a breakthrough opportunity can come from finding a better way to reduce discrepancies—perhaps eliminating some steps in the channel. Many small manufacturers of business products can now reach more customers in distant markets with an Internet website than it was previously possible for them to reach with independent manufacturers reps who sold on commission (but otherwise left distribution to the firm). If it costs the firm less to establish an order-taking website and advertise it by e-mail, at an industry community site, or in a trade magazine, the cost advantage can translate to lower prices and a marketing mix that is a better value for some target segments.[10]

Channel Relationship Must Be Managed

Marketing manager must choose type of channel relationship

Middlemen specialists can help make a channel more efficient. But there may be problems getting the different firms in a channel to work together well. How well they work together depends on the type of relationship they have. This should be carefully considered since marketing managers usually have choices about what type of channel system to join or develop.

The whole channel should have a product-market commitment

Ideally, all of the members of a channel system should have a shared *product-market commitment*—with all members focusing on the same target market at the end of the channel and sharing the various marketing functions in appropriate ways. When members of a channel do this, they are better able to compete effectively for the customer's business.

This simple idea is very important. Unfortunately, many marketing managers overlook it because it's not the way their firms have traditionally handled relationships with others in the channel.

Traditional channel systems involve weak relationships

In **traditional channel systems,** the various channel members make little or no effort to cooperate with each other. They buy and sell from each other—and that's the extent of their relationship. Each channel member does only what it considers to be in its own best interest; it doesn't worry much about the effect of its policies on other members of the channel. This is shortsighted, but it's easy to see how it can happen. The objectives of the various channel members may be different. For example, General Electric wants a wholesaler of electrical building supplies to sell GE products. But an independent wholesaler who carries an assortment of products from different producers may not care whose products get sold. The wholesaler just wants happy customers and a good profit margin.

Conflict gets in the way

Specialization has the potential to make a channel more efficient—but not if the specialists are so independent that the channel doesn't work smoothly. Because members of traditional channel systems often have different objectives—and different ideas about how things should be done—conflict is common.

There are two basic types of conflict in channels of distribution. Vertical conflicts occur between firms at different levels in the channel of distribution. For example, a producer and a retailer may disagree about how much shelf space or promotion effort the retailer should give the producer's product. Or conflict may arise if a producer that wants to reduce its excess inventory pushes a wholesaler to carry more inventory than the wholesaler really needs.

Recently there was vertical conflict between big recording companies—like Sony, Warner Music, and Capitol-EMI—and their retail outlets that wanted to sell used CDs as well as new releases. Retailers were responding to consumers who liked the low cost of used CDs, but the recording companies argued that the used CDs ate into their sales and deprived artists of royalties. When Wherehouse Entertainment (a large retail music chain) started to sell used CDs—at about half the price of new ones—several recording companies said that they would halt cooperative advertising payments to any retailer that sold used CDs. Garth Brooks, the best-selling artist at the time, underscored the conflict and the recording companies' point of view. He said that he would not release his new CDs to any stores that were selling used CDs.[11]

Horizontal conflicts occur between firms at the same level in the channel of distribution. For example, a furniture store that keeps a complete line of furniture on display isn't happy to find out that a store down the street is offering customers lower prices on special orders of the same items. The discounter is getting a free ride from the competing store's investment in inventory. And nothing gets an independent retailer more charged up than finding out that a chain store is selling some product for less than the wholesale price the independent pays.

Traditional channel systems are still typical, and very important, in some industries. The members of these channels have their independence, but they may pay for it too. As we will see, such channels are declining in importance—with good reason.[12]

Cooperative relationships share common objectives

Potential channel conflicts should be anticipated and, if possible, resolved. Usually the best way to do that is to get everyone in the channel working together in a cooperative relationship that is focused on the same basic objective—satisfying the customer at the end of the channel. This leads us away from traditional channels to cooperative channel relationships and the channel captain concept.

Channel captain can guide channel relationships

Each channel system should act as a unit, where each member of the channel collaborates to serve customers at the end of the channel. In this view, cooperation is everyone's responsibility. However, some firms are in a better position to take the lead in the relationship and in coordinating the whole channel effort. This situation calls for a **channel captain**—a manager who helps direct the activities of a whole channel and tries to avoid or solve channel conflicts.

For example, when Harley-Davidson saw an opportunity to expand sales of its popular fashion accessories, it was difficult for motorcycle dealers to devote enough space to all of the different styles and sizes. Harley considered selling the items directly from its own website, but that would take sales away from dealers who were working hard to help Harley sell both cycles and fashions. So Harley's president asked a group of dealers and Harley managers to work together to come up with a plan they all liked. The result was a website that sells Harley products through the dealer that is closest to the customer.[13]

The concept of a single channel captain is logical. But some channels, including most traditional ones, don't have a recognized captain. The various firms don't act as a system. The reason may be lack of leadership or the fact that members of the system don't understand their interrelationship. Many managers—more concerned with individual firms immediately above and below them—seem unaware that they are part of a channel.

But like it or not, firms are interrelated, even if poorly, by their policies. So it makes sense to try to avoid channel conflicts by planning for channel relations. The channel captain arranges for the necessary functions to be performed in the most effective way.

The situation faced by Goodyear is a good example. The Goodyear brand was sold almost exclusively through its own stores and its 2,500 independent tire dealers. But sales were falling. There were many reasons. France's Michelin and Japan's Bridgestone had aggressively expanded distribution in North America. The 850 Sears autocenters were selling one-tenth of all replacement tires. Moreover, many consumers were shopping at discount outlets and warehouse clubs. Goodyear decided it had no choice but to expand distribution beyond its independent dealer network. One of the first changes was to sell Goodyear tires to Sears, Kmart's Penske autocenters, and other big retail chains. To better reach the discount shoppers, Goodyear converted many of its company-owned autocenters to no-frills, quick-serve stores operated under the Just Tires name. However, to reduce the conflict that these changes caused with its independent dealers, Goodyear introduced new lines of premium tires—like the innovative Aquatred line and specialized lines for sports cars and 4-wheel drive vehicles. These were tires that appealed to the dealers' target market. Goodyear also increased advertising and promotion support to pull more customers into the dealers' stores, and offered training on how to build sales of related services. Goodyear also created the Gemini brand name to help promote service by Goodyear dealers. Because of this channel leadership, Goodyear's sales increased and so did the sales of its dealers.[14]

Some producers lead their channels

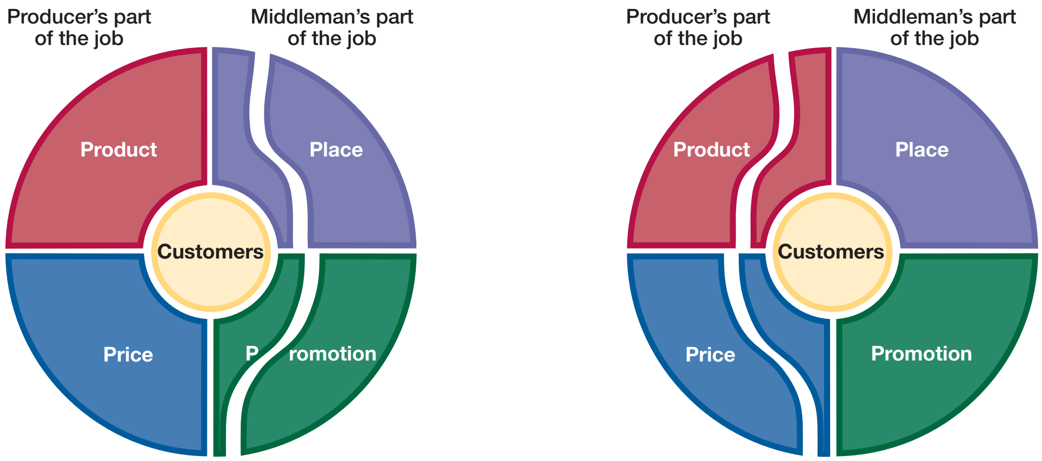
As the Goodyear case suggests, in the U.S. producers frequently take the lead in channel relations. Middlemen often wait to see what the producer intends to do and wants them to do. After marketing managers for Goodyear set Price, Promotion, and Place policies, wholesalers and retailers decide whether their roles will be profitable and whether they want to join in the channel effort.

Exhibit 11-2A shows this type of producer-led channel system. Here the producer has selected the target market and developed the Product, set the Price structure, done some consumer and channel Promotion, and developed the Place setup. Middlemen are then expected to finish the Promotion job in their respective places. Of course, in a retailer-dominated channel system, the marketing jobs would be handled in a different way.

Exhibit 11-2 How Channel Functions May Be Shifted and Shared in Different Channel Systems

A. How strategy decisions are handled in a producer-led channel

B. How strategy decisions are handled in a retailer-led channel

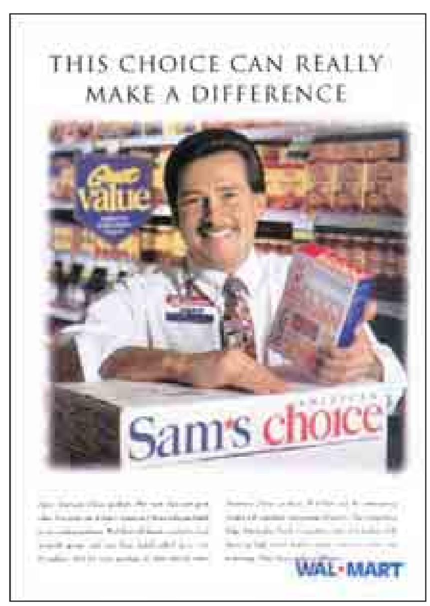


Some middlemen are channel captains

Sometimes large wholesalers or retailers do take the lead. These middlemen analyze the types of products their customers want and then seek out producers who can provide these products at reasonable prices. With the growth of powerful retail chains, like Target and Toys "R" Us, this is becoming more common in the United States. It is already typical in many foreign markets. In Japan, for example, very large wholesalers (trading companies) are often the channel captains.

Channel captains who are middlemen often develop their own dealer brands. Large retailers like Sears or Kmart and wholesalers like Ace Hardware in effect act like producers. They specify the whole marketing mix for a product and merely delegate production to a factory. Exhibit 11-2B shows how marketing strategy might be handled in this sort of retailer-led channel system.

The growing number of retailer-led channel systems is prompting growth of private label dealer brands in a wide variety of product categories.



Kimberly-Clark Boosts Bottom Line for Disposable Diapers

It's a messy problem when a busy parent makes a special trip to a Costco store to buy Huggies disposable diapers and they're out of stock. It can be costly too. The average retailer's loss from out-of-stocks on high-volume items, like diapers, is about 11 percent of annual sales. So what should a Costco manager do to avoid the problem? Nothing. That job is handled by Kimberly-Clark (KC), the firm that makes Huggies. Costco has a system that it calls "vendor managed inventory" in which key suppliers take over responsibility for managing a set of products, often a whole product category. Every day an analyst at KC's headquarters studies Costco's online data that details Huggies' sales and inventory at every Costco store. The analyst studies how much is sold of each item in each store in the average week. If inventory is getting low, a new order is placed and shipping is scheduled. It's also important not to order too much or too early. KC absorbs all of the inventory and delivery costs required to keep Huggies on the shelves at Costco. When KC does this job well, it makes more money and so does Costco. Costco is a powerful customer, but KC is the channel captain for this category. Costco could do the job itself, but it handles such a wide assortment of products that it would be costly to do all the work required in every high-volume category. Many large retailers use similar approaches. Smaller retailers, however, may find that vendors are not as eager to provide this kind of extra support. The benefits justify the costs when the vendor is more selective about where the service is provided.[15]

Some strong middlemen use their power to control channel relationships. Wal-Mart, the largest retail chain, is constantly looking for ways to cut its own costs—and sometimes that means cutting costs in the channel. Buyers for Wal-Mart look at the value added by a wholesaler. If they think Wal-Mart can be more efficient without the wholesaler, they tell the producer that the chain will only buy direct—usually at a lower price than was paid to the wholesaler.

Middlemen are closer to the final user or consumer and are in an ideal position to assume the channel captain role. Middlemen, especially large retailers, may even dominate the marketing systems of the future.[16]

Many marketing managers accept the view that a coordinated channel system can help everyone in the channel. These managers are moving their firms away from traditional channel systems and instead developing or joining vertical market systems.

Vertical Marketing Systems Focus on Final Customers

In contrast to traditional channel systems are **vertical marketing systems**—channel systems in which the whole channel focuses on the same target market at the end of the channel. Such systems make sense, and are growing, because if the final customer doesn't buy the product, the whole channel suffers. There are three types of vertical marketing systems—corporate, administered, and contractual. Exhibit 11-3 summarizes some characteristics of these systems and compares them with traditional systems.

Corporate channel systems shorten channels

Some corporations develop their own vertical marketing systems by internal expansion and/or by buying other firms. With **corporate channel systems**—corporate ownership all along the channel—we might say the firm is going "direct." But actually the firm may be handling manufacturing, wholesaling, *and* retailing—so it's more accurate to think of the firm as a vertical marketing system.

Corporate channel systems develop by vertical integration

Corporate channel systems may develop by **vertical integration**—acquiring firms at different levels of channel activity. Bridgestone, for example, has rubber plantations in Liberia, tire plants in Ohio, and wholesale and retail outlets all over the

Exhibit 11-3 Characteristics of Traditional and Vertical Marketing Systems

	Type of Channel			
		Vertical Marketing Systems		
Characteristics	**Traditional**	**Administered**	**Contractual**	**Corporate**
Amount of cooperation	Little or none	Some to good	Fairly good to good	Complete
Control maintained by	None	Economic power and leadership	Contracts	Ownership by one company
Examples	Typical channel of "independents"	General Electric, Miller Beer, O.M. Scott & Sons (lawn products)	McDonald's, Holiday Inn, IGA, Ace Hardware, Super Valu, Coca-Cola, Chevrolet	Florsheim Shoes, Sherwin-Williams, Mothers Work

world. Sherwin-Williams produces paint, but it also operates 2,000 retail outlets. In England, most of the quaint local pubs are actually owned and operated by the large beer breweries.

Corporate channel systems are not always started by producers. A retailer might integrate into wholesaling and perhaps even manufacturing. Mothers Work is a good example. It started as a mail-order catalog specializing in maternity clothes. Now it sells more than a third of all maternity clothes in the U.S. Vertical integration has been a key factor in this growth and its ability to give its customers what they want when they want it. It has over 700 company-run stores, its own designers, fabric-cutting operations, warehouses, and information systems to tie them all together.[17]

Vertical integration has potential advantages—stability of operations, assurance of materials and supplies, better control of distribution, better quality control, larger research facilities, greater buying power, and lower executive overhead.

Provided that the discrepancies of quantity and assortment are not too great at each level in a channel—that is, that the firms fit together well—vertical integration can be efficient and profitable. However, many firms that have tried vertical integration have found it difficult to achieve these efficiencies. Some managers think it's hard to be really good at running manufacturing, wholesaling, and retailing businesses that are very different from each other. Instead, they try to be more efficient at what they do best and focus on ways to get cooperation in the channel for the other activities.

Administered and contractual systems may work well

Firms can often gain the advantages of vertical integration without building an expensive corporate channel. A firm can develop administered or contractual channel systems instead. In **administered channel systems,** the channel members informally agree to cooperate with each other. They can agree to routinize ordering, share inventory and sales information over computer networks, standardize accounting, and coordinate promotion efforts. In **contractual channel systems,** the channel members agree by contract to cooperate with each other. With both of these systems, the members achieve some of the advantages of corporate integration while retaining some of the flexibility of a traditional channel system. In fact, the opportunities to reduce costs, and provide customers with superior value, are growing in these systems as new information technologies help channel partners share data to make products flow more efficiently through the channel.

An appliance producer may develop an informal arrangement with the independent wholesalers in its administered channel system. It agrees to keep production and inventory levels in the system balanced—using sales data from the wholesalers. Every week, its managers do a thorough analysis of up to 130,000 major appliances located in the many warehouses operated by its 87 wholesalers. Because of this analysis, both the producer and the wholesalers can be sure that they have enough inventory but not the expense of too much. And the producer has better information to plan its manufacturing and marketing efforts.

Middlemen in many industries—like groceries, drugs, hardware, and books—develop and coordinate similar systems. Computerized checkout systems track sales. The information is sent to the wholesaler's computer, which enters orders automatically when needed. Shipping cartons with computer-readable bar codes track the status of shipments and reduce errors. This reduces buying and selling costs, inventory investment, and customer frustration with out-of-stock items throughout the channel.

Vertical marketing systems—new wave in the marketplace

Smoothly operating channel systems are more efficient and successful. In the consumer products field, corporate chains that are at least partially vertically integrated account for about 25 percent of total retail sales. Other vertical systems account for an additional 37.5 percent. Thus, vertical systems in the consumer products area have a healthy majority of retail sales and should continue to increase their share in the future. Vertical marketing systems are becoming the major competitive units in the U.S. distribution system—and they are growing rapidly in other parts of the world as well.[18]

Short-term alliances are also popular

Firms that cooperate to build vertical marketing systems typically share a longer-term commitment. Sometimes, however, what a firm wants is a short-term collaboration to help it be more efficient in accomplishing a specific objective. This may lead to an alliance, a partnership (usually informal) among firms in which they agree to work together to achieve an objective. An alliance often involves two firms, but sometimes it involves a whole network of firms, who spin a web to catch more customers. The firms may be at the same level in the channel or at different levels. For example, a number of firms in the computer business have formed alliances to promote a market for the Linux operating system. Some of these firms produce hardware and some produce software, some focus on distribution, and some are even competitors (at least in some of their product-markets). Nevertheless, by forming a temporary alliance they increase their chances of reaching potential customers at the end of the channel. Without the alliance, it would be difficult for any one of these firms to compete with Microsoft or Intel.[19]

The Best Channel System Should Achieve Ideal Market Exposure

You may think that all marketing managers want their products to have maximum exposure to potential customers. This isn't true. Some product classes require much less market exposure than others. **Ideal market exposure** makes a product available widely enough to satisfy target customers' needs but not exceed them. Too much exposure only increases the total cost of marketing.

Ideal exposure may be intensive, selective, or exclusive

Intensive distribution is selling a product through all responsible and suitable wholesalers or retailers who will stock and/or sell the product. **Selective distribution** is selling through only those middlemen who will give the product special attention. **Exclusive distribution** is selling through only one middleman in a particular geographic area. As

As the percentage of people and firms adopting personal computers has increased, Microsoft has moved to more intensive distribution of its products worldwide.

we move from intensive to exclusive distribution, we give up exposure in return for some other advantage—including, but not limited to, lower cost.

In practice, this means that Wrigley's chewing gum is handled, through intensive distribution, by about a million U.S. outlets. Rolls Royces are handled, through exclusive distribution, by only a limited number of middlemen across the country.

Intensive distribution—sell it where they buy it

Intensive distribution is commonly needed for convenience products and business supplies—such as laser printer cartridges, ring binders, and copier paper—used by all offices. Customers want such products nearby.

The seller's intent is important here. Intensive distribution refers to the desire to sell through *all* responsible and suitable outlets. What this means depends on customer habits and preferences. If target customers normally buy a certain product at a certain type of outlet, ideally, you would specify this type of outlet in your Place policies. If customers preferred to buy Sharp portable TVs only at electronics stores, you would try to sell through all electronics stores to achieve intensive distribution. Today, however, many customers buy small portable TVs at a variety of convenient outlets—including Eckerd drugstores, a local Kmart, over the phone from the Sharper Image catalog, or perhaps from a website on the Internet. This means that an intensive distribution policy requires use of all these outlets, and more than one channel, to reach one target market.

Rayovac batteries were not selling well against Duracell and Energizer, even though the performance of the different batteries was very similar. Part of that may have been due to the heavier advertising for the Duracell and Energizer brands. But consumers usually don't go shopping for batteries—83 percent of the time they're purchased on impulse. So to get a larger share of the purchases, Rayovac had to be in more stores. It offered retailers a marketing mix with less advertising and a lower price. In a period of three years, the brand moved from being available in 36,000 stores to 82,000 stores—and that was enough to give sales a big charge.[20]

Selective distribution—sell it where it sells best

Selective distribution covers the broad area of market exposure between intensive and exclusive distribution. It may be suitable for all categories of products. Only the better middlemen are used here. Companies usually use selective distribution to gain some of the advantages of exclusive distribution—while still achieving fairly widespread market coverage.

Reduce costs and get better partners

A selective policy might be used to avoid selling to wholesalers or retailers who (1) place orders that are too small to justify making calls or providing service, (2) have a reputation for making too many returns or requesting too much service, (3) have a poor credit rating, or (4) are not in a position to do a satisfactory job.

Selective distribution is becoming more popular than intensive distribution as firms see that they don't need 100 percent coverage of a market to justify or support national advertising. Often the majority of sales come from relatively few customers—and the others buy too little compared to the cost of working with them; that is, they are unprofitable to serve. This is called the 80/20 rule—80 percent of a company's sales often come from only 20 percent of its customers *until it becomes more selective in choosing customers*.

Esprit—a producer of colorful, trendy clothing—was selling through about 4,000 department stores and specialty shops nationwide. But Esprit found that about half of the stores generated most of the sales. Sales analysis also showed that sales in Esprit's own stores were about 400 percent better than sales in other sales outlets. As a result, Esprit cut back to about 2,000 outlets and opened more of its own stores and a website—and profits increased.[21]

When producers use selective distribution, fewer sales contacts have to be made—and fewer wholesalers are needed. A producer may be able to contact selected retailers directly. Hanes sells men's underwear this way.

Get special effort from channel members

Selective distribution can produce greater profits not only for the producer but for all channel members—because of the closer cooperation among them. Wholesalers and retailers are more willing to promote products aggressively if they know they're going to obtain the majority of sales through their own efforts. They may carry more stock and wider lines, do more promotion, and provide more service—all of which lead to more sales.

Selective often moves to intensive as market grows

In the early part of the life cycle of a new unsought good, a producer's marketing manager may have to use selective distribution to encourage enough middlemen to handle the product. The manager wants to get the product out of the unsought category as soon as possible—but can't if it lacks distribution. Well-known middlemen may have the power to get such a product introduced but sometimes on their own terms—which often include limiting the number of competing wholesalers and retailers. The producer may be happy with such an arrangement at first but dislike it later when more retailers want to carry the product.

Exclusive distribution sometimes makes sense

Exclusive distribution is just an extreme case of selective distribution—the firm selects only one middleman in each geographic area. Besides the various advantages of selective distribution, producers may want to use exclusive distribution to help control prices and the service offered in a channel.

Retailers of shopping products and specialty products often try to get exclusive distribution rights in their territories. Fast-food franchises often have exclusive distribution—and that's one reason they're popular. Owners of McDonald's franchises pay a share of sales and follow McDonald's strategy to keep the exclusive right to a market.

Unlike selective distribution, exclusive distribution usually involves a verbal or written agreement stating that channel members will buy all or most of a given product from the seller. In return, these middlemen are granted the exclusive rights to that product in their territories. Some middlemen are so anxious to get a producer's exclusive franchise that they will do practically anything to satisfy the producer's demands.

When Honda introduced its Acura luxury car in the U.S., marketing managers decided to set up a completely new dealer system. In return for the right to sell the car, each new dealer agreed to focus exclusively on Acura and its target market. Acura also required its dealers to build expensive new showrooms. The cars sold well with this strategy, but after three years nearly half of Acura's dealers were still losing money or making only a small profit. Steady sales of a few models of just one make of car were not enough to offset the big investment in new facilities. To help its troubled dealers, Acura increased its advertising, developed new models, and worked with dealers to identify ways to earn more profit from service and used cars.[22]

Is limiting market exposure legal?

Exclusive distribution is a vague area under U.S. antimonopoly laws. Courts currently focus on whether an exclusive distribution arrangement hurts competition.

Horizontal arrangements among competitors are illegal

Horizontal arrangements—among *competing* retailers, wholesalers, or producers—to limit sales by customer or territory have consistently been ruled illegal by the U.S. Supreme Court. Courts consider such arrangements obvious collusion that reduces competition and harms customers.

Vertical arrangements may or may not be legal

The legality of vertical arrangements—between producers and middlemen—is not as clear-cut. A 1977 Supreme Court decision (involving Sylvania and the distribution of TV sets) reversed an earlier ruling that it was always illegal to set up vertical relationships limiting territories or customers. Now courts can weigh the possible good effects against the possible restrictions on competition. They look at competition between whole channels rather than just focusing on competition at one level of distribution.

With a very small share of the overall market for television sets, Sylvania couldn't compete on price with bigger producers who sold through self-service stores. So Sylvania decided to target customers who saw TVs as a heterogeneous shopping product. These people preferred stores that specialized in TVs, had a good selection on hand, and provided advice before the purchase and repair service afterward. Such retailers faced added costs to provide these services. They didn't want customers to inspect their TV sets, get information at their stores, and then be able to buy the same sets somewhere else at a lower price. In other words, they didn't want other retailers to get a free ride on their investment in inventory and higher-paid sales help. So Sylvania gave exclusive sales territories to dealers who cooperated with its full-service strategy. Even though this approach tends to reduce competition at the retail level, Sylvania argued that it needed such exclusive sales territories to compete with other producers. The Supreme Court basically agreed.

The Sylvania decision does not mean that all vertical arrangements are legal. Rather, it says that a firm has to be able to legally justify any exclusive arrangements.[23]

Caution is suggested

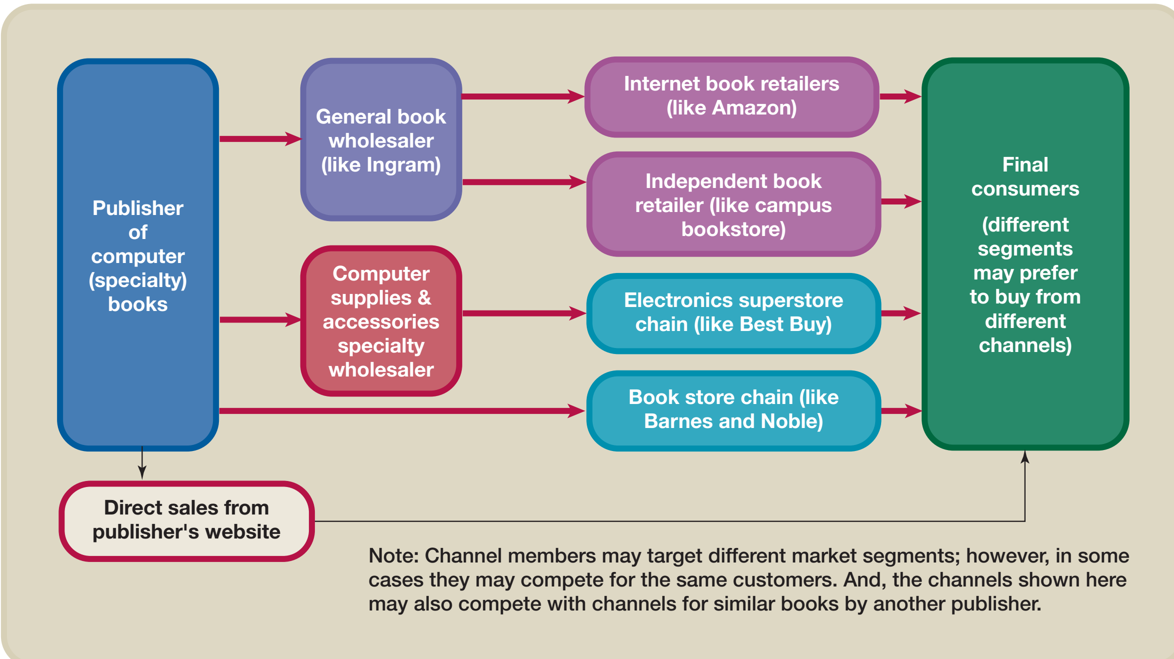
In spite of the 1977 Supreme Court ruling, firms should be extremely cautious about entering into *any* exclusive distribution arrangement. The antimonopoly rules still apply. The courts can force a change in relationships that were expensive to develop. And even worse, the courts can award triple damages if they rule that competition has been hurt.

The same cautions apply to selective distribution. Here, however, less formal arrangements are typical—and the possible impact on competition is more remote. It is now more acceptable to carefully select channel members when building a channel system. Refusing to sell to some middlemen, however, should be part of a logical plan with long-term benefits to consumers.

Channel Systems Can Be Complex

Trying to achieve the desired degree of market exposure can lead to complex channels of distribution. Firms may need different channels to reach different segments of a broad product-market or to be sure they reach each segment. Sometimes this results in competition between different channels.

Exhibit 11-4 An Example of Dual Distribution by a Publisher of Computer Books

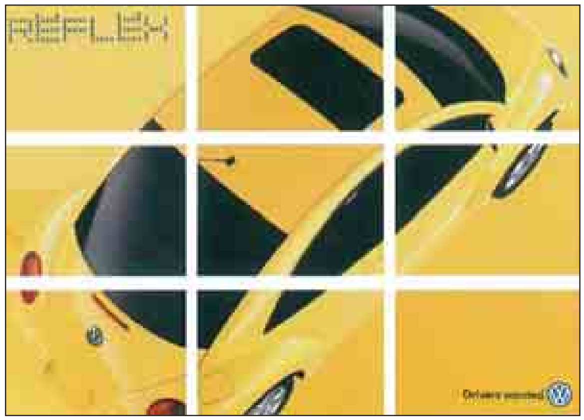


Consider the different channels used by a company that publishes computer books. See Exhibit 11-4. This publisher sells through a general book wholesaler who in turn sells to Internet book retailers and independent book retailers. The publisher may have some direct sales of its best-selling books to a large chain or even to consumers who order directly from its website. However, it might also sell through a computer supplies wholesaler that serves electronics superstores like Best Buy. This can cause problems because different wholesalers and retailers want different markups. It also increases competition, including price competition. And the competition among different middlemen may result in conflicts between the middlemen and the publisher.

Dual distribution systems may be needed

Dual distribution occurs when a producer uses several competing channels to reach the same target market—perhaps using several middlemen in addition to selling directly. Dual distribution is becoming more common. Big retail chains want to deal directly with producers. They want large quantities and low prices. The producer sells directly to retail chains and relies on wholesalers to sell to smaller accounts. Some established middlemen resent this because they don't appreciate *any* competition—especially price competition set up by their own suppliers.

Other times, producers are forced to use dual distribution because their present channels are doing a poor job or aren't reaching some potential customers. For example, Reebok International had been relying on local sporting goods stores to sell its shoes to high school and college athletic teams. But Reebok wasn't getting much of the business. When it set up its own team-sales department to sell directly to the schools, it got a 30,000-unit increase in sales. Of course, some of the stores weren't happy about their supplier also selling to their potential customers. However, they did get the message that Reebok wanted someone to reach that target market.[24]



Some special models of the Beetle could only be ordered online direct from VW's website. However, the customer was then directed to a VW dealer who completed the transaction—an arrangement that avoids conflict between VW and its dealers.

Ethical decisions may be required

A shared product-market commitment guides cooperative relationships among channel members as long as the channel system is competitive. However, if customers' Place requirements change, the current channel system may not be effective. The changes required to serve customer needs may hurt one or more members of the channel. The most difficult ethical dilemmas in the channels area arise in situations like this—because not everyone can win.

For example, wholesalers and the independent retailers that they serve in a channel of distribution may trust a producer channel-captain to develop marketing strategies that will work for the whole channel. However, the producer may conclude that everyone in the channel will ultimately fail if it continues exclusive distribution. It might decide that consumers, and its own business, are best served by a change (say, dropping current middlemen and selling directly to big retail chains). A move of this sort, if implemented immediately, may not give current middlemen-partners a chance to make adjustments of their own. The more dependent they are on the producer, the more severe the impact is likely to be. It's not easy to determine the best or most ethical solution in these situations. However, marketing managers must think carefully about the implications of strategy changes in the Place area—because they can have very severe consequences for other channel members. In channels, as in any business dealing, relationships of trust must be treated with care.[25]

Internet

Internet Exercise Avon sells cosmetics and other products through independent sales representatives (agents), in kiosks and stores, and also through a catalog (both online and printed). Review the Avon website (www.avon.com). Do you think that Avon's independent sales representatives would view the website as competing for their customers' purchases and a source of conflict, or would they think that it helps them promote the product and identify new prospects? Explain your thinking.

Reverse channels should be planned

Most firms focus on getting products to their customers. But some marketing managers must also plan for **reverse channels**—channels used to retrieve products that customers no longer want. The need for reverse channels may arise in a variety of different situations. Toy companies, automobile firms, drug companies, and others sometimes have to recall products because of safety problems. A producer that makes an error in completing an order may have to take returns from middlemen or other business customers. If a Viewsonic computer monitor breaks while it's still under warranty, someone needs to get it to the authorized repair center. Soft-drink companies may need to recycle empty bottles. And of course, at some point or other, most consumers buy something in error and want to return it. For example, this is quite common with online purchases where consumers can't see, touch, or try the actual product before purchasing it.[26]

Another problem arises from products that are damaged in shipping or discontinued. Most manufacturers take them back. For example, until recently P&G had a reclamation center that took back thousands of products, ranging from damaged boxes of Tide to leaking bottles of Crisco Oil. A grocery products trade group says that the cost of such unsalable products, in total, may be as much as $4 billion a year. This has prompted P&G to change its policies. Now, P&G has adopted a no-returns policy and instead gives retailers a payment for damaged items. The system is designed to reduce the cost of returns to both P&G and retailers. Ultimately, that cost must be paid by consumers. Some retailers don't like P&G's policy, but it is important to see that it is a specific plan and part of an overall strategy.

When marketing managers don't plan for reverse channels, the firm's customers may be left to solve "their" problem. That usually doesn't make sense. So a complete plan for Place may need to consider an efficient way to return products—with policies that different channel members agree on. It may also require specialists who were not involved in getting the product to the consumer. But if that's what it takes to satisfy customers, it should be part of marketing strategy planning.[27]

Conclusion

In this chapter, we discussed the role of Place and noted that Place decisions are especially important because they may be difficult and expensive to change.

Marketing specialists, and channel systems, develop to adjust discrepancies of quantity and assortment. Their regrouping activities are basic in any economic system. And adjusting discrepancies provides opportunities for creative marketers.

Channel planning requires firms to decide on the degree of market exposure they want. The ideal level of exposure may be intensive, selective, or exclusive. They also need to consider the legality of limiting market exposure to avoid having to undo an expensively developed channel system or face steep fines.

The importance of planning channel systems was discussed—along with the role of a channel captain. We stressed that channel systems compete with each other and that vertical marketing systems seem to be winning.

In this broader context, the "battle of the brands" is only a skirmish in the battle between various channel systems. And we emphasized that producers aren't necessarily the channel captains. Often middlemen control or even dominate channels of distribution.

Questions and Problems

1. Review the case at the beginning of the chapter and explain why Amazon.com would use a wholesaler like Ingram.
2. Give two examples of service firms that work with other channel specialists to sell their products to final consumers. What marketing functions is the specialist providing in each case?
3. Discuss some reasons why a firm that produces installations might use direct distribution in its domestic market but use middlemen to reach overseas customers.
4. Explain discrepancies of quantity and assortment using the clothing business as an example. How does the application of these concepts change when selling steel to the automobile industry? What impact does this have on the number and kinds of marketing specialists required?
5. Explain the four regrouping activities with an example from the building supply industry (nails, paint, flooring, plumbing fixtures, etc.). Do you think that many specialists develop in this industry, or do

producers handle the job themselves? What kinds of marketing channels would you expect to find in this industry, and what functions would various channel members provide?

6. Insurance agents are middlemen who help other members of the channel by providing information and handling the selling function. Does it make sense for an insurance agent to specialize and work exclusively with one insurance provider? Why or why not?
7. Discuss the Place objectives and distribution arrangements that are appropriate for the following products (indicate any special assumptions you have to make to obtain an answer):
   a. A postal scale for products weighing up to 2 pounds.
   b. Children's toys: (1) radio-controlled model airplanes costing $80 or more, (2) small rubber balls.
   c. Heavy-duty, rechargeable, battery-powered nut tighteners for factory production lines.
   d. Fiberglass fabric used in making roofing shingles.
8. Give an example of a producer that uses two or more different channels of distribution. Briefly discuss what problems this might cause.
9. Explain how a channel captain can help traditional independent firms compete with a corporate (integrated) channel system.
10. Find an example of vertical integration within your city. Are there any particular advantages to this vertical integration? If so, what are they? If there are no such advantages, how do you explain the integration?
11. What would happen if retailer-organized channels (either formally integrated or administered) dominated consumer product marketing?
12. How does the nature of the product relate to the degree of market exposure desired?
13. Why would middlemen want to be exclusive distributors for a product? Why would producers want exclusive distribution? Would middlemen be equally anxious to get exclusive distribution for any type of product? Why or why not? Explain with reference to the following products: candy bars, batteries, golf clubs, golf balls, steak knives, televisions, and industrial woodworking machinery.
14. Explain the present legal status of exclusive distribution. Describe a situation where exclusive distribution is almost sure to be legal. Describe the nature and size of competitors and the industry, as well as the nature of the exclusive arrangement. Would this exclusive arrangement be of any value to the producer or middleman?
15. Discuss the promotion a new grocery products producer would need in order to develop appropriate channels and move products through those channels. Would the nature of this job change for a new producer of dresses? How about for a new, small producer of installations?

Suggested Cases

13. Paper Supplies Corporation
15. Modern Horizons, Inc.
16. Morgan Company
34. Aluminum Basics Co.

Computer-Aided Problem

11. **Intensive versus Selective Distribution**

Hydropump, Inc., produces and sells high-quality pumps to business customers. Its marketing research shows a growing market for a similar type of pump aimed at final consumers—for use with Jacuzzi-style tubs in home remodeling jobs. Hydropump will have to develop new channels of distribution to reach this target market because most consumers rely on a retailer for advice about the combination of tub, pump, heater, and related plumbing fixtures they need. Hydropump's marketing manager, Robert Black, is trying to decide between intensive and selective distribution. With intensive distribution, he would try to sell through all the plumbing supply, bathroom fixture, and hot-tub retailers who will carry the pump. He estimates that about 5,600 suitable retailers would be willing to carry a new pump. With selective distribution, he would focus on about 280 of the best hot-tub dealers (2 or 3 in the 100 largest metropolitan areas).

Intensive distribution would require Hydropump to do more mass selling—primarily advertising in home renovation magazines—to help stimulate consumer familiarity with the brand and convince retailers that Hydropump equipment will sell. The price to the retailer might have to be lower too (to permit a bigger markup) so they will be motivated to sell Hydropump rather than some other brand offering a smaller markup.

With intensive distribution, each Hydropump sales rep could probably handle about 300 retailers effectively. With selective distribution, each sales rep could handle only about 70 retailers because more merchandising help would be necessary. Managing the smaller sales force and fewer retailers, with the selective approach, would require less manager overhead cost.

Going to all suitable and available retailers would make the pump available through about 20 times as many retailers and have the potential of reaching more customers. However, many customers shop at more than one retailer before making a final choice—so selective distribution would reach almost as many potential customers. Further, if Hydropump is using selective distribution, it would get more in-store sales attention for its pump and a larger share of pump purchases at each retailer.

Black has decided to use a spreadsheet to analyze the benefits and costs of intensive versus selective distribution.

a. *Based on the initial spreadsheet, which approach seems to be the most sensible for Hydropump? Why?*
b. *A consultant points out that even selective distribution needs national promotion. If Black has to increase advertising and spend a total of $100,000 on mass selling to be able to recruit the retailers he wants for selective distribution, would selective or intensive distribution be more profitable?*
c. *With intensive distribution, how large a share (percent) of the retailers' total unit sales would Hydropump have to capture to sell enough pumps to earn $200,000 profit?*

For additional questions related to this problem, see Exercise 11-3 in the *Learning Aid for Use with Basic Marketing*, 14th edition.

When You Finish This Chapter, You Should

1. Understand why logistics (physical distribution) is such an important part of Place *and* marketing strategy planning.

2. Understand why the physical distribution customer service level is a key marketing strategy variable.

3. Understand the physical distribution concept and why it requires coordination of storing, transporting, and related activities.

4. See how firms can cooperate and share logistics activities to improve value to the customer at the end of the channel.

5. Know about the advantages and disadvantages of the various transporting methods.

6. Know how inventory decisions and storing affect marketing strategy.

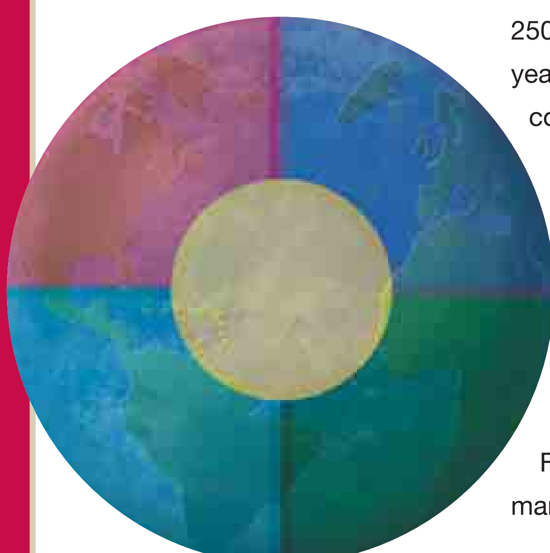
7. Understand the distribution center concept.

8. Understand the important new terms (shown in red).

Chapter Twelve

Distribution Customer Service and Logistics

If you want a Coca-Cola, there's usually one close by—no matter where you might be in the world. And that's no accident. An executive for the best-known brand name in the world stated the objective simply: "Make Coca-Cola available within an arm's reach of desire." To achieve that objective, Coke works with many different channels of distribution. But that's just the start. Think about what it takes for a bottle, can, or cup of Coke to be there whenever you're ready. In warehouses and distribution centers, on trucks, in gyms and sports arenas, and thousands of other retail outlets, Coke handles, stores, and transports over 250 billion servings of soft drink a year. Getting all of that product to consumers could be a logistical nightmare, but Coke does it effectively and at a low cost. Think about it: A can of Coke at the store costs only about 15 cents more that it costs you to have the post office deliver a letter.



Fast information about what the market needs helps keep Coke's

place price promotion produc

distribution on target. In the United States, computer systems show Coke managers exactly what's selling in each market; that allows Coke to plan inventories and deliveries. Coke also operates a 24-hour-a-day communications center to respond to the two million requests it gets from channel members each year. Orders are processed instantly—so sales to consumers at the end of the channel aren't lost because of stock-outs. And Coke products move efficiently through the channel. In Cincinnati, for example, Coke built the beverage industry's first fully automated distribution center. Forklifts were replaced with automatically guided vehicles that speed up the product flow and reduce labor costs.

Coke's strategies in international markets rely on many of the same ideas. But the stage of market development varies in different countries, so Coke's emphasis varies as well. To increase sales in France, for example, Coke must first make more product available at retail stores; so Coke is installing thousands of soft-drink coolers in French supermarkets. In Great Britain, Coke is using multipacks because it wants to have more inventory at the point of consumption—in consumers' homes. In Japan, by contrast, single-unit vending machine sales are very important—so Coke uses an army of truck drivers to constantly restock its 870,000 vending machines, more per capita than anywhere else in the world. Coke is even testing vending machines that raise the price when it's hot or when few cans are left. In less-developed areas, the Place system is not always so sophisticated. In China, for example, the Communist Party won't let Coke control all of the details, but a local manager struck a deal. For some cash, the Communist Party keeps inventories in some of its local offices. Then retired party members use bicycle-powered pushcarts to sell the Coke inventory at densely populated housing projects.

place price promotion product

Coke is also working to increase fountain-drink sales in domestic and international markets. As part of that effort, Coke equips restaurants and food outlets with Coke dispensers. Once a Coke dispenser is installed, the retailer usually doesn't have room for a competitor's dispenser. And when a consumer wants a fountain drink, Coke isn't just "the real thing," it's the only thing. The number of fountain outlets has grown so rapidly that one Coke account rep serves as many as a 1,000 customers in a geographic area. That means that the little guys could get lost in the shuffle. However, to give them the service they need at a reasonable cost, Coke recently initiated Coke.net, a password-protected Web portal where fountain customers can access account managers online, track syrup orders, request equipment repairs, or download marketing support materials.

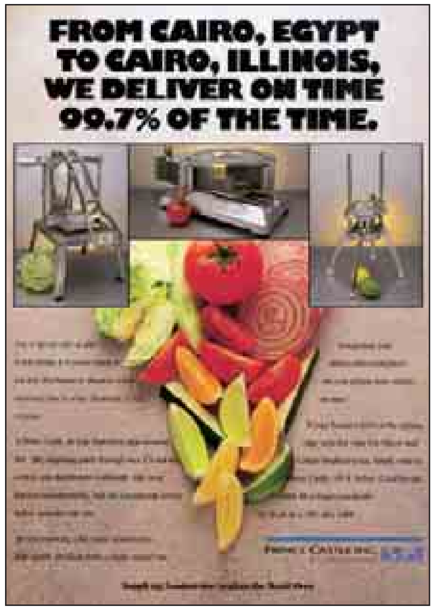
Of course, Pepsi is a tough competitor and isn't taking all of this sitting down. In recent years it has added more non-cola products, and its edgy ads for Mountain Dew and other products are helping it gain market share—which means it gets more shelf space and more Pepsi stocked at the point of purchase. Coke is pushing on new fronts as well. So the competition is becoming even more intense. It's not just the "Cola Wars" any more but rather the wars for cola, juice, water, sports drinks, tea, and many other beverages. And who wins customers and profits in this broader competition will depend on overall marketing programs—but clearly Place has an important role to play.[1]

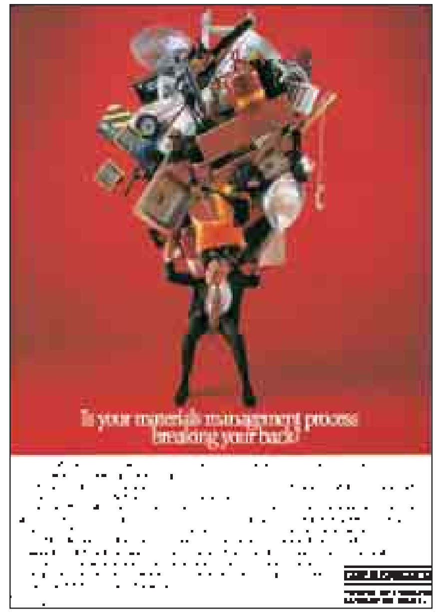
Physical Distribution Gets It to Customers

Choosing the right channel of distribution is crucial in getting products to the target market's Place. But as the Coke case shows, that alone is usually not enough to ensure that products are available at the right time and in the right quantities. Whenever the product includes a physical good, Place requires logistics decisions. **Logistics** is the transporting, storing, and handling of goods to match target customers' needs with a firm's marketing mix—both within individual firms and along a channel of distribution. **Physical distribution (PD)** is another common name for logistics.

PD provides time and place utility and makes possession utility possible. A marketing manager may have to make many decisions to ensure that the physical distribution system provides utility and meets customers' needs with an acceptable service level and cost.

Logistics costs are very important to both firms and consumers. These costs vary from firm to firm and, from a macro-marketing perspective, from country to country. However, for many physical goods, firms spend half or more of their total marketing dollars on physical distribution activities. The total amount of money involved is so large that even small improvements in this area can have a big effect on a whole macro-marketing system and consumers' quality of life. For example, during the past decade many supermarket chains and producers that supply them collaborated to create a system called Efficient Consumer Response (ECR) that cut grocers' costs, and prices, by about 11 percent. That translates to savings of about $30 *billion* a year for U.S. consumers! The basic idea of ECR involves paperless, The physical distribution customer service level—including fast and reliable delivery of whatever assortment is needed—is critical to many business customers.





computerized links between grocers and their suppliers, which leads to more effective merchandise assortments and continuous replenishment of shelves based on what actually sells each day. Although the ECR movement started in the U.S. and Canada, it quickly spread across Europe and in other regions. Now, 50 consumer packaged goods companies have banned together to create Transora, a Web portal (www.transora.com), to bring more e-commerce benefits to the ECR concept. Obviously, far-reaching innovations like these don't transform everything overnight, but you can see that more effective approaches in the distribution area have the potential to save firms, and their customers, massive amounts of money.[2]

Physical Distribution Customer Service

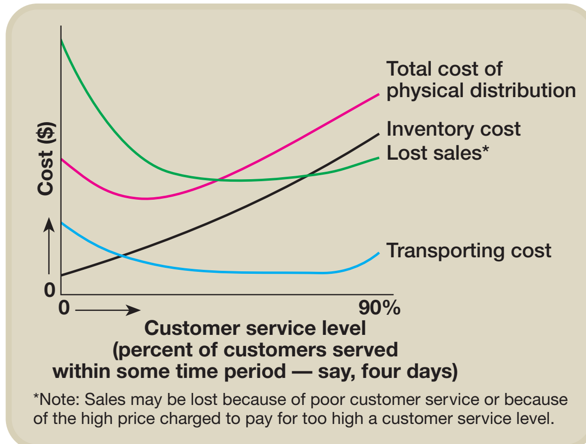
From the beginning, we've emphasized that marketing strategy planning is based on meeting customers' needs. Planning for logistics and Place is no exception. So let's start by looking at logistics through a customer's eyes.

Customers want products, not excuses

Customers don't care how a product was moved or stored or what some channel member had to do to provide it. Rather, customers think in terms of the physical distribution **customer service level**—how rapidly and dependably a firm can deliver what they, the customers, want. Marketing managers need to understand the customer's point of view.

What does this really mean? It means that Toyota wants to have enough windshields delivered to make cars *that* day—not late so production stops *or* early so there are a lot of extras to move around or store. In turn, it means that the Toyota dealer wants the car when it's due so that salespeople are not left making lame excuses to the customer who ordered it. It means that business executives who rent cars from Hertz want them to be ready when they get off their planes. It means that when you order a blue shirt at the Lands' End website you receive blue,

Exhibit 12-1
Trade-Offs among Physical Distribution Costs, Customer Service Level, and Sales



not pink. It means you want your Lay's Baked Potato Chips to be whole when you buy a bag at the snack bar—not crushed into crumbs from rough handling in a warehouse.

Physical distribution is invisible to most consumers

PD is, and should be, a part of marketing that is "invisible" to most consumers. It only gets their attention when something goes wrong. At that point, it may be too late to do anything that will keep them happy.

In countries where physical distribution systems are inefficient, consumers face shortages and inconvenient waits for the products they need. By contrast, most consumers in the United States and Canada don't think much about physical distribution. This probably means that these market-directed macro-marketing systems work pretty well—that a lot of individual marketing managers have made good decisions in this area. But it doesn't mean that the decisions are always clear-cut or simple. In fact, many trade-offs may be required.

Trade-offs of costs, service, and sales

Most customers would prefer very good service at a very low price. But that combination is hard to provide because it usually costs more to provide higher levels of service. So most physical distribution decisions involve trade-offs between costs, the customer service level, and sales.

If you want a new Compaq computer and the Best Buy store where you would like to buy it doesn't have it on hand, you're likely to buy it elsewhere; or if that model Compaq is hard to get you might just switch to some other brand. Perhaps the Best Buy store could keep your business by guaranteeing two-day delivery of your computer—by using airfreight from Compaq's factory. In this case, the manager is trading the cost of storing inventory for the extra cost of speedy delivery—assuming that the computer is available in inventory *somewhere* in the channel. In this example, missing one sale may not seem that important, but it all adds up. In fact, using Compaq Computer to illustrate this point is quite purposeful. A few years ago Compaq lost over $500 million in sales because its computers weren't available when and where customers were ready to buy them. With that kind of lesson in lost sales, you can see why Compaq worked hard to improve on the trade-off it was making.

Exhibit 12-1 illustrates trade-off relationships like those highlighted in the Compaq example. For example, faster but more expensive transportation may reduce the need for a costly inventory of computers. There is also a trade-off between the service level and sales. If the service level is too low—if products are not available on a timely and dependable basis—customers will buy elsewhere, and sales will be lost. Alternatively, the supplier may hope that a higher service level will attract more customers or motivate them to pay a higher price. But if the service level is higher than customers want or are willing to pay for, sales will be lost to competitors who have figured out what kind of service customers value.

The important point is that many trade-offs must be made in the PD area. The trade-offs can be complicated. The lowest-cost approach may not be best—if customers aren't satisfied. A higher service level may make a better strategy. Further, if different channel members or target markets want different customer service levels, several different strategies may be needed.[3]

Many firms are trying to address these complications with e-commerce. Information technology can improve service levels and cut costs at the same time. As you'll see, better information flows make it easier to coordinate the different activities and cut inefficiency that doesn't add value for the customer.

Physical Distribution Concept Focuses on the Whole Distribution System

The physical distribution concept

The **physical distribution (PD) concept** says that all transporting, storing, and product-handling activities of a business and a whole channel system should be coordinated as one system that seeks to minimize the cost of distribution for a given customer service level. Both lower costs and better service help to increase customer value. It may be hard to see this as a startling development. But until just a few years ago, even the most progressive companies treated physical distribution functions as separate and unrelated activities.

Within a firm, responsibility for different distribution activities was spread among various departments—production, shipping, sales, warehousing, and others. No one person was responsible for coordinating storing and shipping decisions or seeing how they related to customer service levels. Some firms even failed to calculate the costs for these activities, so they never knew the total cost of physical distribution. If it was unusual for distribution to be coordinated within a firm, it was even rarer for different firms in the channel to collaborate. Each just did its own thing.[4]

Unfortunately, in too many firms old-fashioned ways persist—with a focus on individual functional activities rather than the whole physical distribution system. Trying to reduce the cost of individual functional activities may actually increase total distribution costs—not only for the firm, but also for the whole channel. It may also lead to the wrong customer service level. Well-run firms now avoid these problems by paying attention to the physical distribution concept.

Decide what service level to offer

With the physical distribution concept, firms work together to decide what aspects of service are most important to customers at the end of the channel and what specific service level to provide. Then they focus on finding the least expensive way to achieve the target level of service.

Exhibit 12-2 shows a variety of factors that may influence the customer service level (at each level in the channel). The most important aspects of customer service depend on target market needs. Xerox might focus on how long it takes to deliver copy machine repair parts once it receives an order. When a copier breaks down, customers want the repair "yesterday." The service level might be stated as

Exhibit 12-2
Examples of Factors that Affect PD Service Levels

- Advance information on product availability
- Time to enter and process orders
- Backorder procedures
- Where inventory is stored
- Accuracy in filling orders
- Damage in shipping, storing, and handing
- Online status information
- Advance information on delays
- Time needed to deliver an order
- Reliability in meeting delivery date
- Complying with customer's instructions
- Defect-free deliveries
- How needed adjustments are handled
- Procedures for handling returns

"we will deliver 90 percent of all emergency repair parts within 8 business hours and the remainder within 24 hours." Such a service level might require that almost all such parts be kept in inventory, that the most commonly needed parts be available on the service truck, that order processing be very fast and accurate, and that parts not available locally be sent by airfreight. If Xerox doesn't make the part, it would need to be sent directly from Xerox's supplier. Obviously, supplying this service level will affect the total cost of the PD system. But it may also beat competitors who don't provide this service level.

Increasing service levels may be very profitable in highly competitive situations where the firm has little else to differentiate its marketing mix. Marketing managers at Clorox, for example, must do everything they can to develop and keep strong partnerships with Clorox middlemen (supermarket chains, convenience stores, mass merchandisers, warehouse clubs, and wholesalers) and other business customers (ranging from white-tablecloth restaurants to the fast-service chains). Many other firms sell products with precisely the same ingredients as Clorox and are constantly trying to get orders from Clorox's 100,000 business customers worldwide. Yet Clorox's objective is to "maintain the highest standards for customer service" in the product-markets it serves because that helps it obtain a competitive advantage. For example, when the bleach buyer for a major retail chain went on vacation, the fill-in person was not familiar with the computerized reorder procedures. As a result, the chain's central distribution center almost ran out of Clorox liquid bleach. But Clorox's distribution people identified the problem themselves—because of a computer system that allowed Clorox to access the chain's inventory records and sales data for Clorox products. Clorox rearranged production to get a shipment out fast enough to prevent the chain, and Clorox, from losing sales at individual stores. In the future when some other bleach supplier tries to tell buyers for the chain that "bleach is bleach," they'll remember the distribution service Clorox provides.[5]

Find the lowest total cost for the right service level

In selecting a PD system, the **total cost approach** involves evaluating each possible PD system and identifying *all* of the costs of each alternative. This approach uses the tools of cost accounting and economics. Costs that otherwise might be ignored—like inventory carrying costs—are considered. The possible costs of lost sales due to a lower customer service level may also be considered. The following simple example clarifies why the total cost approach is important.

A cost comparison of alternative systems

The Good Earth Vegetable Company was shipping produce to distant markets by train. The cost of shipping a ton of vegetables by train averaged less than half the cost of airfreight so the company assumed that rail was the best method. But then Good Earth managers did a more complete analysis. To their surprise, they found the airfreight system was faster and cheaper.

Exhibit 12-3 compares the costs for the two distribution systems—airplane and railroad. Because shipping by train was slow, Good Earth had to keep a large

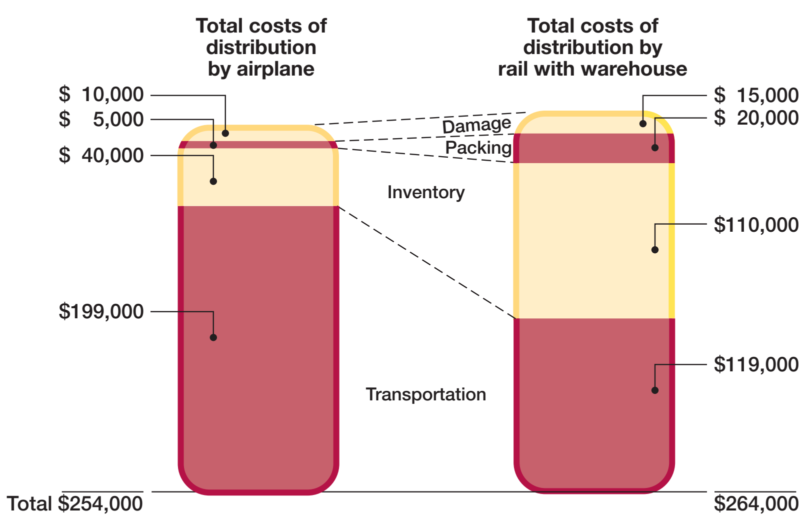
Both Business Objects and Sauder try to help customer firms do a better job of tracking the status of orders and making certain that products are where they are needed at the right time.

inventory in a warehouse to fill orders on time. And the company was also surprised at the extra cost of carrying the inventory in transit. Good Earth's managers also found that the cost of spoiled vegetables during shipment and storage in the warehouse was much higher when they used rail shipping.

In this case, total cost analyses showed that airfreight, while more costly by itself, provided better service than the conventional means—and at a lower total distribution cost. The case also illustrates why it is important to get beyond a focus on individual functional elements of PD and instead consider the costs and service level of a whole system. This broader focus should consider how the whole channel operates, not just individual firms.

Many firms are now applying this type of thinking to improve value to customers and profits. For example, after two years of work with the total cost approach,

Exhibit 12-3
Comparative Costs of Airplane versus Rail and Warehouse



National Semiconductor cut its standard delivery time in half, reduced distribution costs 2.5 percent, and increased sales by 34 percent. In the process it shut down six warehouses around the globe and started to airfreight microchips to its worldwide customers from a new 125,000-square-foot distribution center in Singapore. In advance of these changes, no one would have said that this was an obvious thing to do. But it proved to be the smart thing.

Identifying all the alternatives is sometimes difficult

It's important for firms to compare the costs and benefits of all practical PD alternatives, including how functions can be shared in the channel. Sometimes, however, there are so many possible combinations that it is difficult to study each one completely. For example, there may be hundreds of possible locations for a warehouse. And each location might require different combinations of transporting, storing, and handling costs. Some companies use computer simulation to compare the many possible alternatives. But typically, the straightforward total cost analysis discussed above is practical and will show whether there is need for a more sophisticated analytical approach.[6]

Coordinating Logistics Activities among Firms

Functions can be shifted and shared in the channel

As a marketing manager develops the Place part of a strategy, it is important to decide how physical distribution functions can and should be divided within the channel. Who will store, handle, and transport the goods—and who will pay for these services? Who will coordinate all of the PD activities?

There is no right sharing arrangement. Physical distribution can be varied endlessly in a marketing mix and in a channel system. And competitors may share these functions in different ways—with different costs and results.

How PD is shared affects the rest of a strategy

How the PD functions are shared affects the other three Ps—especially Price. The sharing arrangement can also make (or break) a strategy. Consider Channel Master, a firm that wanted to take advantage of the growing market for the dish-like antennas used to receive TV signals from satellites. The product looked like it could be a big success, but the small company didn't have the money to invest in a large inventory. So Channel Master decided to work only with wholesalers who were willing to buy (and pay for) several units—to be used for demonstrations and to ensure that buyers got immediate delivery.

In the first few months Channel Master earned $2 million in revenues—just by providing inventory for the channel. And the wholesalers paid the interest cost of carrying inventory—over $300,000 the first year. Here the wholesalers helped share the risk of the new venture—but it was a good decision for them too. They won many sales from a competing channel whose customers had to wait several months for delivery. And by getting off to a strong start, Channel Master became a market leader.

A coordinated effort reduces conflict

PD decisions interact with other Place decisions, the rest of the marketing mix, and the whole marketing strategy. As a result, if firms in the channel do not plan and coordinate how they will share PD activities, PD is likely to be a source of conflict rather than a basis for competitive advantage. Holly Farms' problems in introducing a new product illustrate this point.

Marketers at Holly Farms were encouraged when preroasted chicken performed well in a market test. But channel conflict surfaced when they moved to broader distribution. As with other perishable food products, the Holly Farm label indicated a date by which the chicken should be sold. Many grocers refused to buy the roast chicken because they worried that they had only a few days after it was delivered to sell it. They didn't want it to spoil—at their expense—on the shelf. They also didn't want to sell their customers something that wasn't fresh.

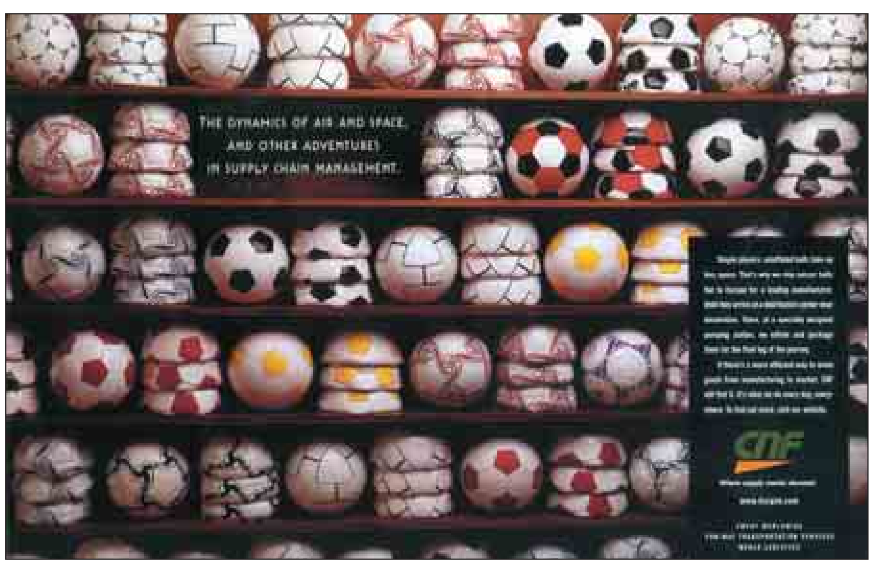
Shelf life had not been a problem with Holly Farms' raw chicken. It sold in higher volume and moved off shelves more quickly. The source of the problem with the roast chicken was that it took too long to ship from the plant to distant stores. Coupled with slow turnover, that didn't leave grocers enough selling time. To address the problem, Holly Farms changed its transportation arrangements. It also developed new packaging that allowed grocers to store the chicken longer. Holly Farms also shifted its promotion budget to put more emphasis on in-store promotions to speed up sales once the chicken arrived. With these changes, Holly Farms was able to win cooperation in the channel and establish its product in the market.[7]

JIT requires a close, cooperative relationship

We introduced the concept of just-in-time (JIT) delivery in Chapter 7. Now that you know more about PD alternatives, it's useful to consider some of the marketing strategy implications of this approach.

A key advantage of JIT for business customers is that it reduces their PD costs—especially storing and handling costs. However, if the customer doesn't have any backup inventory, there's no security blanket if something goes wrong. If a supplier's delivery truck gets stuck in traffic, if there's an error in what's shipped, or if there are any quality problems when the products arrive, the customer's business stops. Thus, a JIT system requires that a supplier have extremely high quality control in production and in every PD activity, including its PD service.

For example, to control the risk of transportation problems, JIT suppliers often locate their facilities close to important customers. Trucks may make smaller and more frequent deliveries—perhaps even several times a day. As this suggests, a JIT system usually requires a supplier to be able to respond to very short order lead times. In fact, a supplier's production often needs to be based on the customer's production schedule. Thus, e-commerce order systems and information sharing over computer networks are often required. However, if that isn't possible, the supplier must have adequate inventory to meet the customer's needs. Moreover, the supplier in turn may need better service from firms that it relies on, say, for raw materials or supplies.



To help a manufacturer of soccer balls reduce its logistics costs, CNF ships the balls to Europe uninflated and then pumps them up before the last leg of their journey to individual outlets.

You can see that the JIT system shifts greater responsibility for PD activities backward in the channel. If the supplier can be more efficient than the customer could be in controlling PD costs—and still provide the customer with the service level required—this approach can work well for everyone in the channel. However, it should be clear that JIT is not always the lowest-cost or best approach. It may be better for a supplier to produce and ship in larger, more economical quantities—if the savings offset the distribution system's total inventory and handling costs.

While not every firm can, or should, use a just-in-time approach, it is an important idea. It focuses attention on the need to coordinate the PD system throughout the channel. It also highlights the value of close working relationships and effective communication between marketers and their customers. Whether or not a firm uses the JIT approach, good information (and technology to share it quickly) is often the key to coordinating PD activities and improving the customer service level.[8]

Chain of supply may involve even more firms

In our discussion, we have taken the point of view of a marketing manager. This focuses on how logistics should be coordinated to meet the needs of customers at the end of the channel of distribution. Now, however, we should broaden the picture somewhat because the relationships within the distribution channel are sometimes part of a broader network of relationships in the **chain of supply**—the complete set of firms and facilities and logistics activities that are involved in procuring materials, transforming them into intermediate or finished products, and distributing them to customers. For example, Toyota not only works with dealers and customers further down its channel of distribution but also is coordinating with all of the supplier firms from which it buys parts, supplies, and raw materials. Those firms, in turn, are linked to other suppliers who come earlier in the chain of supply. What happens at each link along the chain can impact coordination further down the chain. If the firm that produces seats for Toyota doesn't get the fabric from its supplier on time, the seats will be delayed in route to Toyota and the car will be slow getting to the dealer and consumer.

Ideally, all of the firms in the chain of supply should work together to meet the needs of the customer at the very end of the chain. That way, at each link along the chain the shifting and sharing of logistics functions and costs are handled to result in maximum value for the final customer. Further, all of the firms in the whole chain of supply are able to do a better job of competing against competitors who are involved in other chains of supply.

The practical reality is that coordination across the whole chain of supply doesn't always happen. The customer service level that a marketing manager needs to compete may not be possible if firms earlier in the chain of supply can't or won't do what is needed. In these situations the purchasing and manufacturing departments can't be expected to do the impossible. Resolving this sort of problem requires strategic decisions by the firm's top management. For example, the CEO might decide that the firm needs to invest in costly new computer networks and software that will provide e-commerce order systems that also give suppliers information they need.

The challenges of coordinating logistics functions across the complete chain of supply have prompted some firms to put a high-level executive in charge of chain of supply decisions. This person works with people in marketing, procurement, manufacturing, and other areas to find the best ways to address problems that arise. Yet, it's still difficult for a manager in any one company to know what kind of logistics sharing arrangement will work best, or even be possible, in a whole series of other companies. Because of that, many firms turn to outside experts for help. For example, specialists have developed to design e-commerce computer systems that link all of the firms in a chain of supply. Similarly, there are consultants who use computer models to figure out the best locations for inventory or the best way to shift logistics functions among firms. In other cases, firms sometimes outsource the whole job of planning *and* implementing their logistics systems.[9]

Internet

Internet Exercise Large corporations often turn to other firms that specialize in logistics—transportation and warehousing services, consultants, developers of software for e-commerce, and the like—to help implement the physical distribution aspects of their marketing strategies. The website of the Virtual Logistics Directory (www.logisticdirectory.com) lists many logistics specialists and what they do. Go to the website and select the *Integrated Logistics* category. Review the descriptions of some of the firms listed, and then pick one. Explain why a large corporation with a logistics problem might seek its help rather than just trying to tackle the problem internally.

Better information helps coordinate PD

Coordinating all of the elements of PD has always been a challenge—even in a single firm. Trying to coordinate PD throughout the whole supply chain is even tougher. Keeping track of inventory levels, when to order, and where goods are when they move is complicated. The Internet is becoming more and more important in finding solutions to these challenges.

Many firms now continuously update their marketing information systems—so they can immediately find out what products have sold, the level of the current inventory, and when goods being transported will arrive. And coordination of physical distribution decisions throughout channels of distribution continues to improve as more firms are able to have their computers "talk to each other" directly and as managers can get information from a website whenever they need it.

Electronic data interchange sets a standard

Until recently, differences in computer systems from one firm to another hampered the flow of information. Many firms attacked this problem by adopting **electronic data interchange (EDI)**—an approach that puts information in a standardized format easily shared between different computer systems. In many firms, purchase orders, shipping reports, and other paper documents were replaced with computerized EDI. With EDI, a customer transmits its order information directly to the supplier's computer. The supplier's computer immediately processes the order and schedules production, order assembly, and transportation. Inventory information is automatically updated, and status reports are available instantly. The supplier might then use EDI to send the updated information to the transportation provider's computer. This type of system is now very common. In fact, almost all international transportation firms rely on EDI links with their customers.

EDI systems were originally developed and popularized before the World Wide Web and Internet gained widespread use. Most traditional EDI systems are expensive to develop, rely on proprietary computer networks, and use specialized software to exchange data securely. Alternatives to this approach that rely on the Internet are gaining in popularity. However, there are still some obstacles. While it's easy for firms to share many types of information that use the standard HTML web-page format, HTML is not well suited for exchanging numerical data (like sku numbers, sales volume, purchase quantities, and the like) between software programs on different computers. However, a new standard format, called XML, is gaining popularity and fostering easier EDI-type data exchanges over the Internet.[10]

This improved information flow and coordination affects other PD activities too. Instantaneous order processing or using an EDI system or the Internet, for example, can have the same effect on the customer service level as faster, more expensive transportation. And knowing what a customer has sold or has in stock can improve a supplier's own production planning and reduce both inventory costs and stockouts in the whole channel.

Better coordination of PD activities is a key reason for the success of Pepperidge Farm's line of premium cookies. It was making the wrong products and delivering them too slowly to the wrong market. Poor information was the problem. Delivery truck drivers took orders from retailers, assembled them manually at regional offices,

Transporting costs can be a large part of the total cost for heavy products that are low in value, like sheet aluminum. But the cost of transportation adds little to the total cost of products—like pharmaceuticals—that are already valuable relative to their size and weight.

and then mailed them to Pepperidge Farm's bakeries. Now the company has instant networked data sharing between sales, delivery, inventory, and production. Many of the company's 2,200 drivers use hand-held computers to record the inventory at each stop along their routes. They use the Internet to transmit the information into a computer at the bakeries—so that cookies in short supply will be produced. The right assortment of fresh cookies is quickly shipped to local markets, and delivery trucks are loaded with what retailers need that day. Pepperidge Farm now moves cookies from its bakeries to store shelves in about three days; most cookie producers take about 10 days. That means fresher cookies for consumers and helps to support Pepperidge Farm's high-quality positioning and premium price.[11]

In summary, using computers to share information and coordinate activities is helping some firms and channels compete successfully for customers and increase their own profits.

Ethical issues may arise

Most of the ethical issues that arise in the PD area concern communications about product availability. For example, some critics say that Internet sellers too often take orders for products that are not available or which they cannot deliver as quickly as customers expect. Yet a marketing manager can't always know precisely how long it will take before a product will be available. It doesn't make sense for the marketer to lose a customer if it appears that he or she can satisfy the customer's needs. But the customer may be inconvenienced or face added cost if the marketer's best guess isn't accurate. Similarly, some critics say that stores too often run out of products that they promote to attract consumers to the store. Yet it may not be possible for the marketer to predict demand, or to know when placing an ad that deliveries won't arrive. Different people have different views about how a firm should handle such situations. Some retailers just offer rain checks.

Some suppliers criticize customers for abusing efforts to coordinate PD activities in the channel. For example, some retailers hedge against uncertain demand by telling suppliers that they plan to place an order, but then they don't confirm the order until the last minute. They want to be able to say that it wasn't an order in the first place—if sales in the store are slow. This shifts the uncertainty to the supplier and reduces the retailer's inventory costs. Is this unethical? Some think it is. However, a marketing manager should realize that the firm's order policies can reduce such problems—if the cost of providing the service customers want is higher than what they will pay. In other words, this may simply be another trade-off that the marketer must consider in setting up the PD system.[12]

Now that you see why the coordination of physical distribution activities is so important, let's take a closer look at some of the PD decision areas.

The Transporting Function Adds Value to a Marketing Strategy

Transporting aids economic development and exchange

Transporting is the marketing function of moving goods. Transportation provides time and place utilities—at a cost. But the cost is less than the value added to products by moving them or there is little reason to ship in the first place.

Transporting can help achieve economies of scale in production. If production costs can be reduced by producing larger quantities in one location, these savings may more than offset the added cost of transporting the finished products to customers. Without low-cost transportation, both within countries and internationally, there would be no mass distribution as we know it today.

Transporting can be costly

Transporting costs may limit the target markets a marketing manager can consider. Shipping costs increase delivered cost—and that's what really interests customers. Transport costs add little to the cost of products that are already valuable relative to their size and weight. A case of medicine, for example, might be shipped to a drugstore at low cost. But transporting costs can be a large part of the total cost for heavy products of low value—like many minerals and raw materials. You can imagine that shipping a massive roll of aluminum to a producer of soft-drink cans is an expensive proposition. Exhibit 12-4 shows transporting costs as a percent of total sales dollars for several products.[13]

Governments may influence transportation

Government often plays an important role in the development of a country's transportation system—including its roads, harbors, railroads, and airports. And different countries regulate transportation differently—although regulation has in general been decreasing.

For example, as part of their move toward unification, most European countries are reducing their transporting regulations. The construction of the tunnel under the English Channel is a dramatic example of the changes taking place. The "chunnel" allows trains to speed between England and the rest of Europe.

As regulations decreased in the U.S., competition in the transportation industry increased. As a result, a marketing manager generally has many carriers in one or more modes competing for the firm's transporting business. Or a firm can do its own transporting. So knowing about the different modes is important.[14]

Exhibit 12-4
Transporting Costs as a Percent of Selling Price for Different Products

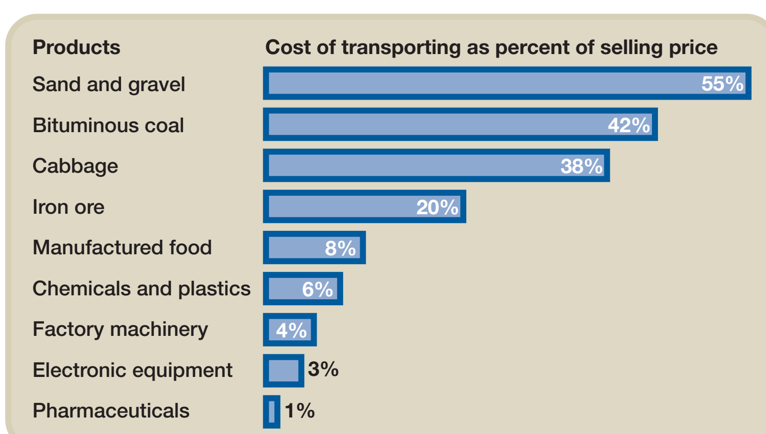


Exhibit 12-5 Benefits and Limitations of Different Transport Modes

	Transporting Features					
Mode	Cost	Delivery speed	Number of locations served	Ability to handle a variety of goods	Frequency of scheduled shipments	Dependability in meeting schedules
Truck	High	Fast	Very extensive	High	High	High
Rail	Medium	Average	Extensive	High	Low	Medium
Water	Very low	Very slow	Limited	Very high	Very low	Medium
Air	Very high	Very fast	Extensive	Limited	High	High
Pipeline	Low	Slow	Very limited	Very limited	Medium	High

Which Transporting Alternative Is Best?

Transporting function must fit the whole strategy

The transporting function should fit into the whole marketing strategy. But picking the best transporting alternative can be difficult. The "best" alternative depends on the product, other physical distribution decisions, and what service level the company wants to offer. The best alternative should not only be as low-cost as possible but also provide the level of service (for example, speed and dependability) required. Exhibit 12-5 shows that different modes of transportation have different strengths and weaknesses. You can find more detail at the website of the Bureau of Transportation Statistics (www.bts.gov). Low transporting cost is *not* the only criterion for selecting the best mode.[15]

Railroads—large loads moved at low cost

Railroads are still the workhorse of the U.S. transportation system. They carry more freight over more miles than any other mode. However, they account for less

Mercedes recently introduced a new, smaller truck that is designed to be more flexible in making deliveries in congested cities like Istanbul, where this ad appeared.

Babbages Changes the Rules to Win Game Lovers' Business

Winning the hearts, wallets, and loyalty of electronic game fanatics isn't easy, but Babbages' marketing strategy has done just that. Imagine, for instance, the week in which the folks at Babbages shipped 500,000 units of 73 different games by overnight delivery to 900 different stores. Or there was the time they filled tractor-trailer trucks at Nintendo's loading dock, at midnight, and then rushed to a chartered jet so that a highly anticipated game would be available in stores the same day it was released. Have they lost their minds? No, but some people think that their customers have. Big-spending game enthusiasts want to be the very first to get a new game when it comes out. So Babbages ships every new game for overnight delivery. While Wal-Mart and Best Buy stores can stock more at a lower price, it takes longer for games to work through their distribution centers and get to store shelves. By then, Babbages would like to be sold out. The shelf life of a new game is only about 15 weeks, and most sales are at the beginning. So gamers will drive across town to get a game sooner at Babbages, even if it's more pricey. That way, when someone asks their opinions about a new game, they will be in the know. In fact, game manufacturers like Nintendo know that avid gamers post reviews of a game on the Internet within 24 hours of when it gets to Babbages. If reviews say that a game is really hot, the manufacturer can ramp up production. That saves time because the factories are in Asia, and it takes about three weeks to reorder and get product on shelves.[16]

www.mhhe.com/fourps

than 10 percent of transport revenues. In the United States, as in other countries, they carry heavy and bulky goods—such as raw materials, steel, chemicals, and coal—over long distances. By handling large quantities, the railroads are able to transport at relatively low cost. For example, in the United States the average cost to ship by rail runs about 2 to 3 cents a ton-mile. Because railroad freight moves more slowly than truck shipments, it is not as well suited for perishable items or those in urgent demand. Railroads are most efficient at handling full carloads of goods. Less-than-carload (LCL) shipments take a lot of handling and rehandling, which means they usually move more slowly and at a higher price per pound than carload shipments.[17]

Trucks are more expensive, but flexible and essential

The flexibility and speed of trucks make them better at moving small quantities of goods for shorter distances. They can travel on almost any road. They go where the rails can't. They are also reliable in meeting delivery schedules, which is an essential requirement for many of today's logistics systems that require rapid replenishment of inventory after a sale. In combination these factors explain why at least 75 percent of U.S. consumer products travel at least part of the way from producer to consumer by truck. And in countries with good highway systems, trucks can give extremely fast service. Trucks compete for high-value items. This is reflected in their rates, which average about 26 cents per ton-mile in the United States. Critics complain that trucks congest traffic and damage highways. But trucks are essential to our present macro-marketing system.[18]

Ship it overseas—but slowly

Water transportation is the slowest shipping mode—but usually the lowest-cost way of shipping heavy freight. Water transportation is very important for international shipments and often the only practical approach. This explains why port cities like Boston, New York City, Rotterdam, Osaka, and Singapore are important centers for international trade.

The growth of airfreight has made it easier and faster for firms to serve customers in foreign markets.

Inland waterways are important too

Inland waterways (such as the Mississippi River and Great Lakes in the United States and the Rhine and Danube in Europe) are also important, especially for bulky, nonperishable products such as iron ore, grain, steel, petroleum products, and gravel. However, when winter ice closes freshwater harbors, alternate transportation must be used. Some shippers—such as those moving iron ore—ship their total annual supply during the summer months and store it near their production facilities for winter use. Here low-cost transporting combined with storing reduces *total* cost.

Pipelines move oil and gas

Pipelines are used primarily by the petroleum industry to move oil and natural gas. So pipelines are important both in the oil-producing and oil-consuming countries. Only a few major cities in the United States, Canada, Mexico, and Latin America are more than 200 miles from a major pipeline system. Of course, the majority of the pipelines in the United States are located in the Southwest—connecting the oil fields and refineries. From there, the more flexible railroads, trucks, and ships usually take over—bringing refined and graded products to customers.

Airfreight is expensive but fast and growing

The most expensive cargo transporting mode is airplane—but it is fast! Airfreight rates are on average three times higher than trucking rates—but the greater speed may offset the added cost. Trucks took the cream of the railroads' traffic. Now airplanes are taking the cream of the cream.

High-value, low-weight goods—like high-fashion clothing and parts for the electronics and metal-working industries—are often shipped by air. Perishable products that previously could not be shipped are now being flown across continents and oceans. Flowers and bulbs from Holland, for example, now are jet-flown to points all over the world. And airfreight has become very important for small emergency deliveries—like repair parts, special orders, and business documents that must be somewhere the next day.

Internet

Internet Exercise A firm that is just starting to export to international markets may want help figuring out what shipping services are available. The North Carolina Ports Authority's website (www.ncports.com) helps provide such information. Go to the website, select *Ports Directory,* and review the different firms and agencies that might be able to provide you with help if you had to ship a large quantity of furniture to the Middle East. Identify an organization from those listed that you might want to contact first, and indicate why.

But airplanes may cut the total cost of distribution

An important advantage of using planes is that the cost of packing, unpacking, and preparing the goods for sale may be reduced or eliminated. Planes may help a firm reduce inventory costs by eliminating outlying warehouses. Valuable by-products of airfreight's speed are less spoilage, theft, and damage. Although the *transporting* cost of air shipments may be higher, the *total* cost of distribution may be lower. As more firms realize this, airfreight firms—like DHL Worldwide Express, FedEx, Airborne, and Emery Air Freight—have enjoyed rapid growth.

These firms play an especially important role in the growth of international business. While the bulk of international cargo moves on ships, the speed of airfreight opens up global markets for many businesses that previously had only domestic opportunities. For example, DHL Worldwide Express offers 24-hour delivery service from Tokyo to Los Angeles, New York to Rome, and London to Chicago. For a firm whose products are valuable relative to their weight and size, the cost of air deliveries may seem trivial when compared to the sales potential of competing in new markets.[19]

Put it in a container—and move between modes easily

Products often move by several different modes and carriers during their journey. This is especially common for international shipments. Japanese firms—like Sony—ship stereos to the United States, Canada, and Europe by boat. When they arrive at the dock, they are loaded on trains and sent across the country. Then the units are delivered to a wholesaler by truck or rail.

Loading and unloading goods several times used to be a real problem. Parts of a shipment would become separated, damaged, or even stolen. And handling the goods—perhaps many times—raised costs and slowed delivery. Many of these problems are reduced with **containerization**—grouping individual items into an economical shipping quantity and sealing them in protective containers for transit to the final destination. This protects the products and simplifies handling during shipping. Some containers are as large as truck bodies.

Piggyback—a ride on two or more modes

Piggyback service means loading truck trailers—or flatbed trailers carrying containers—on railcars to provide both speed and flexibility. Railroads now pick up truck trailers at the producer's location, load them onto specially designed rail flatcars, and haul them as close to the customer as rail lines run. The trailers are then hooked up to a truck tractor and delivered to the buyer's door. Similar services are offered on ocean-going ships—allowing door-to-door service between cities around the world.

To better coordinate the flow of products between modes, transportation companies like CSX offer customers a complete choice of different transportation modes. Then CSX, not the customer, figures out the best and lowest-cost way to shift and share transporting functions between the modes.[20]

Transportation choices affect environmental costs too

Marketing managers must be sensitive to the environmental effects of transportation decisions. Some say trucks cause air pollution in already crowded cities. People who live near airports suffer the consequences of noise pollution. A damaged pipeline can spew thousands of gallons of oil before it can be repaired. The Exxon *Valdez* oil spill in Alaska is a dramatic example of the kind of environmental disaster that can happen when a transportation accident occurs.

Many firms are taking steps to reduce these problems. For example, Conoco, a subsidiary of Du Pont, is building ships with double hulls to reduce the risk of leaks. Some trucking and railroad firms establish elaborate safety procedures for dealing with toxic cargo. Today, the public *expects* companies to manufacture, transport, sell, and dispose of products in an environmentally sound manner. If companies are environmentally unsafe, consumers will show their dissatisfaction through their market choices. However, these environmental efforts increase the cost of distribution.[21]

Economies of Scale in Transporting

Most transporting rates—the prices charged for transporting—are based on the idea that large quantities of a good can be shipped at a lower transport cost per pound than small quantities. Whether a furniture producer sends a truck to deliver one sofa or a full carload, the company still has to pay for the driver, the truck, the gas, and other expenses like insurance.

Transporters often give much lower rates for quantities that make efficient use of their transport facilities. Thus, transport costs per pound for less-than-full carloads or truckloads are often twice as high as for full loads. These quantity rate differences are one important reason for the development of some wholesalers. They buy in large quantities to get the advantage of economies of scale in transporting. Then they sell in the smaller quantities their customers need.

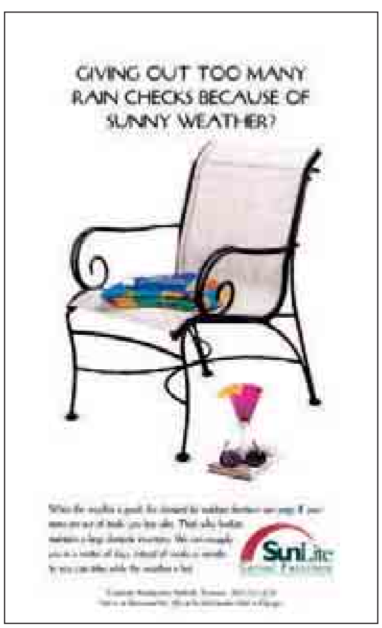
Freight forwarders accumulate economical shipping quantities

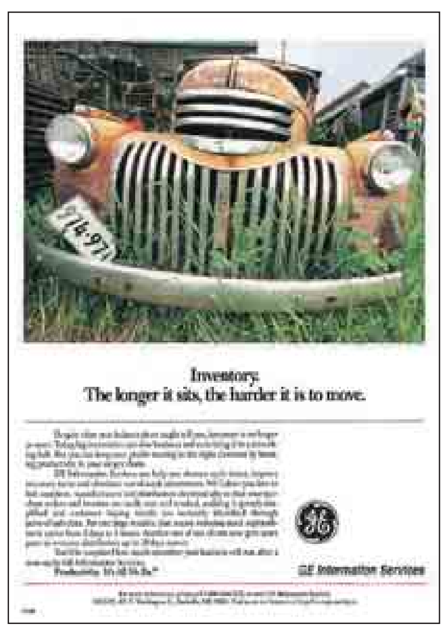
Freight forwarders combine the small shipments of many shippers into more economical shipping quantities. Freight forwarders do not own their own transporting facilities—except perhaps for delivery trucks. Rather, they wholesale air, ship, rail, and truck space. They accumulate small shipments from many shippers and reship in larger quantities to obtain lower transporting rates.

Freight forwarders are especially useful in arranging international shipping. They handle 75 percent of the general cargo shipped from U.S. ports to foreign countries. They are also very helpful for handling international airfreight. For example, Air Express International specializes in helping marketing managers find the most efficient air cargo firm to speed deliveries around the world.[22]

Should you do it yourself?

To cut transporting costs or get more control, some marketing managers do their own transporting rather than buy from specialists. Large producers, like Levi Strauss, often buy or lease their own truck fleets. Shell Oil and other large petroleum, iron ore, and gypsum rock producers have their own ships. Some firms now buy their own planes for airfreight.[23]





Both SunLite and GE provide logistics-related services that help firms reduce big inventories and improve customer service.

The Storing Function and Marketing Strategy

Store it and smooth out sales, increase profits and consumer satisfaction

Storing is the marketing function of holding goods. It provides time utility. **Inventory** is the amount of goods being stored.

Maintaining the right inventory level is difficult when it's hard to forecast likely demand. Even so, a firm that is stocked out when customers are ready to buy may not only lose the sale but may also damage the relationship and the possibility of future sales. Kmart ran into this problem. A number of consumers decided it was no longer a convenient place to shop when stores repeatedly ran out of basic staples that consumers expected to find.

Storing is necessary when production of goods doesn't match consumption. This is common with mass production. Nippon Steel, for example, might produce thousands of steel bars of one size before changing the machines to produce another size. Changing the production line can be costly and time-consuming. It's often cheaper to produce large quantities of one size, and store the unsold quantity, than to have shorter production runs. Thus, storing goods allows the producer to achieve economies of scale in production.

Some buyers purchase in large quantities to get quantity discounts from the producer or transporter. Then the extra goods must be stored until there is demand. And goods are sometimes stored as a hedge against future price rises, strikes, shipping interruptions, and other disruptions.

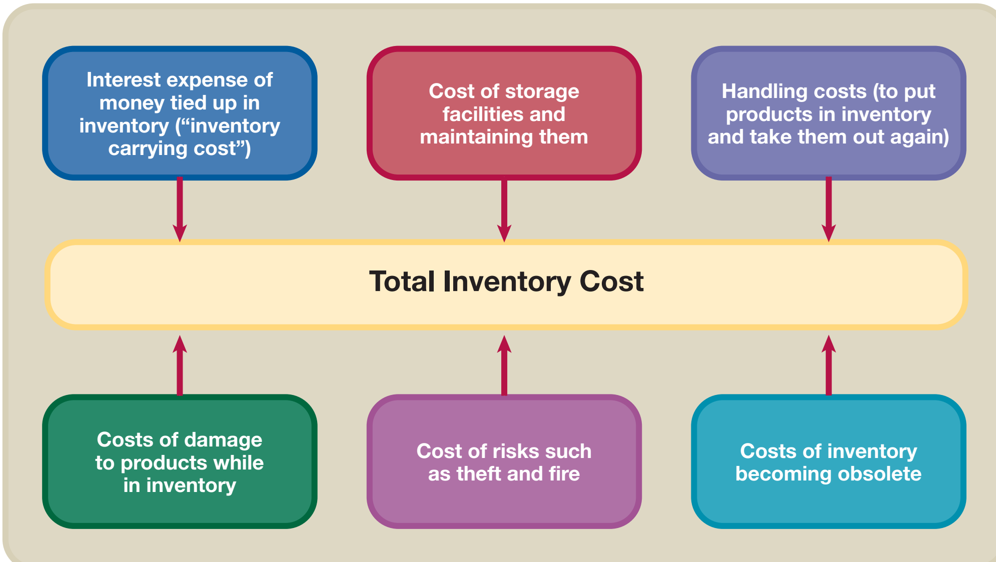
Storing varies the channel system

Storing allows producers and middlemen to keep stocks at convenient locations—ready to meet customers' needs. In fact, storing is one of the major activities of some middlemen.

Most channel members provide the storing function for some length of time. Even final consumers store some things for their future needs. Since storing can be provided anywhere along the channel, the storing function offers several ways to vary a firm's marketing mix and its channel system by (1) adjusting the time goods are held, (2) sharing the storing costs, and (3) delegating the job to a specialized storing facility. This latter variation would mean adding another member to the distribution channel.

When consumers buy in large quantities and keep the product inventory near the point of consumption they take over some of the inventory carrying costs—and they may consume more too.

Exhibit 12-6 Many Expenses Contribute to Total Inventory Cost



Which channel members store the product, and for how long, affects the behavior of all channel members. For example, the producer of Snapper lawn mowers tries to get wholesalers to inventory a wide selection of its machines. That way, retailers can carry smaller inventories since they can be sure of dependable local supplies. And they might decide to sell Snapper—rather than Toro or some other brand that they would have to store at their own expense.

If final customers “store” the product, more of it may be used or consumed. You saw this in the Coke case that introduces this chapter. Coke wants customers to buy six packs and 2-liter bottles. Then consumers have an “inventory” in the refrigerator when thirst hits. Of course, consumers aren’t always willing or able to hold the inventory. In China, for example, Coke had little success until it gave up pushing 2-liter bottles and switched to single-serving 75 ml bottles. Only 1 out of 10 Chinese families has a refrigerator—so they didn’t have a good way to store a bottle once it was open.

Goods are stored at a cost

Storing can increase the value of goods and make them more available when customers want them. But a manager must remember that *storing always involves costs* too. Different kinds of cost are involved. See Exhibit 12-6. Car dealers, for example, must store cars on their lots—waiting for the right customer. The interest expense of money tied up in the inventory is a major cost. In addition, if a new car on the lot is dented or scratched, there is a repair cost. If a car isn’t sold before the new models come out, its value drops. There is also a risk of fire or theft—so the retailer must carry insurance. And, of course, dealers incur the cost of leasing or owning the display lot where they store the cars.

In today’s competitive markets, most firms watch their inventories closely. Taken in total, the direct and indirect costs of unnecessary inventory can make the difference between a profitable strategy and a loser. Annually these costs are typically 20 to 40 percent of the average value of the inventory. As a result, well-run firms everywhere are trying to cut unnecessary stock and reduce the drain it puts on profits. On the other hand, a marketing manager must be very careful in making the distinction between unnecessary inventory and inventory needed to provide the distribution service customers expect.[24]

Rapid response cuts inventory costs

Many firms are finding that they can cut inventory costs and still provide the desired customer service—if they can reduce the time it takes to replace items that are sold. This is one important reason that the JIT and ECR approaches we discussed earlier in the chapter have been widely adopted. These approaches work because the firms involved use EDI, the Internet, and similar computerized approaches to share information and speed up the order cycle and delivery process.

Rapid replenishment of inventories is not the only reason that inventory costs have been reduced. By using the information from JIT and ECR systems, firms can see the benefit of dropping some of the items that they stock and sell. P&G is a vivid example. Between 1991 and 1996 it introduced many new products but cut its total number of skus (individual stock-keeping units) by 34 percent. P&G hasn't stopped selling bar soap, but it has cut the number of sizes and colors for some of its brands. After the cuts, sales of the remaining products went up and costs came down. With fewer products, P&G can put more marketing effort behind those it has. Its retailers are also more willing to push products that turn over quickly. Reducing the number of skus does reduce consumer choice, but there is a point where additional choice doesn't add enough value for consumers to justify the extra inventory.[25]

Specialized Storing Facilities May Be Required

New cars can be stored outside on the dealer's lot. Fuel oil can be stored in a specially designed tank. Coal and other raw materials can be stored in open pits. But most products must be stored inside protective buildings. Often, firms can choose among different types of specialized storing facilities. The right choice may reduce costs and serve customers better.

Private warehouses are common

Private warehouses are storing facilities owned or leased by companies for their own use. Most manufacturers, wholesalers, and retailers have some storing facilities either in their main buildings or in a separate location. A sales manager often is responsible for managing a manufacturer's finished-goods warehouse—especially if regional sales branches aren't near the factory. In retailing, storing is so closely tied to selling and available shelf space that buyers may control this function.

Firms use private warehouses when a large volume of goods must be stored regularly. Yet private warehouses can be expensive. If the need changes, the extra space may be hard, or impossible, to rent to others.

Public warehouses fill special needs

Public warehouses are independent storing facilities. They can provide all the services that a company's own warehouse can provide. A company might choose a public warehouse if it doesn't have a regular need for space. For example, Tonka Toys uses public warehouses because its business is seasonal. Tonka pays for the space only when it is used. Public warehouses are also useful for manufacturers who must maintain stocks in many locations—including foreign countries.

In most countries, public warehouses are located in all major metropolitan areas and many smaller cities. See Exhibit 12-7 for a comparison of private and public warehouses.[26]

Warehousing facilities cut handling costs too

The cost of physical handling is a major storing cost. Goods must be handled once when put into storage and again when removed to be sold. In old warehouse districts—located in big cities or at ports—traffic congestion, crowded storage areas, and slow elevators delay the process and increase the costs.

Exhibit 12-7
A Comparison of Private Warehouses and Public Warehouses

	Type of warehouse	
Characteristics	Private	Public
Fixed investment	Very high	No fixed investment
Unit cost	High if volume is low Very low if volume is very high	Low: charges are made only for space needed
Control	High	Low managerial control
Adequacy for product line	Highly adequate	May not be convenient
Flexibility	Low: fixed costs have already been committed	High: easy to end arrangement

Today, modern one-story buildings away from downtown traffic are replacing the old multistory warehouses. They eliminate the need for elevators and permit the use of power-operated lift trucks, battery-operated motor scooters, roller-skating order pickers, electric hoists for heavy items, and hydraulic ramps to speed loading and unloading. Most of these new warehouses use lift trucks and pallets (wooden trays that carry many cases) for vertical storage and better use of space. Bar codes and UPC (uniform product code) numbers make it easy for computers to monitor inventory, order needed stock, and track storing and shipping costs. Some warehouses have computer-controlled order-picking systems or conveyor belts that speed the process of locating and assembling the assortment required to fill an order.[27]

The Distribution Center—A Different Kind of Warehouse

Is storing really needed?

Discrepancies of assortment or quantity between one channel level and another are often adjusted at the place where goods are stored. It reduces handling costs to regroup and store at the same place—*if both functions are required.* But sometimes regrouping is required when storing isn't.

Don't store it, distribute it

A **distribution center** is a special kind of warehouse designed to speed the flow of goods and avoid unnecessary storing costs. Anchor Hocking moves over a million pounds of its housewares products through its distribution center each day. Faster inventory turnover and easier bulk-breaking reduce the cost of carrying inventory and lead to bigger profits.

Today, the distribution center concept is widely used by firms at all channel levels. Many products buzz through a distribution center without ever tarrying on a shelf; workers and equipment immediately sort the products as they come in and then move them to an outgoing loading dock and the vehicle that will take them to their next stop. While these "cross-docking" approaches have become more efficient, the basic benefits of the distribution center approach are still the same as they were over 25 years ago when the idea was pioneered. In fact, a good way to see how the distribution center works is to consider an early application.

Pillsbury's distribution system was overwhelmed by expanding product lines and sales

Pillsbury—the manufacturer of baking products—used to ship in carload quantities directly from its factories to large middlemen. Initially, plants were as close to customers as possible, and each plant produced the whole Pillsbury line. As lines expanded, however, no single plant could produce all the products. When customers began to ask for mixed carload shipments and faster delivery,

McKesson is a leading distributor of drugs, and effective use of technology has been a key reason for its success. The space-age gizmo on this man's arm combines a scanner, computer, and two-way radio—to speed up order assembly and delivery from McKesson's distribution center.

Pillsbury added warehouse space and started hauling goods from plant to plant. Over time, Pillsbury set up 100 branch warehouses—controlled by 33 sales offices. Accounting, credit, and other processing operations were duplicated in each sales office. PD costs were high, but the customer service level was still a problem. It took Pillsbury a week just to process an order. And the company had no effective control over its inventories. Pillsbury needed a change to distribution centers.

The distribution center brings it all together

Pillsbury first specialized production at each plant to a few product lines. Then Pillsbury sent carload shipments directly to the distribution centers—almost eliminating storing at the factories. The distribution centers were controlled by regional data processing centers, which quickly determined where and when goods were to be shipped. Centralized accounting got invoices to customers faster—resulting in quicker payment. Because each distribution center always had adequate inventory, it could ship orders the most economical way. And because the field sales organization no longer handled physical distribution or inventory, it could focus on sales. Pillsbury could guarantee customers delivery within three days.

There are many variations of the distribution center. The Pillsbury example shows it within an integrated operation. But public warehouses offer similar services.

Managers must be innovative to provide customers with superior value

Improved technology, coordination among firms, and efficient new distribution centers are bringing big improvements to the PD area. Yet the biggest challenges may be more basic. As we've emphasized here, physical distribution activities transcend departmental, corporate, and even national boundaries. So seeing and taking advantage of the opportunities for improvement often requires cooperation all along the channel system. Too often, such cooperation doesn't exist—and changing ingrained ways of doing things is hard. But marketing managers who push for innovations in these areas are likely to win customers away from firms and whole channel systems that are stuck doing things in the old way.[28]

Conclusion

This chapter deals with logistics activities and how they provide *time* and *place* utility to improve value to the customer. We looked at the customer service level and why it is important.

We emphasized the relation between customer service level, transporting, and storing. The physical distribution concept focuses on coordinating all the storing, transporting, and product handling activities into a smoothly working system—to deliver the desired service level and customer value at the lowest cost.

Marketing managers often want to improve service and may select a higher-cost alternative to improve their marketing mix. The total cost approach might reveal that it is possible *both* to reduce costs and to improve service—perhaps by identifying creative new distribution alternatives.

We discussed various modes of transporting and their advantages and disadvantages. We also discussed ways to reduce inventory costs. We explained why distribution centers are an important way to cut storing and handling costs, and we explained how computerized information links—within firms and among firms in the channel—are increasingly important in blending all of the activities into a smooth-running system.

Effective marketing managers make important strategy decisions about physical distribution. Creative strategy decisions may result in lower PD costs while maintaining or improving the customer service level. And production-oriented competitors may not even understand what is happening.

Questions and Problems

1. Explain how adjusting the customer service level could improve a marketing mix. Illustrate.
2. Briefly explain which aspects of customer service you think would be most important for a producer that sells fabric to a firm that manufactures furniture.
3. Briefly describe a purchase you made where the customer service level had an effect on the product you selected or where you purchased it.
4. Discuss the types of trade-offs involved in PD costs, service levels, and sales.
5. Give an example of why it is important for different firms in the chain of supply to coordinate logistics activities.
6. Discuss some of the ways computers are being used to improve PD decisions.
7. Explain why a just-in-time delivery system would require a supplier to pay attention to quality control. Give an example to illustrate your points.
8. Discuss the problems a supplier might encounter in using a just-in-time delivery system with a customer in a foreign country.
9. Review the list of factors that affect PD service level in Exhibit 12-2. Indicate which ones are most likely to be improved by EDI links between a supplier and its customers.
10. Explain the total cost approach and why it may cause conflicts in some firms. Give examples of how conflicts might occur between different departments.
11. Discuss the relative advantages and disadvantages of railroads, trucks, and airlines as transporting methods.
12. Discuss why economies of scale in transportation might encourage a producer to include a regional merchant wholesaler in the channel of distribution for its consumer product.
13. Discuss some of the ways that air transportation can change other aspects of a Place system.
14. Explain which transportation mode would probably be most suitable for shipping the following goods to a large Los Angeles department store:
    a. 300 pounds of Maine lobster.
    b. 15 pounds of screwdrivers from Ohio.
    c. Three dining room tables from High Point, North Carolina.
    d. 500 high-fashion dresses from the fashion district in Paris.
    e. A 10,000-pound shipment of exercise equipment from Germany.
    f. 600,000 pounds of various appliances from Evansville, Indiana.
15. Indicate the nearest location where you would expect to find large storage facilities. What kinds of products would be stored there? Why are they stored there instead of some other place?

16. When would a producer or middleman find it desirable to use a public warehouse rather than a private warehouse? Illustrate, using a specific product or situation.
17. Discuss the distribution center concept. Is this likely to eliminate the storing function of conventional wholesalers? Is it applicable to all products? If not, cite several examples.
18. Clearly differentiate between a warehouse and a distribution center. Explain how a specific product would be handled differently by each.
19. If a retailer operates only from a website and ships all orders by UPS, is it freed from the logistics issues that face traditional retailers? Explain your thinking.

Suggested Cases

16. Morgan Company
26. Rainbow Packers, Inc.

Computer-Aided Problem

12. **Total Distribution Cost**

Proto Company has been producing various items made of plastic. It recently added a line of plain plastic cards that other firms (such as banks and retail stores) will imprint to produce credit cards. Proto offers its customers the plastic cards in different colors, but they all sell for $40 per box of 1,000. Tom Phillips, Proto's product manager for this line, is considering two possible physical distribution systems. He estimates that if Proto uses airfreight, transportation costs will be $7.50 a box, and its cost of carrying inventory will be 5 percent of total annual sales dollars. Alternatively, Proto could ship by rail for $2 a box. But rail transport will require renting space at four regional warehouses—at $26,000 a year each. Inventory carrying cost with this system will be 10 percent of total annual sales dollars. Phillips prepared a spreadsheet to compare the cost of the two alternative physical distribution systems.

a. *If Proto Company expects to sell 20,000 boxes a year, what are the total physical distribution costs for each of the systems?*
b. *If Phillips can negotiate cheaper warehouse space for the rail option so that each warehouse costs only $20,000 per year, which physical distribution system has the lowest overall cost?*
c. *Proto's finance manager predicts that interest rates are likely to be lower during the next marketing plan year and suggests that Tom Phillips use inventory carrying costs of 4 percent for airfreight and 7.5 percent for railroads (with warehouse cost at $20,000 each). If interest rates are in fact lower, which alternative would you suggest? Why?*

For additional questions related to this problem, see Exercise 12-3 in the *Learning Aid for Use with Basic Marketing*, 14th edition.

When You Finish This Chapter, You Should

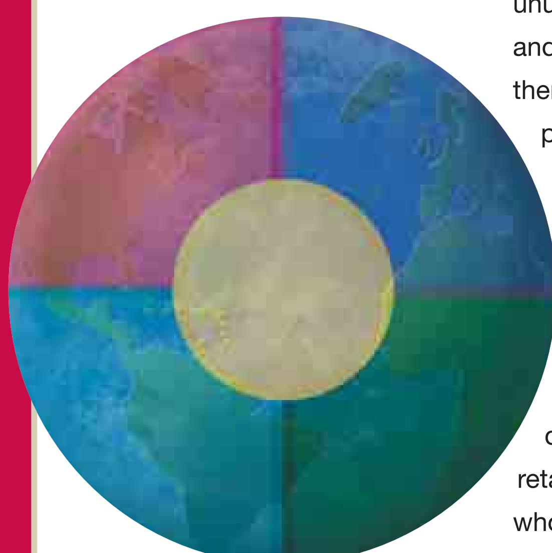
1. Understand how retailers plan their marketing strategies.
2. Know about the many kinds of retailers that work with producers and wholesalers as members of channel systems.
3. Understand the differences among the conventional and nonconventional retailers—including Internet merchants and others who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

Chapter Thirteen

Retailers, Wholesalers, and Their Strategy Planning

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

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

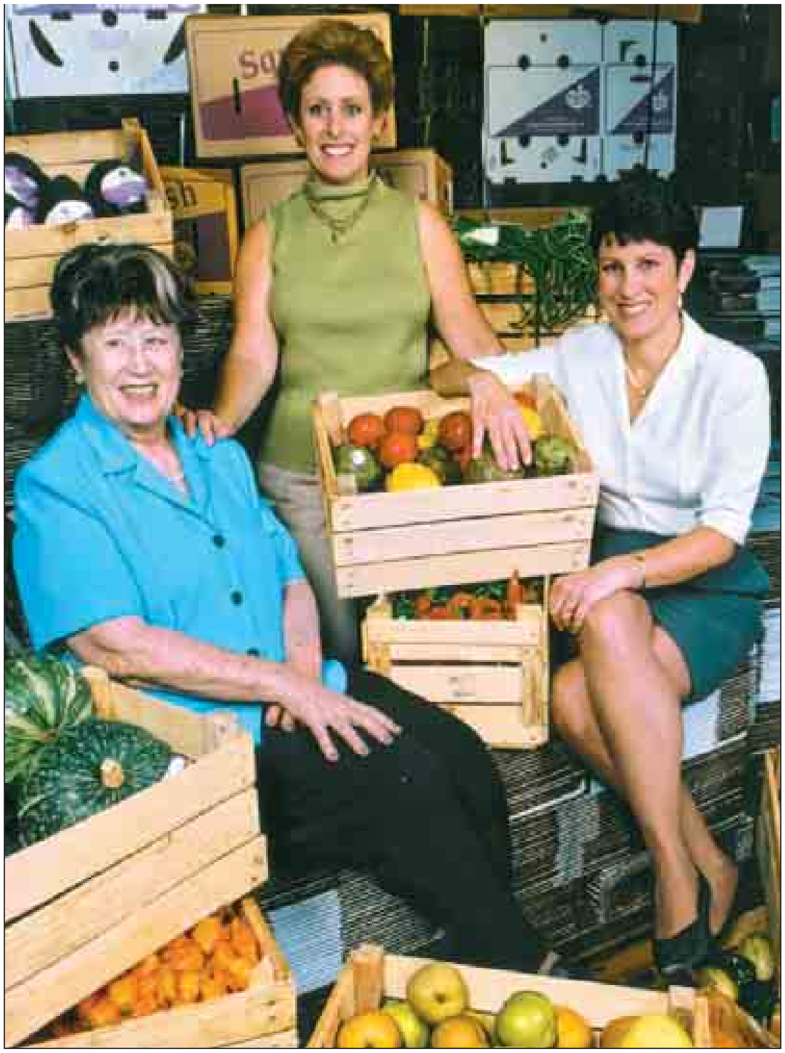


place

price

promotion

produc



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

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

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

The Caplans recently established a retail operation,

www.mhhe.com/fourps

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

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

Wholesalers and Retailers Plan Their Own Strategies

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

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

Understand how retailing and wholesaling are evolving

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

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

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

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

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

The Nature of Retailing

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

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

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

Planning a Retailer's Strategy

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

Consumers have reasons for buying from particular retailers

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

Retailer's whole offering is its Product

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

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

Features of offering relate to needs

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

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

Some features that relate to social and emotional factors include

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

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

Strategy requires carefully set policies

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

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

Consumer needs relate to segmentation and positioning

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

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

Different types of retailers emphasize different strategies

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

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

Conventional Retailers—Try to Avoid Price Competition

Single-line, limited-line retailers specialize by product

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

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

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

Single-line, limited-line stores are being squeezed

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

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

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

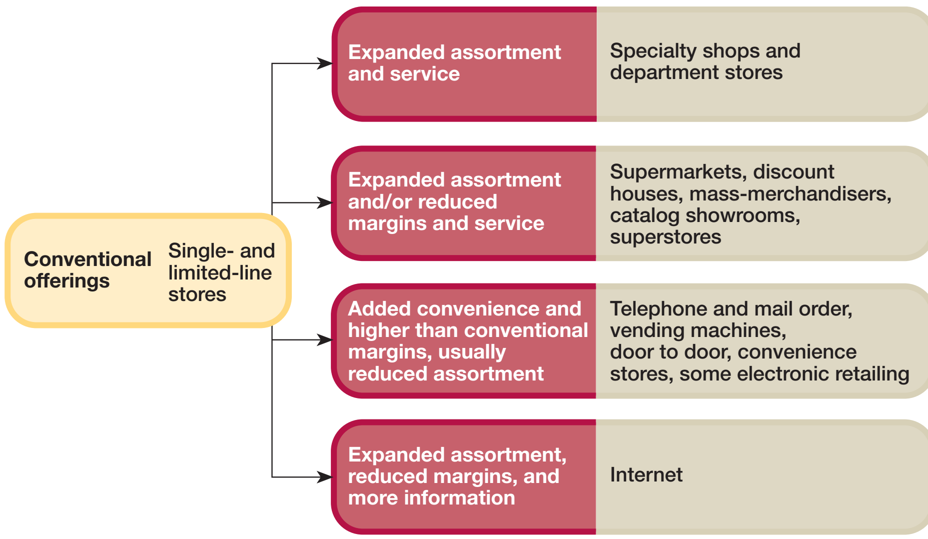
Expand Assortment and Service—To Compete at a High Price

Specialty shops usually sell shopping products

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

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

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



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

Department stores combine many limited-line stores and specialty shops

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

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

Evolution of Mass-Merchandising Retailers

Mass-merchandising is different from conventional retailing

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

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

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

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

Supermarkets started the move to mass-merchandising

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

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

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

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

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

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

Catalog showroom retailers preceded discount houses

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

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

Discount houses upset some conventional retailers

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

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

Mass-merchandisers are more than discounters

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

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

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

Supercenters meet all routine needs

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

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

New mass-merchandising formats keep coming

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

Single-line mass-merchandisers are coming on strong

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

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

Some Retailers Focus on Added Convenience

Convenience (food) stores must have the right assortment

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

Vending machines are convenient

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

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

Shop at home—in a variety of ways

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

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

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

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

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

Put the catalog on cable TV or computer

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

Retailing on the Internet

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

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

It's still in its infancy

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

Moving information versus moving goods

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

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

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

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

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

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

Product assortments are not limited by location

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

Convenience takes on new meanings

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

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

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

More and less information at the same time

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

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

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

Why eToys.com Is eToys.Gone

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

www.mhhe.com/fourps

Lost in the "aisles" of the Internet

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

Internet

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

The costs are still deceptive

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

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

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

Competitive effects will influence other retailers

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

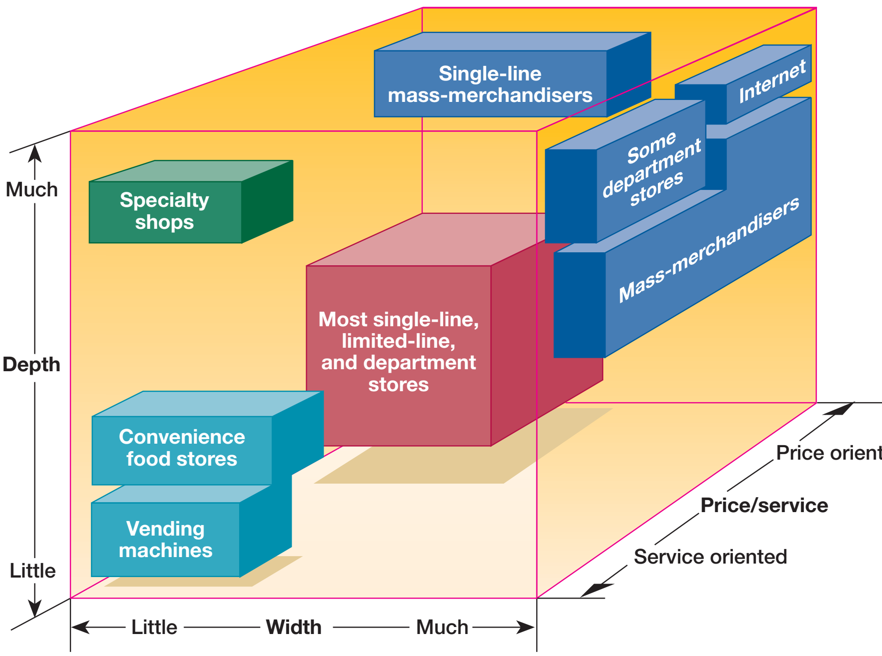
None of these retailers knows what will come of Internet selling. And some of the initial results have been surprises. For example, many orders on Wal-Mart's website are from U.S. citizens who are in the military overseas. Regardless of surprises, retailers need to work to understand the longer-term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

Retailing Types Are Explained by Consumer Needs Filled

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

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

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



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

Why Retailers Evolve and Change

The wheel of retailing keeps rolling

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

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

Scrambled merchandising—mixing product lines for higher profits

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

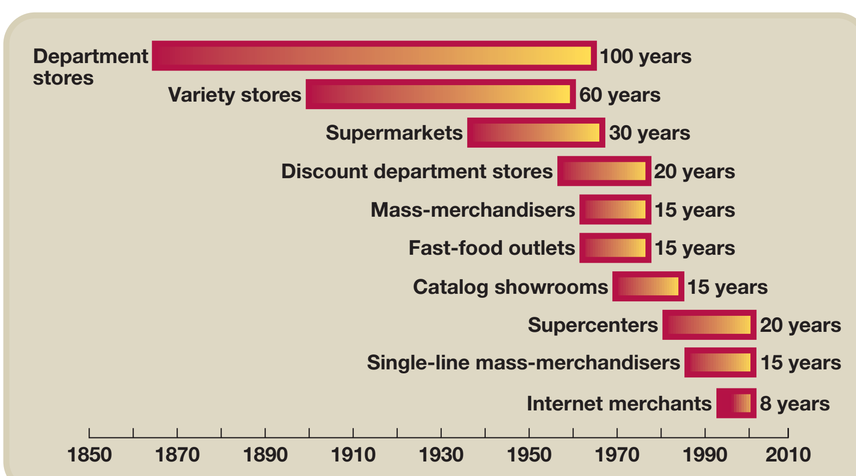
Some manufacturers have always had outlet stores near their factories, but outlet malls are emerging as a new retailing format that is popular with some consumers.

Product life cycle concept applies to retailer types too

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

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

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



Ethical issues may arise

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

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

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

Retailer Size and Profits

A few big retailers do most of the business

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

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

Big chains are building market clout

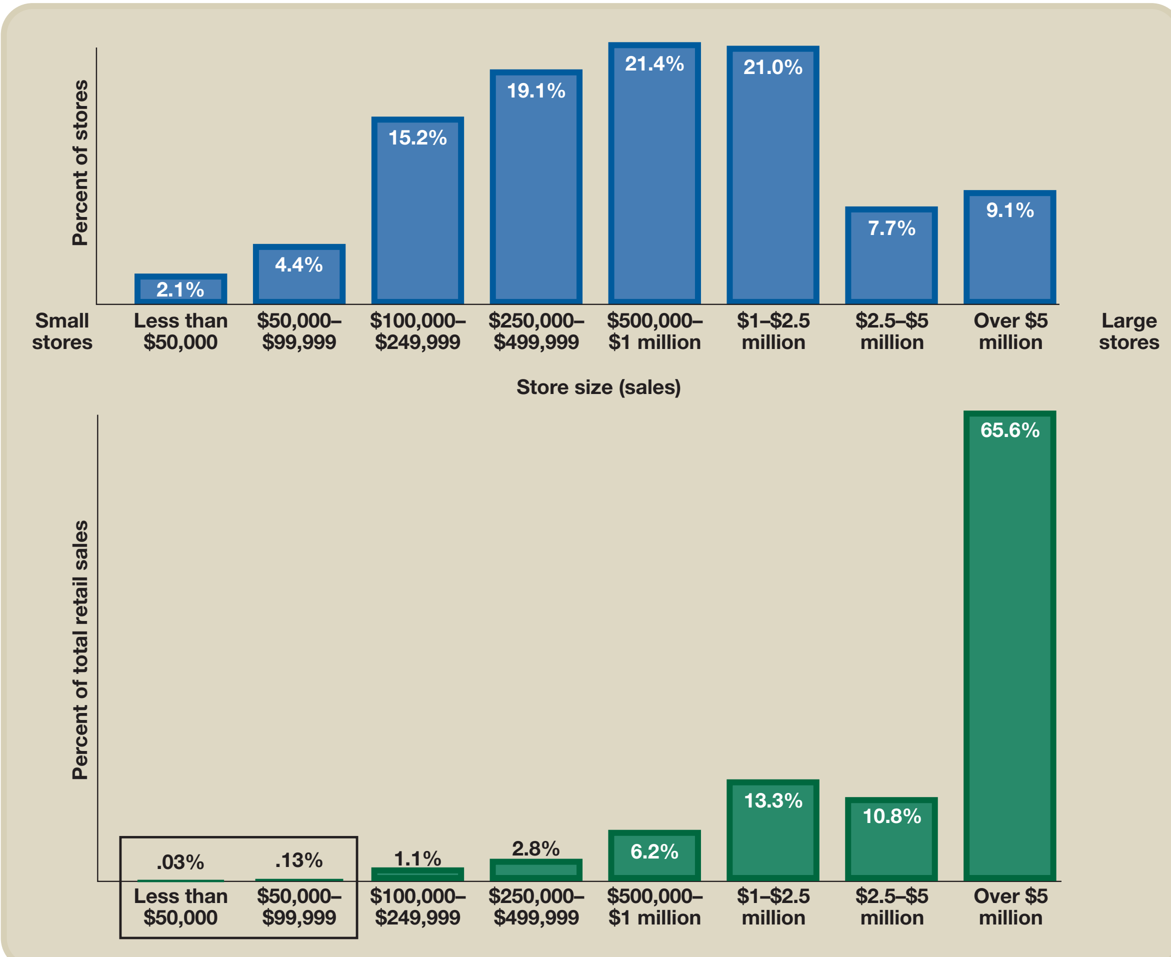
The main way for a retailer to achieve economies of scale is with a corporate chain. A **corporate chain** is a firm that owns and manages more than one store—and often it's many. Chains have grown rapidly and now account for about half of all retail sales. You can expect chains to continue to grow and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

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

Independents form chains too

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

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



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

Franchisors form chains too

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

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

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

Differences in Retailing in Different Nations

New ideas spread across countries

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

Mass-merchandising requires mass markets

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

Consumer cooperatives are popular in some countries

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

Some countries block change

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

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

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

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

What Is a Wholesaler?

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

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

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

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

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

Wholesaling Is Changing with the Times

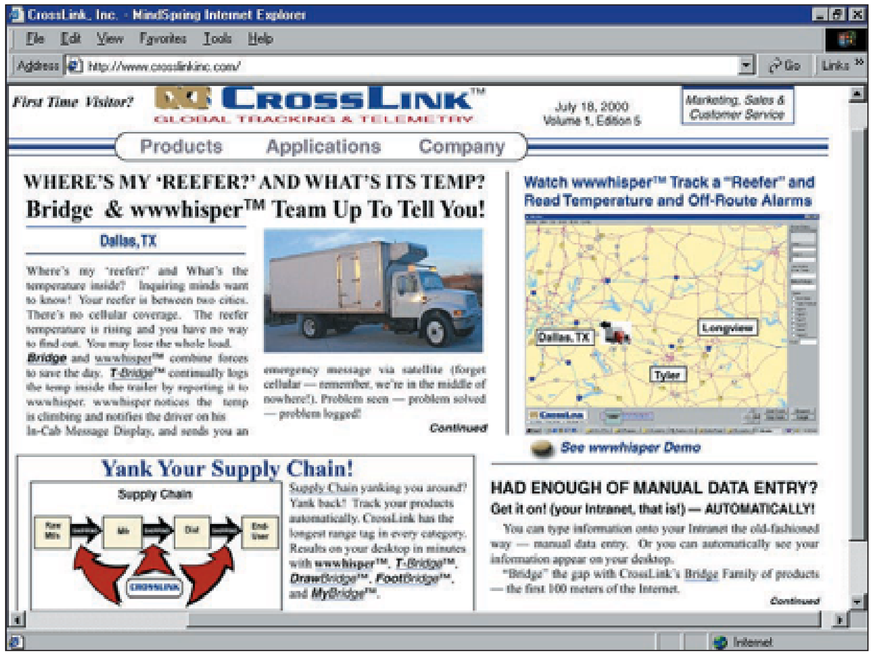
A hundred years ago wholesalers dominated distribution channels in the United States and most other countries. The many small producers and small retailers needed their services. This situation still exists in many countries, especially those with less-developed economies. However, in the developed nations,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

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

Producing profits, not chasing orders

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

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



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

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

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

Progress—or fail

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

Perhaps good-bye to some

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

Is it an ethical issue?

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

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

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

Survivors will need effective strategies

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

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

Wholesalers Add Value in Different Ways

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

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

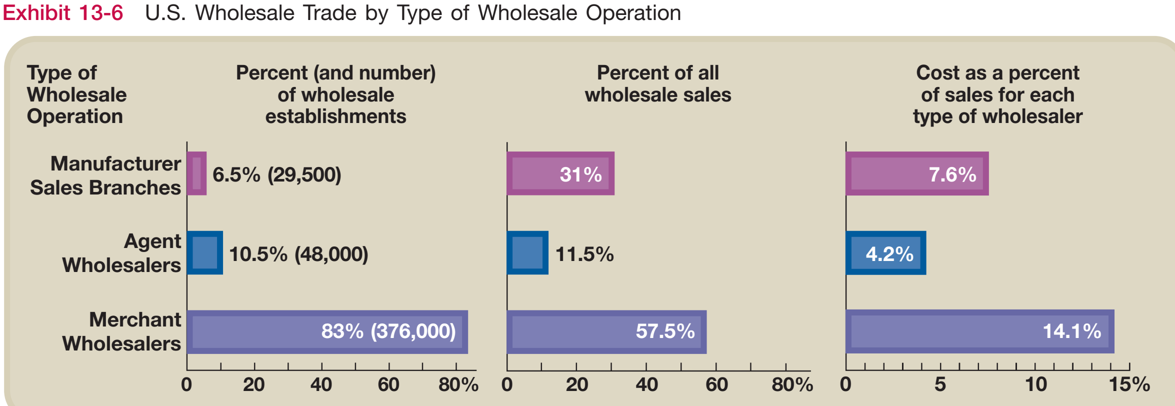
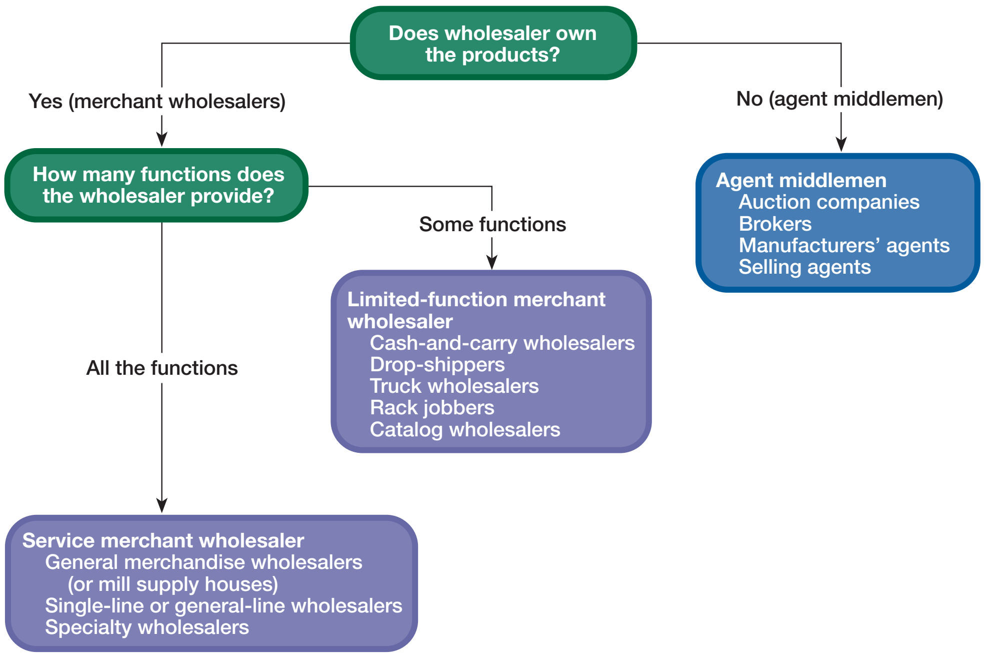


Exhibit 13-7 Types of Wholesalers



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

Manufacturers' sales branches are considered wholesalers

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

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

Merchant Wholesalers Are the Most Numerous

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

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

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

Internet

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

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

Service wholesalers provide all the functions

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

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

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

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

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

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

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

Limited-function wholesalers provide some functions

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

Cash-and-carry wholesalers want cash

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

Drop-shippers do not handle the products

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

Truck wholesalers deliver—at a cost

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

Rack jobbers sell hard-to-handle assortments

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

Catalog wholesalers reach outlying areas

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

Agent Middlemen Are Strong on Selling

They don't own the products

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

They are important in international trade

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

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

Manufacturers' agents—free-wheeling sales reps

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

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

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

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

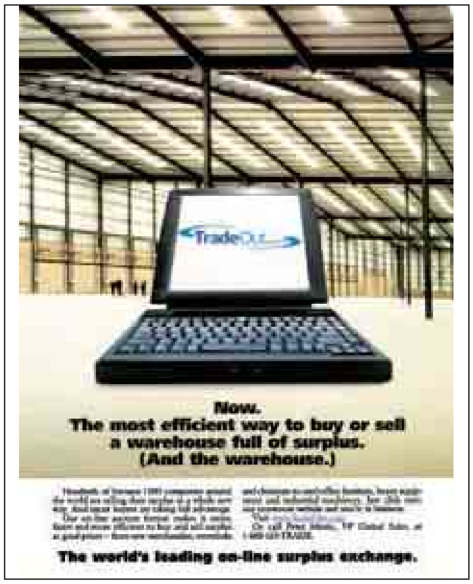
Agents can be especially useful for introducing new products. For this service, they may earn 10 to 15 percent commission. (In contrast, their commission on large-volume established products may be quite low—perhaps only 2 percent.) A 10 to 15 percent commission rate may seem small for a new product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

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

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

Brokers provide information

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



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

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

Selling agents—almost marketing managers

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

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

Auction companies—speed up the sale

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

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

What Will Happen to Retailers and Wholesalers in the Future?

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

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

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

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

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

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

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

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

Conclusion

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

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

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

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

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

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

Questions and Problems

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

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

Suggested Cases

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

Computer-Aided Problem

13. **Selecting Channel Intermediaries**

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

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

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

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

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

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

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

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

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

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

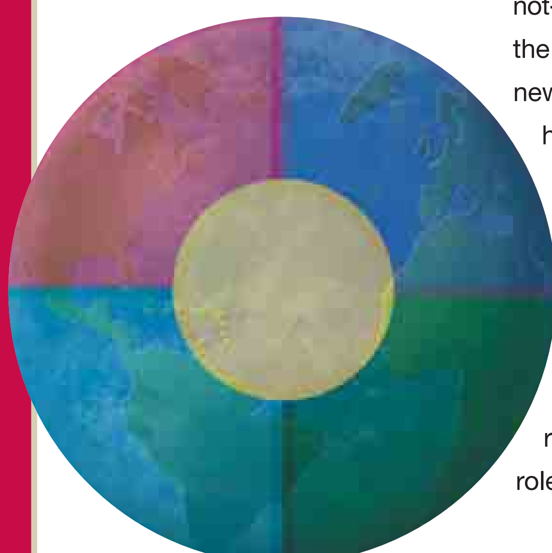
Chapter Fourteen

Promotion—Introduction to Integrated Marketing Communications

When You Finish This Chapter, You Should

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

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



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

place price promotion produc

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

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

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

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

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

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

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

Several Promotion Methods Are Available

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

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