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15

Managing Marketing Channels and Supply Chains

LEARNING OBJECTIVES

After reading this chapter you should be able to:

**LO 15-
1**

Explain what is meant by a marketing channel of distribution and why intermediaries are needed.

**LO 15-
2**

Distinguish among traditional marketing channels, electronic marketing channels, and different types of vertical marketing systems.

**LO 15-
3**

Describe factors that marketing executives consider when selecting and managing a marketing channel, including legal restrictions.

**LO 15-
4**

Explain what supply chain and logistics management are and how they relate to marketing strategy.

Callaway Golf: Designing and Delivering the Goods for Great Golf

What do Morgan Pressel and Phil Mickelson, two world-class golf professionals, have in common? Both use Callaway Golf equipment, accessories, and apparel when playing their favorite sport.

With annual sales approaching \$900 million, Callaway Golf is one of the most recognized and highly regarded companies in the golf industry. With its commitment to continuous product innovation and broad distribution in the United States and more than 100 countries worldwide, Callaway Golf has built a strong reputation for designing and delivering the goods for golfers of all skill levels, both amateur and professional.

Callaway Golf primarily markets its products through more than 15,000 on- and off-course authorized golf retailers and sporting goods retailers, such as Golf Galaxy, Inc., Dick's Sporting Goods, Inc., and PGA Tour Superstores, which sell quality golf products and provide a level of customer service appropriate for the sale of such products. Callaway Golf considers its retailers a valuable marketing asset.

The company also has its own online store (CallawayGolf.com), which makes it a full-fledged multichannel marketer, and a successful one as well. Soon after CallawayGolf.com was launched, the chief executive of PGA of America called the store "innovative in that it combines that old legacy relationship with the retail channel with the new innovation of the Web." According to a Marketing Group spokesperson, "Callaway produces in-house a wide-ranging, high volume of original content from instructional videos to interviews with R&D leads and Tour Pros, blog posts and even live streams of Callaway events. This commitment to creating original content helps to give consumers a better feel for the Company and its products when they go to purchase equipment online and at retail."

Today, CallawayGolf.com is a dynamic, engaging and interactive website that constantly delivers new in-depth product information and media, original social content, user-generated content, and e-commerce capabilities. All of this helps consumers become better informed during the purchasing process. Not surprisingly, CallawayGolf.com is listed among the top Internet retailers in the United States.

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#BerthasBack

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Providing Callaway's authorized golf retailers and sporting goods retailers with the right products, at the right place, at the right time, and in the right

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quantity and condition is the responsibility of the company's Page 407
supply chain. Callaway sources raw materials for its golf equipment, accessories, and all apparel from around the world. At the same time, Callaway delivers its finished products to company retailers through external shipping companies, such as United Parcel Service (UPS).¹

This chapter first focuses on marketing channels of distribution and why they are an important component in the marketing mix. It then shows how such channels benefit consumers and the sequence of firms that make up a marketing channel. Finally, it describes factors that influence the choice and management of marketing channels, including channel conflict and cooperation.

The discussion then turns to the significance of supply chains and logistics management. In particular, attention is placed on the necessary alignment between supply chain management and marketing strategy and the trade-offs managers make between total distribution costs and customer service.

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Page 408

NATURE AND IMPORTANCE OF MARKETING CHANNELS

LO 15-1

Explain what is meant by a marketing channel of distribution and why intermediaries are needed.

Reaching prospective buyers, either directly or indirectly, is a prerequisite for successful marketing. At the same time, buyers benefit from distribution systems used by companies.

What Is a Marketing Channel of Distribution?

You see the results of distribution every day. You may have purchased Lay's potato chips at a 7-Eleven convenience store, a book online through Amazon.com, and Levi's jeans at a Kohl's department store. Each of these items was brought to you by a marketing channel of distribution, or simply a **marketing channel**, which consists of individuals and firms involved in the process of making a product or service available for use or consumption by consumers or industrial users.

Marketing channels can be compared to a pipeline through which water flows from a source to a terminus. Marketing channels make possible the flow of products and services from a producer, through intermediaries, to a buyer. Intermediaries go by

various names (see **Figure 15–1**) and perform various functions. Some intermediaries purchase items from the seller, store them, and resell them to buyers. For example, Celestial Seasonings produces specialty teas and sells them to food wholesalers. The wholesalers then sell these teas to supermarkets and grocery stores, which, in turn, sell them to consumers. Other intermediaries such as brokers and agents represent sellers but do not actually take title to products—their role is to bring a seller and buyer together. Century 21 real estate agents are examples of this type of intermediary.

TERM	DESCRIPTION
Middleman	Any intermediary between the manufacturer and end-user markets
Agent or broker	Any intermediary with legal authority to act on behalf of the manufacturer
Wholesaler	An intermediary who sells to other intermediaries, usually to retailers; term usually applies to consumer markets
Retailer	An intermediary who sells to consumers
Distributor	An imprecise term, usually used to describe intermediaries who perform a variety of distribution functions, including selling, maintaining inventories, extending credit, and so on; a more common term in business markets but may also be used to refer to wholesalers
Dealer	A more imprecise term than <i>distributor</i> that can mean the same as distributor, retailer, wholesaler, and so forth

Figure 15–1 Terms used for marketing intermediaries vary in specificity and use in consumer and business markets.

How Customer Value Is Created by Intermediaries

The importance of intermediaries is made even clearer when we consider the functions they perform and the value they create for buyers.

Important Functions Performed by Intermediaries

Intermediaries make possible the flow of products from producers to ultimate consumers by performing three basic functions (see **Figure 15–2**). Intermediaries perform a *transactional function* when they buy and sell products or services. But an intermediary such as a wholesaler

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also performs the function of sharing risk with the producer when it stocks merchandise in anticipation of sales. If the stock is unsold for any reason, the intermediary—not the producer—suffers the loss.

Page 409

TYPE OF FUNCTION	ACTIVITIES RELATED TO FUNCTION
Transactional function	<ul style="list-style-type: none"> • <i>Buying</i>: Purchasing products for resale or as an agent for supply of a product • <i>Selling</i>: Contacting potential customers, promoting products, and seeking orders • <i>Risk taking</i>: Assuming business risks in the ownership of inventory that can become obsolete or deteriorate
Logistical function	<ul style="list-style-type: none"> • <i>Assorting</i>: Creating product assortments from several sources to serve customers • <i>Storing</i>: Assembling and protecting products at a convenient location to offer better customer service • <i>Sorting</i>: Purchasing in large quantities and breaking into smaller amounts desired by customers • <i>Transporting</i>: Physically moving a product to customers
Facilitating function	<ul style="list-style-type: none"> • <i>Financing</i>: Extending credit to customers • <i>Grading</i>: Inspecting, testing, or judging products and assigning them quality grades • <i>Marketing information and research</i>: Providing information to customers and suppliers, including competitive conditions and trends

Figure 15–2 Marketing channel intermediaries perform these fundamental functions, each of which consists of different activities.

The logistics of a transaction (described at length later in this chapter) involve the details of preparing and getting a product to buyers. Gathering, sorting, and dispersing products are some of the *logistical functions* of the intermediary—imagine the several books required for a literature course sitting together on one shelf at your college bookstore! Finally, intermediaries perform *facilitating functions* that, by definition, make a transaction easier for buyers. For example, Macy's issues credit cards to consumers so they can buy now and pay later.

All three functions must be performed in a marketing channel, even though each channel member may not participate in all three. Channel members often negotiate which specific functions they will perform and for what price.

Consumer Benefits

Consumers also benefit from intermediaries. Having the products and services you want, when you want them, where you want them, and in the form you want them is the ideal result of marketing channels.

In more specific terms, marketing channels help create value for consumers through the four utilities described in **Chapter 1**: time, place, form, and possession. *Time utility* refers to having a product or service when you want it. For example, FedEx provides next-morning delivery. *Place utility* means having a product or service available where consumers want it, such as having a Chevron gas station located on a long stretch of lonely highway. *Form utility* involves enhancing a product or service to make it more appealing to buyers. Consider the importance of bottlers in the soft-drink industry. Coca-Cola and Pepsi-Cola manufacture the flavor concentrate (cola, lemon-lime) and sell it to bottlers—intermediaries—which then add sweetener and the concentrate to carbonated water and package the beverage in bottles and cans, which are then sold to retailers. *Possession utility* entails efforts by intermediaries to help buyers take possession of a product or service, such as having airline tickets delivered by a travel agency.

learning review

- 15- What is meant by a marketing channel?
 - 1.
- 15- What are the three basic functions performed by intermediaries?
 - 2.

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MARKETING CHANNEL STRUCTURE AND ORGANIZATION

LO 15-2

Distinguish among traditional marketing channels, electronic marketing channels, and different types of vertical marketing systems.

A product can take many routes on its journey from a producer to buyers. Marketers continually search for the most efficient route from the many alternatives available. As you'll see, there are some important differences between the marketing channels used for consumer products and business products.

Marketing Channels for Consumer Products and Services

Figure 15–3 shows the four most common marketing channels for consumer products and services. It also shows the number of levels in each marketing channel, as evidenced by the number of intermediaries between a producer and ultimate buyers. As the number of intermediaries between a producer and buyer increases, the channel is viewed as increasing in length. Thus, the producer → wholesaler → retailer → consumer channel is longer than the producer → consumer channel.

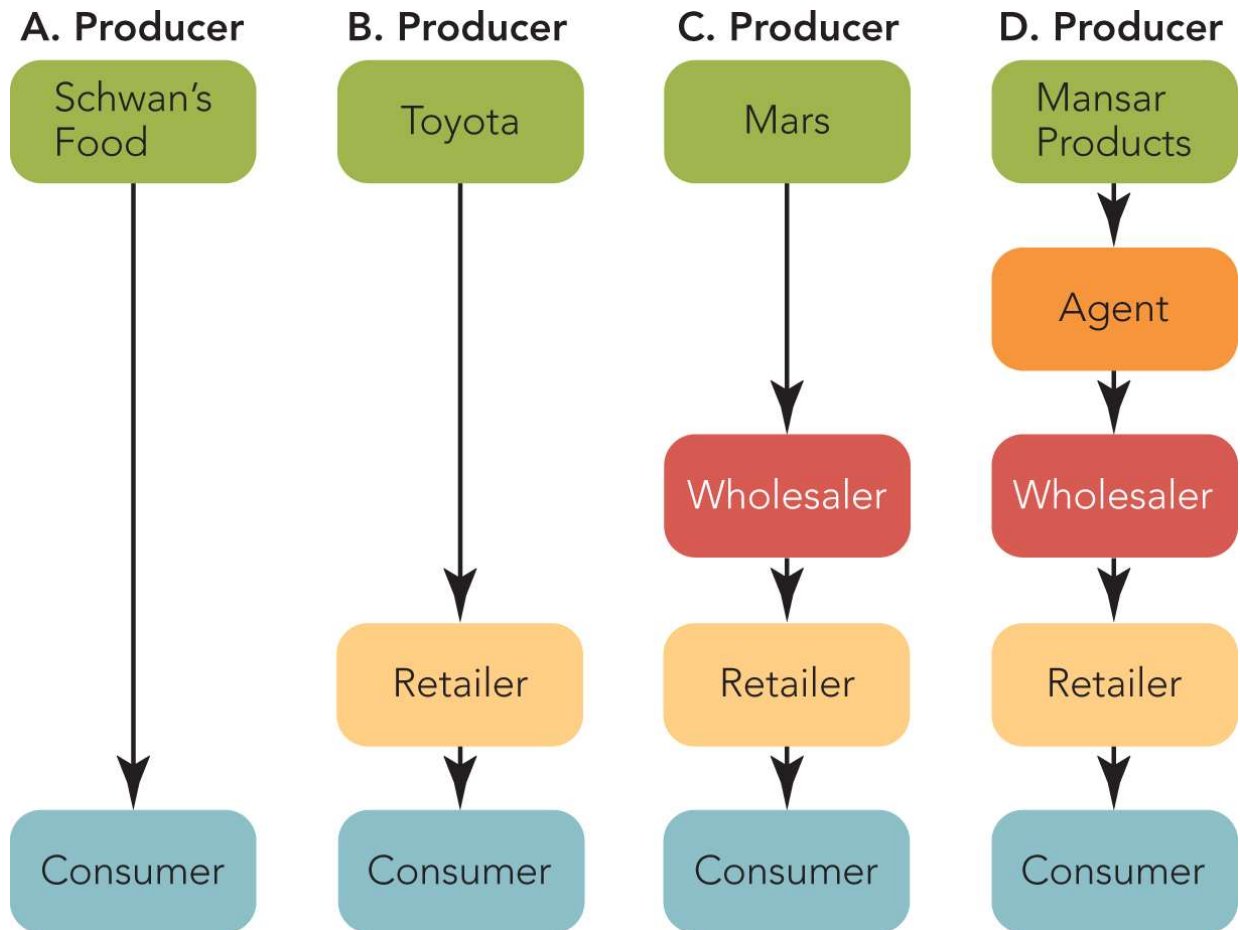


Figure 15–3 Common marketing channels for consumer products and services differ by the kind and number of intermediaries involved.

Direct Channel

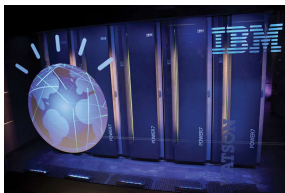
Channel A represents a *direct channel* because the producer and the ultimate consumers deal directly with each other. Many products and services are distributed this way. Many insurance companies sell their services using a direct channel and branch sales offices. The Schwan's Food Company of Marshall, Minnesota, the largest direct-to-home provider of frozen foods in the United States, uses route sales representatives who sell from refrigerated trucks. Because there are no intermediaries with a direct channel, the producer performs all channel functions.

Indirect Channel

The remaining three channel forms in **Figure 15–3** are *indirect channels* because intermediaries are inserted between the producer and consumers and perform

numerous channel functions. Channel B, with a retailer added, is most common when a retailer is large and can buy in large quantities from a producer or when the cost of inventory makes it too expensive to use a wholesaler. Automobile manufacturers such as Toyota use this channel, and a local car dealer acts as a retailer. Why is there no wholesaler? So many variations exist in the product that it would be impossible for a wholesaler to stock all the models required to satisfy buyers; in addition, the cost of maintaining an inventory would be too high. However, large retailers such as Target, 7-Eleven, Staples, Safeway, and Home Depot buy in sufficient quantities to make it cost effective for a producer to deal with only a retail intermediary.

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What kind of marketing channel does IBM use for its Watson computer—an artificially intelligent computer system capable of answering questions in natural language? Read the text to find out.

© Ben Hider/Getty Images

Adding a wholesaler in Channel C is most common for low-cost, low-unit value items that are frequently purchased by consumers, such as candy, confectionary items, and magazines. For example, Mars sells case quantities of its line of candies to wholesalers, who then break down (sort) the cases so that individual retailers can order in boxes or much smaller quantities.

Channel D, the most indirect channel, is employed when there are many small manufacturers and many small retailers; in this type of channel, an agent is used to help coordinate a large supply of the product. Mansar Products, Ltd. is a Belgian producer of specialty jewelry that uses agents to sell to wholesalers in the United States, who then sell to many small independent jewelry retailers.

Marketing Channels for Business Products and Services

The four most common channels for business products and services are shown in **Figure 15-4**. In contrast with channels used for consumer products, business channels typically are shorter and rely on one intermediary or none at all because business users are fewer in number, tend to be more concentrated geographically, and buy in larger quantities.

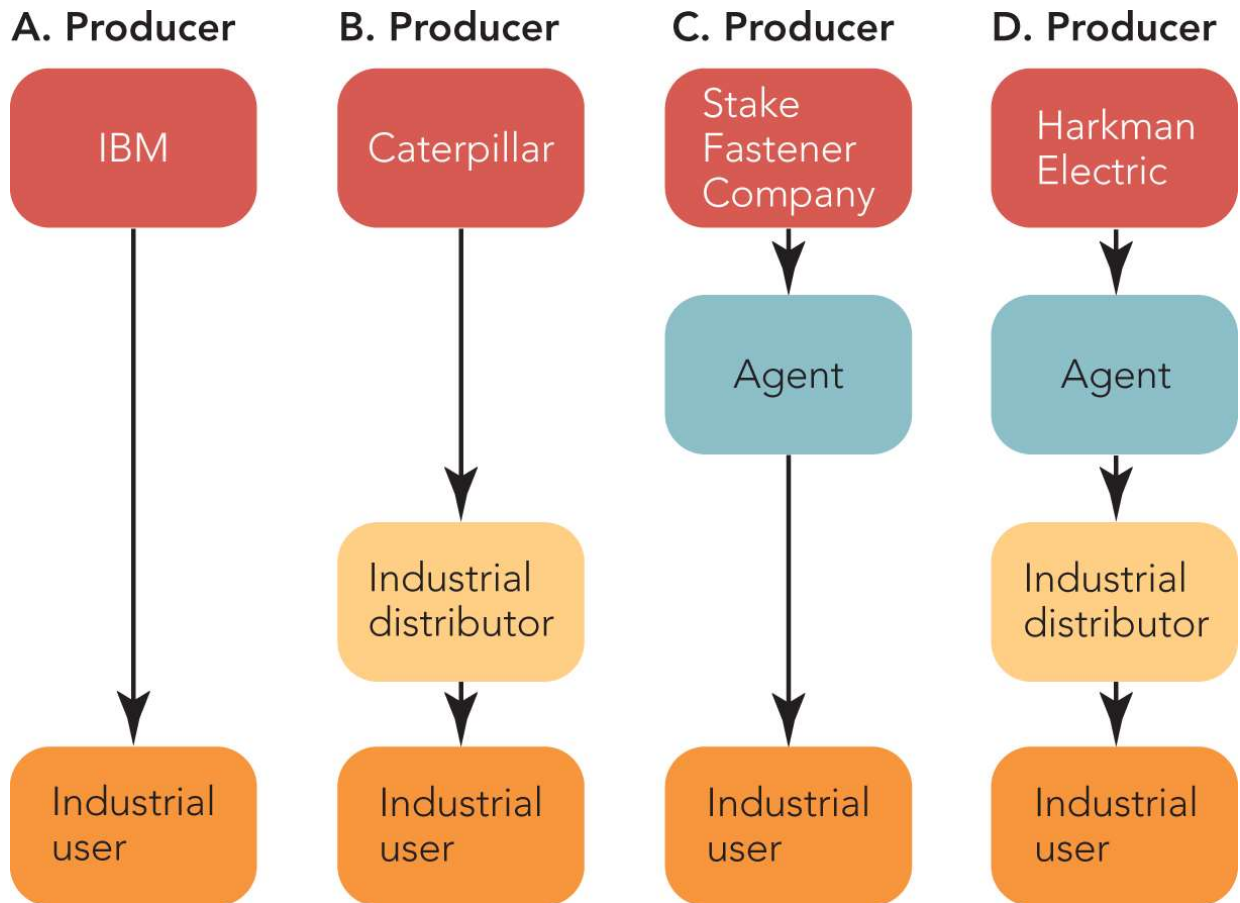


Figure 15-4 Common marketing channels for business products and services differ by the kind and number of intermediaries involved.

Direct Channel

Channel A in **Figure 15-4**, represented by IBM's large, mainframe computer business, is a direct channel. Firms using this channel maintain their own salesforce and perform all channel functions. This channel is employed when buyers are large and well defined, the sales effort requires extensive negotiations, and the products are of high unit value and require hands-on expertise in terms of installation or use. Not surprisingly, IBM's Watson supercomputer, priced at \$3 million, is sold and delivered directly to buyers.

Indirect Channel

Channels B, C, and D in **Figure 15-4** are indirect channels with one or more intermediaries between the producer and the industrial user. In Channel B, an industrial

distributor performs a variety of marketing channel functions, including selling, stocking, delivering a full product assortment, and financing. In many

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ways, industrial distributors are like wholesalers in consumer channels.

Page 412

Caterpillar uses industrial distributors to sell its construction and mining equipment in over 180 countries. In addition to selling, Caterpillar distributors stock 40,000 to 50,000 parts and service equipment using highly trained technicians.

Channel C introduces a second intermediary, an agent, who serves primarily as the independent selling arm of producers and represents a producer to industrial users. For example, Stake Fastener Company, a producer of industrial fasteners, has an agent call on industrial users rather than employing its own salesforce.

Channel D is the longest channel and includes both agents and industrial distributors. For instance, Harkman Electric, a producer of electric products, uses agents to call on electrical distributors who sell to industrial users.

Internet Marketing Channels

These common marketing channels for consumer and business products and services are not the only routes to the marketplace. *Internet marketing channels* also make products and services available for consumption or use by consumers or organizational buyers. A unique feature of these channels is that they combine electronic and traditional intermediaries to create time, place, form, and possession utility for buyers.

Figure 15–5 shows the Internet marketing channels for books (Amazon.com), automobiles (Autobytel.com), reservation services (Orbitz.com), and personal computers (Dell.com). Are you surprised that they look a lot like common consumer product marketing channels? An important reason for the similarity resides in the channel functions detailed in **Figure 15–2**. Electronic intermediaries can and do

perform transactional and facilitating functions effectively and at a relatively lower cost than traditional intermediaries because of efficiencies made possible by Internet technology. But electronic intermediaries are incapable of performing elements of the logistical function, particularly for products such as books and automobiles. This function remains with traditional intermediaries or with the producer, as is evident with Dell Inc. and its direct channel.

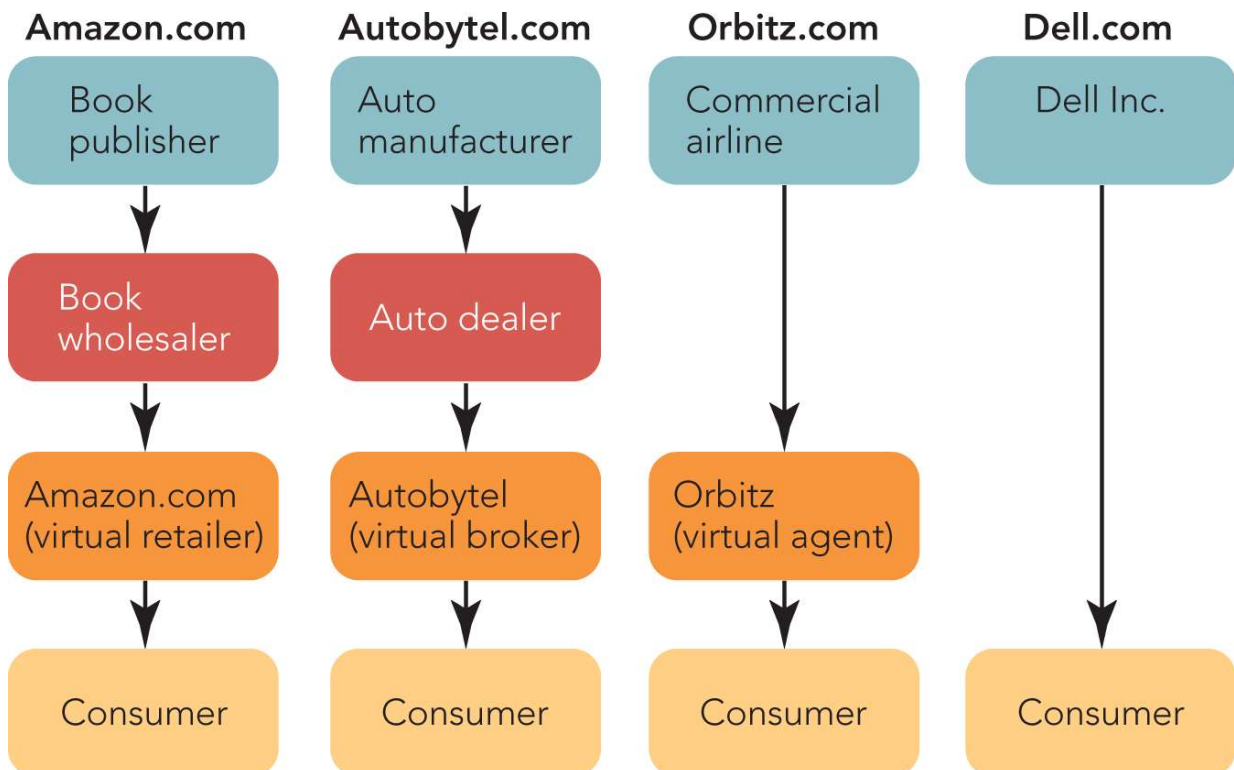


Figure 15–5 Consumer Internet marketing channels look much like those for consumer products and services. Read the text to learn why.

Many services can be distributed through electronic marketing channels, such as car rental reservations marketed by Alamo.com, financial securities by Schwab.com, and insurance by MetLife.com. However, many other services, such as health care and auto repair, still involve traditional intermediaries.



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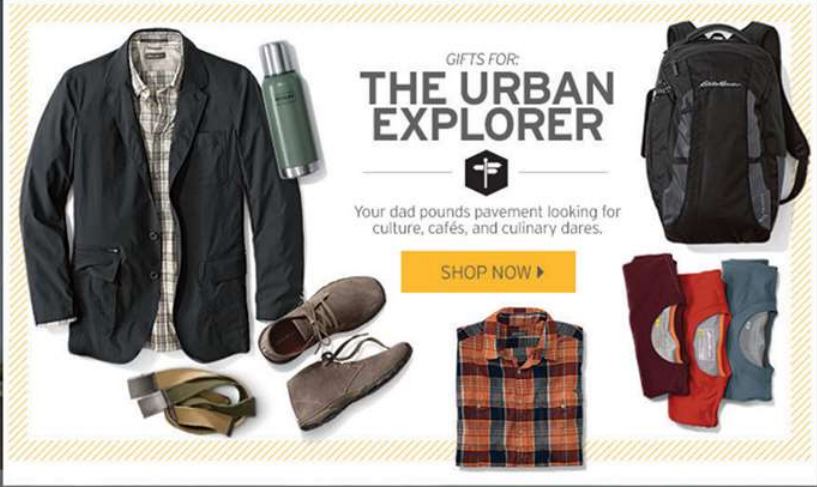
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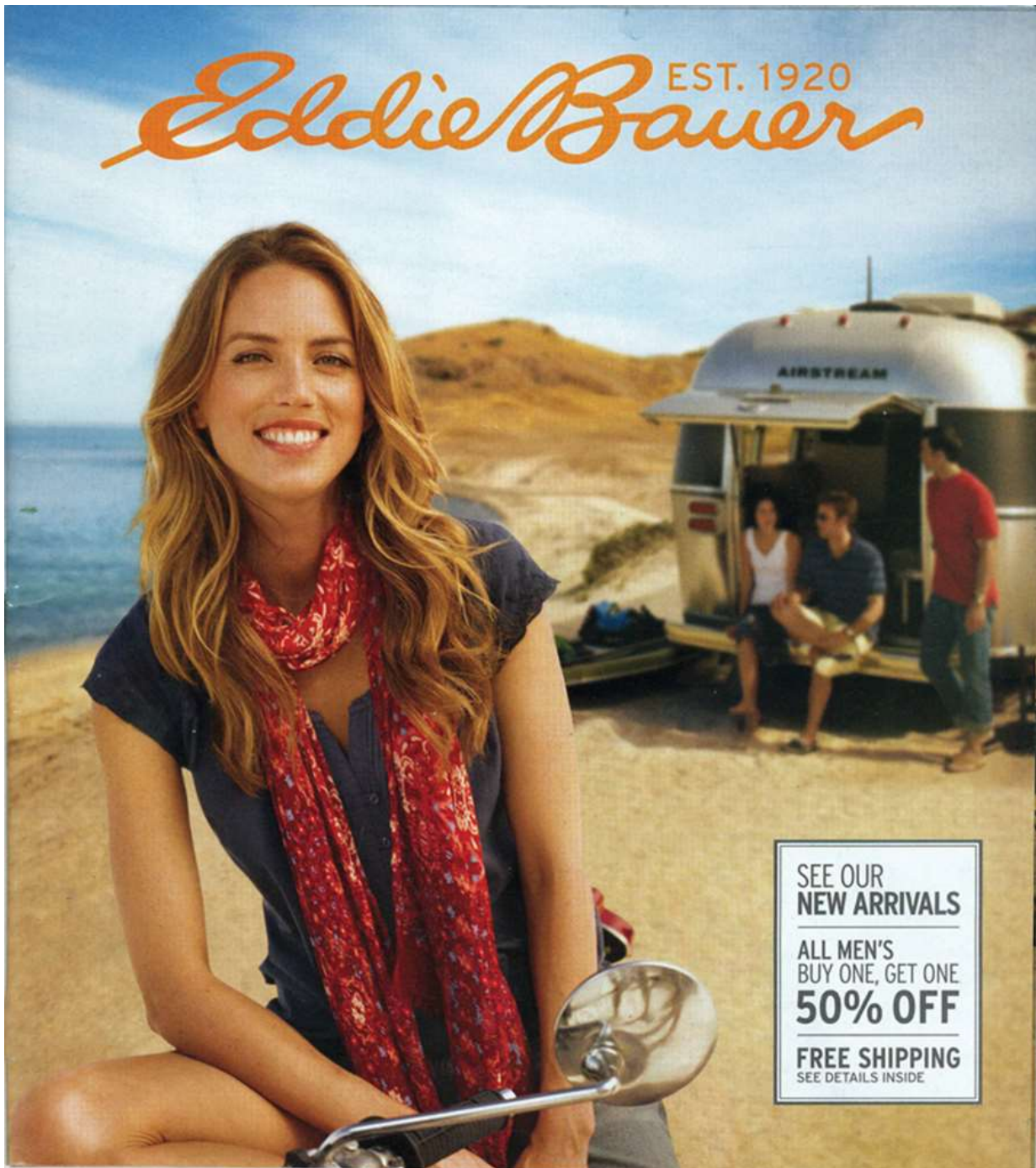
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Eddie Bauer successfully engages in multichannel marketing through its 370 retail and outlet stores, its website, and its catalog.

Left: © Bonnie Kamin/PhotoEdit, Inc.; Middle: Source: Eddie Bauer, LLC; Right: © Mike Hruby

Eddie Bauer

www.eddiebauer.com

Direct and Multichannel Marketing

Many firms also use direct and multichannel marketing to reach buyers. *Direct marketing channels* allow consumers to buy products by interacting with various advertising media without a face-to-face meeting with a salesperson. Direct marketing channels include mail-order selling, direct-mail sales, catalog sales, telemarketing, interactive media, and televised home shopping (the Home Shopping Network). Some firms sell products almost entirely through direct marketing. These firms include L.L.Bean (apparel) and Newegg.com (consumer electronics). Marketers such as Nestlé, in addition to using traditional channels composed of wholesalers and retailers, also employ direct marketing through catalogs and telemarketing to reach more buyers.

Multichannel marketing, sometimes called *omnichannel marketing*, is the *blending* of different communication and delivery channels that are *mutually reinforcing* in attracting, retaining, and building relationships with consumers who shop and buy in traditional intermediaries and online. Multichannel marketing seeks to integrate a firm's electronic marketing and delivery channels. At Eddie Bauer, for example, every effort is made to make the apparel shopping and purchase experience for its customers the same across its retail store, catalog, and website channels. According to an Eddie Bauer marketing manager, "We don't distinguish between channels because it's all Eddie Bauer to our customers."²

Multichannel marketing also can leverage the value-adding capabilities of different channels. For example, retail stores leverage their physical presence by allowing customers to pick up their online orders at a nearby store or return or exchange nonstore purchases if they wish. Catalogs can serve as shopping tools for online purchasing, as they do for store purchasing. Websites can help consumers do their homework before visiting a store. Staples has leveraged its store, catalog, and website channels with impressive results. Staples is the third largest Internet retailer in the United States behind Amazon and Apple.³

Dual Distribution and Strategic Channel Alliances

In some situations, producers use **dual distribution**, an arrangement whereby a firm reaches different buyers by employing two or more different types of channels for the same basic product. For example, GE sells its large appliances directly to home and apartment builders but uses retail stores, including Lowe's home centers, to sell to consumers. In some instances, firms pair multiple channels with a multibrand strategy (see **Chapter 10**). This is done to minimize cannibalization of the firm's family brand

and differentiate the channels. For example, Hallmark sells its Hallmark greeting cards through Hallmark stores and select department stores and its Ambassador brand of cards through discount and drugstore chains.

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VIDEO 15-1

Honey Nut Cheerios Ad

kerin.tv/13e/v15-1

An innovation in marketing channels is the use of *strategic channel alliances*, whereby one firm's marketing channel is used to sell another firm's products. Strategic alliances are popular in global marketing, where the creation of marketing channel relationships is expensive and time-consuming. For example, General Mills and Nestlé have an extensive alliance that spans about 140 international markets from Mexico to China. Read the Marketing Matters box so you won't be surprised when you are served Nestlé (not General Mills) Cheerios when traveling outside North America.⁴

Marketing Matters

customer
value

Nestlé and General Mills—Cereal Partners Worldwide

Can you say Nestlé Cheerios *miel amandes*? Millions in France start their day with this European equivalent of General Mills's Honey Nut Cheerios, made possible by Cereal Partners Worldwide (CPW). CPW is a strategic alliance designed from the start to be a global business. It combines the cereal manufacturing and marketing

capability of U.S.-based General Mills with the worldwide distribution clout of Swiss-based Nestlé. The photo shows Nestlé's Trix cereal (not General Mills) sold in China.

From its headquarters in Switzerland, CPW first launched General Mills cereals under the Nestlé label in France, the United Kingdom, Spain, and Portugal in 1991. Today, CPW competes in more than 140 international markets.

The General Mills–Nestlé strategic channel alliance also increased the ready-to-eat cereal worldwide market share of these companies, which are already rated as the two best-managed firms in the world. CPW currently accounts for more than 10 percent of the nearly \$30 billion worldwide hot- and cold-cereal market, with more than \$4 billion in annual revenue.



© picture alliance/Daniel Kalker/Newscom

Vertical Marketing Systems

The traditional marketing channels described so far represent a loosely knit network of independent producers and intermediaries brought together to distribute products and services. However, other channel arrangements exist for the purpose of improving efficiency in performing channel functions and achieving greater marketing effectiveness. These arrangements are called vertical marketing systems. **Vertical marketing systems** are professionally managed and centrally coordinated marketing channels designed to achieve channel economies and maximum marketing impact. **Figure 15–6** depicts the three major types of vertical marketing systems: corporate, contractual, and administered.

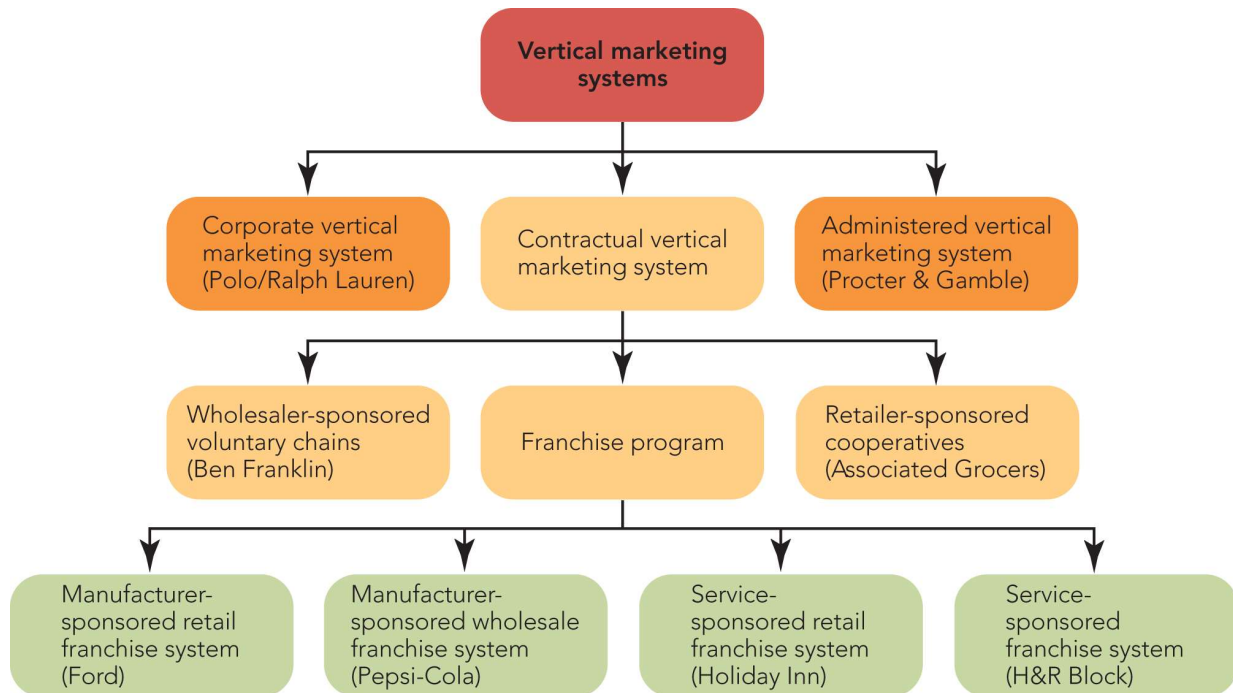


Figure 15–6 There are three major types of vertical marketing systems—corporate, contractual, and administered. Contractual systems are the most popular for reasons described in the text.

Corporate Systems

The combination of successive stages of production and distribution under a single ownership is a *corporate vertical marketing system*. For example, a producer might own the intermediary at the next level down in the channel. This practice, called *forward integration*, is exemplified by Ralph Lauren, which manufactures clothing and also owns apparel shops. Other examples of forward integration include Goodyear, Apple, and Sherwin-Williams. Alternatively, a retailer might own a manufacturing operation, a practice called *backward integration*. For example, Kroger supermarkets operate manufacturing facilities that produce everything from aspirin to cottage cheese for sale under the Kroger label. Tiffany & Co., the exclusive jewelry retailer, manufactures about half of the fine jewelry items for sale through its over 250 specialty stores and boutiques worldwide.

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Companies seeking to reduce distribution costs and gain greater control over supply sources or resale of their products pursue forward and backward integration. However, both types of integration increase a company's capital investment and fixed costs. For this reason, many companies favor contractual vertical marketing systems to achieve channel efficiencies and marketing effectiveness.

Page 415

Contractual Systems

Under a *contractual vertical marketing system*, independent production and distribution firms integrate their efforts on a contractual basis to obtain greater functional economies and marketing impact than they could achieve alone. Contractual systems are the most popular among the three types of vertical marketing systems.

Three variations of contractual systems exist. *Wholesaler-sponsored voluntary chains* involve a wholesaler that develops a contractual relationship with small, independent retailers to standardize and coordinate buying practices, merchandising programs, and inventory management efforts. With the organization of a large number of independent retailers, economies of scale and volume discounts can be achieved to compete with chain stores. IGA and Ben Franklin variety and craft stores represent wholesaler-sponsored voluntary chains. *Retailer-sponsored cooperatives* exist when small, independent retailers form an organization that operates a wholesale facility cooperatively. Member retailers then concentrate their buying power through the wholesaler and plan collaborative promotional and pricing activities. Examples of retailer-sponsored cooperatives include Associated Grocers and Ace Hardware.

The most visible variation of contractual systems is franchising. *Franchising* is a contractual arrangement between a parent company (a franchisor) and an individual or firm (a franchisee) that allows the franchisee to operate a certain type of business under an established name and according to specific rules.

Four types of franchise arrangements are most popular. *Manufacturer-sponsored retail franchise systems* are prominent in the automobile industry, where a manufacturer such as Ford licenses dealers to sell its cars subject to various sales and service conditions. *Manufacturer-sponsored wholesale franchise systems* exist in the soft-drink industry. For example, Pepsi-Cola licenses wholesalers (bottlers) that purchase concentrate from Pepsi-Cola and then carbonate, bottle, promote, and distribute its products to retailers and restaurants. *Service-sponsored retail franchise systems* are used by firms that have designed a unique approach for performing a service and wish

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to profit by selling the franchise to others. Holiday Inn, Avis, and McDonald's represent this type of franchising approach. *Service-sponsored franchise systems* exist when franchisors license individuals or firms to dispense a service under a trade name and according to specific guidelines. Examples include Snelling and Snelling, Inc. employment services and H&R Block tax services. Page 416

Administered Systems

In comparison, *administered vertical marketing systems* achieve coordination at successive stages of production and distribution by the size and influence of one channel member rather than through ownership. Procter & Gamble, given its broad product assortment ranging from disposable diapers to detergents, is able to obtain cooperation from supermarkets in displaying, promoting, and pricing its products. Walmart obtains cooperation from manufacturers in terms of product specifications, price levels, and promotional support due to its position as the world's largest retailer.

learning review

- 15- What is the difference between a direct and an indirect channel?
 - 3.
- 15- Why are channels for business products typically shorter than
 - 4. channels for consumer products?
- 15- What is the principal distinction between a corporate vertical
 - 5. marketing system and an administered vertical marketing system?

MARKETING CHANNEL CHOICE AND MANAGEMENT

LO 15-3

Describe factors that marketing executives consider when selecting and managing a marketing channel, including legal restrictions.

Marketing channels not only link a producer to its buyers but also provide the means through which a firm implements various elements of its marketing strategy. Therefore, choosing a marketing channel is a critical decision.

Factors Affecting Channel Choice and Management

Marketing executives consider three questions when choosing a marketing channel and intermediaries:

1. Which channel and intermediaries will provide the best coverage of the target market?
2. Which channel and intermediaries will best satisfy the buying requirements of the target market?
3. Which channel and intermediaries will be the most profitable?

Target Market Coverage

Achieving the best coverage of the target market requires attention to the *density*—that is, the number of stores in a geographical area—and type of intermediaries to be used at the retail level of distribution. Three degrees of distribution density exist: intensive, exclusive, and selective.

Intensive distribution means that a firm tries to place its products and services in as many outlets as possible. Intensive distribution is usually chosen for convenience products or services such as candy, fast food, newspapers, and soft drinks. For example, Coca-Cola's retail distribution objective is to place its products "within an arm's reach of desire." Cash, yes cash, is distributed intensively by Visa. It operates over 1.4 million automated teller machines in more than 200 countries.

Exclusive distribution is the extreme opposite of intensive distribution because only one retailer in a specific geographical area carries the firm's products. Exclusive distribution is typically chosen for specialty products or services, such as some women's fragrances and men's and women's apparel and accessories. Gucci, one of the world's leading luxury products companies, uses exclusive distribution in the marketing of its Yves Saint Laurent, Sergio Rossi, Boucheron, Opium, and Gucci brands.

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Retailers and industrial distributors prefer exclusive distribution for two reasons. First, it limits head-to-head competition for an identical product.

Page 417

Second, it provides a point of difference for a retailer or distributor. For instance, luxury retailer Saks Inc. seeks exclusive product lines for its stores. According to the company CEO, "It's incumbent on us not to be just a place where you can buy the big brands. Those brands are still critical—the Chanel's, the Prada's, the Gucci's—but even with those brands, we need to find things unique to us."⁶

Selective distribution lies between these two extremes and means that a firm selects a few retailers in a specific geographical area to carry its products. Selective distribution weds some of the market coverage benefits of intensive distribution to the control over resale evident with exclusive distribution. For example, Dell Inc. chose selective distribution when it decided to sell its products through U.S. retailers along with its direct channel.⁷ According to Michael Dell, the company CEO, "There were plenty of retailers who said, 'sell through us,' but we didn't want to show up everywhere." The company now sells a limited range of its products through Walmart, Sam's Club, Best Buy, and Staples. Dell's decision was consistent with current trends. Today, selective distribution is the most common form of distribution intensity.

Buyer Requirements

A second consideration in channel choice is gaining access to channels and intermediaries that satisfy at least some of the interests buyers might want fulfilled when they purchase a firm's products or services. These interests fall into four broad categories: (1) information, (2) convenience, (3) variety, and (4) pre- or postsale services. Each relates to customer experience.

Information is an important requirement when buyers have limited knowledge or desire specific data about a product or service. Properly chosen intermediaries communicate with buyers through in-store displays, demonstrations, and personal selling. Apple has opened over 400 retail outlets staffed with highly trained personnel to communicate how its products can better satisfy each customer's needs.



Which buying requirements are satisfied by Jiffy Lube? Read the text to find out.

© David McNew/Getty Images

Convenience has multiple meanings for buyers, such as proximity or driving time to a retail outlet. For example, 7-Eleven stores, with more than 50,000 outlets worldwide, many of which are open 24 hours a day, satisfy this interest for buyers. Candy and snack-food firms benefit by gaining display space in these

stores. For other consumers, convenience means a minimum of time and hassle. Jiffy Lube, which promises to change engine oil and filters quickly, appeals to this aspect of convenience. For those who shop on the Internet, convenience means that websites must be easy to locate and navigate, and image downloads must be fast. A commonly held view among website developers is the “eight second rule”: Consumers will abandon their efforts to enter or navigate a website if download time exceeds eight seconds.⁸

Variety reflects buyers' interest in having numerous competing and complementary items from which to choose. Variety is evident in the breadth and depth of products and brands carried by intermediaries, which enhances their attraction to buyers. Thus, manufacturers of pet food and supplies seek distribution through pet superstores such as Petco and PetSmart, which offer a wide array of pet products and services.

Pre- or postsale services provided by intermediaries are an important buying requirement for products such as large household appliances that require delivery, installation, and credit. Therefore, Whirlpool seeks dealers that provide such services.

Profitability

The third consideration in choosing a channel is profitability, which is determined by the margins earned (revenue minus cost) for each channel member and for the channel as a whole. Channel cost is the critical dimension of profitability.

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These costs include distribution, advertising, and selling expenses associated with different types of marketing channels. The extent to which channel members share these costs determines the margins received by each member and by the channel as a whole. Page 418

Companies routinely monitor the performance of their marketing channels. Read the Applying Marketing Metrics box to see how Charlesburg Furniture views the sales and profit performance of its marketing channels.

Applying Marketing Metrics

Channel Sales and Profit at Charlesburg Furniture

Charlesburg Furniture is one of 1,000 wood furniture manufacturers in the United States. The company sells its furniture through furniture store chains, independent furniture stores, and department store chains, mostly in the southern United States. The company has traditionally allocated its marketing funds for cooperative advertising, in-store displays, and retail sales support on the basis of dollar sales by channel.

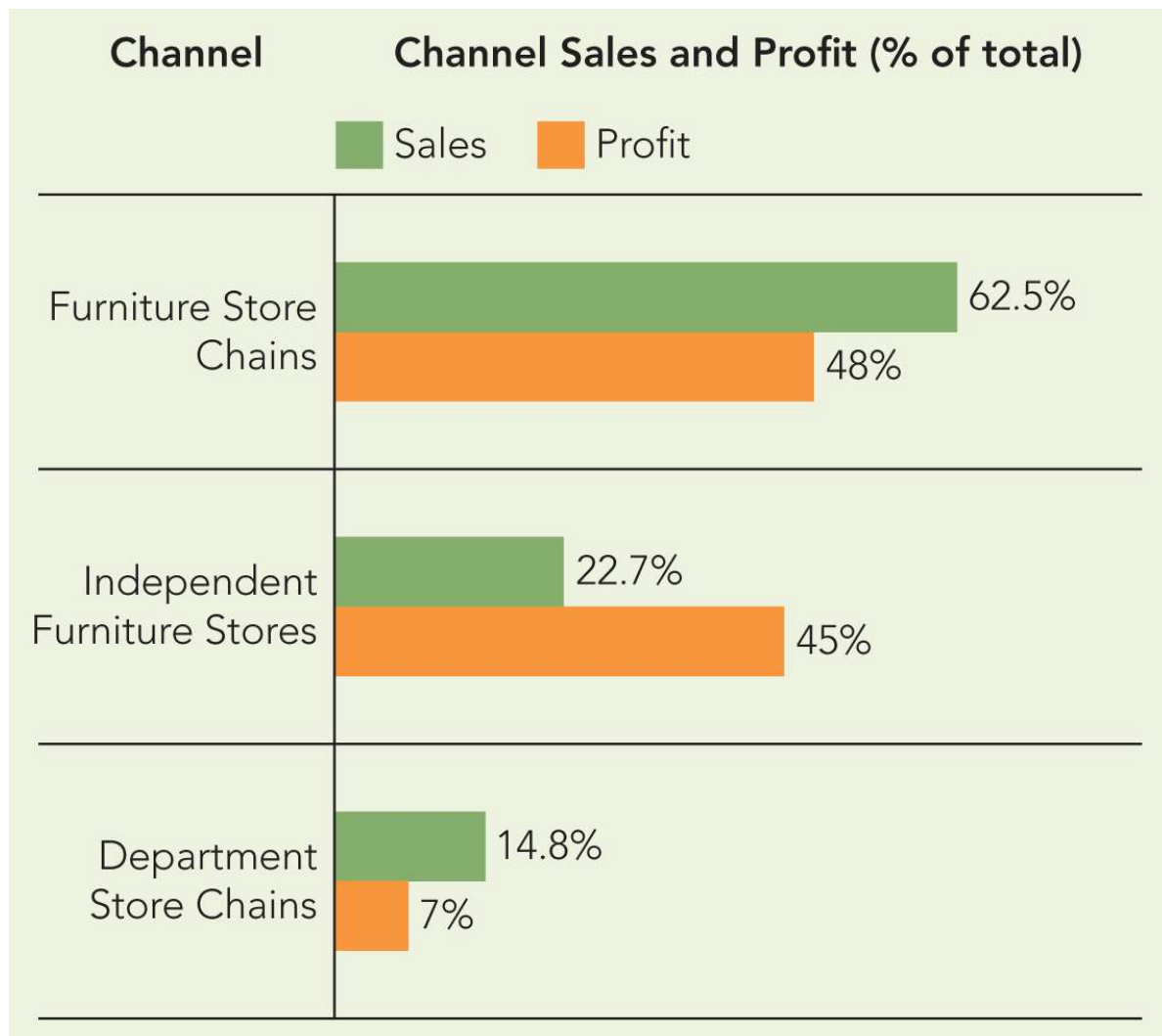
Your Challenge

As the vice president of sales and marketing at Charlesburg Furniture, you have been asked to review the company's sales and profit in its three channels and recommend a

course of action. The question: Should Charlesburg Furniture continue to allocate its marketing funds on the basis of channel dollar sales or profit?

Your Findings

Charlesburg Furniture tracks the sales and profit from each channel (and individual customer) and the three-year trend of sales by channel on its marketing dashboard. This information is displayed in the marketing dashboards below.

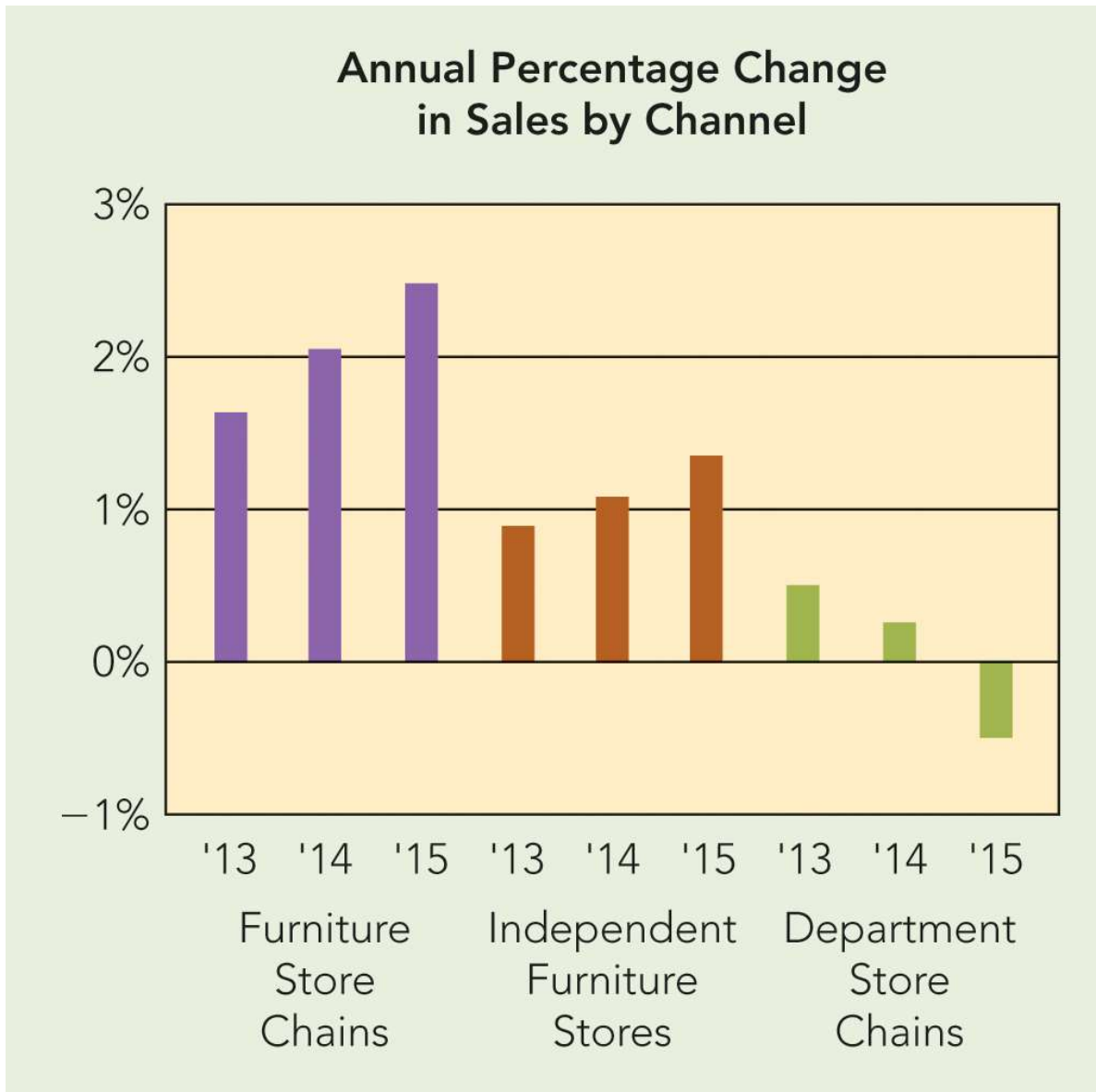


Several findings stand out. Furniture store chains and independent furniture stores account for 85.2 percent of Charlesburg Furniture sales and 93 percent of company profit. These two channels also evidence growth as measured by annual percentage change in sales. By comparison, the annual percentage sales growth of department

store chains has declined, recording negative growth in 2015. This channel accounts for 14.8 percent of company sales and 7 percent of company profit.

Your Action

Charlesburg Furniture should consider abandoning the practice of allocating marketing funds solely on the basis of channel sales volume. The importance of independent furniture stores to Charlesburg's profitability warrants further spending, particularly given this channel's favorable sales trend. Doubling the percentage allocation for marketing funds for this channel may be too extreme, however. Charlesburg Furniture might also consider the longer term role of department store chains as a marketing channel.



Managing Channel Relationships: Conflict and Cooperation

Unfortunately, because channels consist of independent individuals and firms, there is always the potential for disagreements concerning who performs which channel

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functions, how profits are allocated, which products and services will be provided by whom, and who makes critical channel-related decisions. These channel conflicts necessitate measures for dealing with them.

Page 419

Sources of Conflict in Marketing Channels

Channel conflict arises when one channel member believes another channel member is engaged in behavior that prevents it from achieving its goals. Two types of conflict occur in marketing channels: vertical conflict and horizontal conflict.

Vertical conflict occurs between different levels in a marketing channel—for example, between a manufacturer and a wholesaler or retailer or between a wholesaler and a retailer. Three sources of vertical conflict are most common.⁹ First, conflict arises when a channel member bypasses another member and sells or buys products direct, a practice called **disintermediation**. For example, conflict occurred when American Airlines decided to terminate its relationship with Orbitz and Expedia, two online ticketing and travel sites, and sell directly through AA Direct Connect. Second, conflict occurs due to disagreements over how profit margins are distributed among channel members. This happened when Amazon and the Hachette Book Group, the third-largest trade book and educational publisher, engaged in a seven-month dispute about how e-book revenue should be divided between the two companies. A third conflict situation arises when manufacturers believe wholesalers or retailers are not giving their products adequate attention. For example, Nike stopped shipping popular sneakers such as Nike Shox NZ to Foot Locker in retaliation for the retailer's decision to give more shelf space to shoes costing under \$120.



Channel conflict is sometimes visible to consumers. Read the text to learn what type of channel conflict has antagonized this independent Goodyear tire dealer.

© Joe & Kathy Heiner/Lindgren & Smith, Inc.

Horizontal conflict occurs between intermediaries at the same level in a marketing channel, such as between two or more retailers (Target and Kmart) or two or more wholesalers that handle the same manufacturer's brands. Two sources of horizontal conflict are common.¹⁰ First, horizontal conflict arises when a manufacturer increases its distribution coverage in a geographical area. For example, a franchised Cadillac dealer in Chicago might complain to

General Motors that another franchised Cadillac dealer has located too close to its dealership. Second, dual distribution causes conflict when different types of retailers carry the same brands. For instance, independent Goodyear tire dealers became irate when Goodyear Tire Company decided to sell its brands through Sears, Walmart, and Sam's Club. Many switched to competing tire makers.

Securing Cooperation in Marketing Channels

Conflict can have destructive effects on the workings of a marketing channel so it is necessary to secure cooperation among channel members. One means is through a *channel captain*, a channel member that coordinates, directs, and supports other channel members. Channel captains can be producers, wholesalers, or retailers. P&G assumes this role because it has a strong consumer following in brands such as Crest, Tide, and Pampers. Therefore, it can set policies or terms that supermarkets will follow. McKesson, a pharmaceutical drug wholesaler, is a channel captain because it coordinates and supports the product flow from numerous small drug manufacturers to drugstores and hospitals nationwide. Walmart is a retail channel captain because of its strong consumer image, number of outlets, and purchasing volume.

A firm becomes a channel captain because it is the channel member with the ability to influence the behavior of other members. Influence can take four forms.

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First, economic influence arises from the ability of a firm to *reward* other members given its strong financial position or customer franchise. Microsoft Corporation and Walmart have such influence. *Expertise* is a second source of influence. For example, American Hospital Supply helps its customers (hospitals) manage inventory and streamline order processing for hundreds of medical supplies. Third, *identification* with a particular channel member can create influence for that channel member. For instance, retailers may compete to carry the Ralph Lauren line, or clothing manufacturers may compete to be carried by Neiman Marcus, Nordstrom, or Bloomingdale's. In both instances, the desire to be identified with a channel member gives that firm influence over others. Finally, influence can arise from the *legitimate right* of one channel member to direct the behavior of other members. This situation is likely to occur in contractual vertical marketing systems where a franchisor can legitimately direct how a franchisee behaves.

Page 420

Legal Considerations

Conflict in marketing channels is typically resolved through negotiation or the exercise of influence by channel members. Sometimes conflict produces legal action. Therefore, knowledge of legal restrictions affecting channel strategies and practices is important. Some restrictions were described in **Chapter 14**, namely vertical price fixing and price discrimination. However, other legal considerations are unique to marketing channels.

In general, suppliers can select whomever they want as channel intermediaries and may refuse to deal with whomever they choose. However, the Federal Trade Commission and the Justice Department monitor channel practices that restrain competition, create monopolies, or otherwise represent unfair methods of competition under the Sherman

Act (1890) and the Clayton Act (1914). Six channel practices have received the most attention (see **Figure 15-7**).

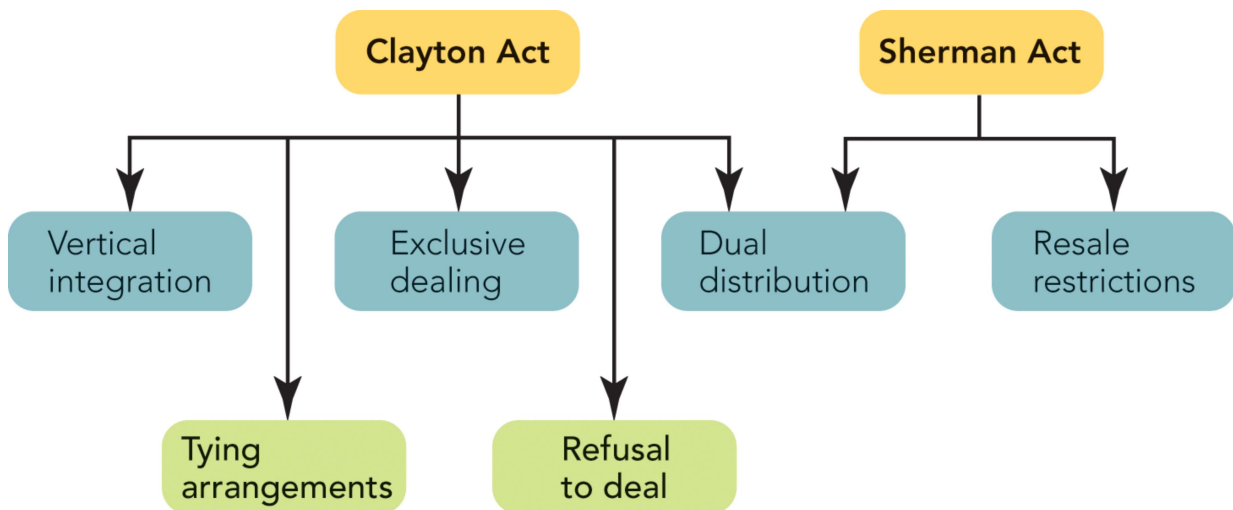


Figure 15-7 Channel strategies and practices are affected by legal restrictions. The Clayton Act and the Sherman Act restrict specific channel strategies and practices.

Dual distribution, although not illegal, can be viewed as anticompetitive in some situations. The most common situation arises when a manufacturer distributes through its own vertically integrated channel in competition with independent wholesalers and retailers that also sell its products. If the manufacturer's behavior is viewed as an attempt to lessen competition by eliminating wholesalers or retailers, then such action would violate both the Sherman and Clayton Acts.

Vertical integration is viewed in a similar light. Although not illegal, this practice is sometimes subject to legal action under the Clayton Act if it has the potential to lessen competition or foster monopoly.

The Clayton Act specifically prohibits exclusive dealing and tying arrangements when they lessen competition or create monopolies. *Exclusive dealing* exists when a supplier requires channel members to sell only its products or restricts distributors from selling directly competitive products. *Tying arrangements* occur when a supplier requires a distributor purchasing some products to buy others from the supplier. These arrangements often arise in franchising. They are illegal if the tied products could be purchased at fair market values from other suppliers at desired quality standards of the

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franchiser. *Full-line forcing* is a special kind of tying arrangement. This practice involves a supplier requiring that a channel member carry its full line of products in order to sell a specific item in the supplier's line.

Page 421

Even though a supplier has a legal right to choose intermediaries to carry and represent its products, a *refusal to deal* with existing channel members may be illegal under the Clayton Act. *Resale restrictions* refer to a supplier's attempt to stipulate to whom distributors may resell the supplier's products and in what specific geographical areas or territories they may be sold. These practices have been prosecuted under the Sherman Act. Today, however, the courts apply the "rule of reason" in such cases and consider whether such restrictions have a "demonstrable economic effect."

learning review

- 15- What are the three questions marketing executives consider
6. when choosing a marketing channel and intermediaries?
- 15- What are the three degrees of distribution density?
- 7.
- 15- What is meant by exclusive dealing?
- 8.

LOGISTICS AND SUPPLY CHAIN MANAGEMENT

LO 15-4

Explain what supply chain and logistics management are and how they relate to marketing strategy.

A marketing channel relies on logistics to make products available to consumers and industrial users. **Logistics** involves those activities that focus on getting the right amount of the right products to the right place at the right time at the lowest possible cost. The performance of these activities is *logistics management*, the practice of organizing the cost-effective flow of raw materials, in-process inventory, finished goods, and related

information from point of origin to point of consumption to satisfy *customer requirements*.

Three elements of this definition deserve emphasis. First, logistics deals with decisions needed to move a product from the source of raw materials to consumption—that is, the *flow* of the product. Second, those decisions have to be *cost effective*. Third, while it is important to drive down logistics costs, there is a limit: A firm needs to drive down logistics costs as long as it can deliver expected *customer service*, which means satisfying customer requirements. The role of management is to see that customer needs are satisfied in the most cost-effective manner. When properly done, the results can be spectacular. Consider Procter & Gamble. The company set out to meet consumer needs more effectively by collaborating and partnering with its suppliers and retailers to ensure that the right products reached store shelves at the right time and at a lower cost. The effort was judged a success when, during an 18-month period, P&G's retail customers posted a \$65 million savings in logistics costs and customer service increased.

11

The P&G experience is not an isolated incident. Companies now recognize that getting the right items needed for consumption or production to the right place at the right time in the right condition at the right cost is often beyond their individual capabilities and control. Instead, collaboration, coordination, and information sharing among manufacturers, suppliers, and distributors are necessary to create a seamless flow of products and services to customers. This perspective is represented in the concept of a supply chain and the practice of supply chain management.

Supply Chains versus Marketing Channels

A **supply chain** refers to the various firms involved in performing the activities required to create and deliver a product or service to consumers or industrial users. It

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differs from a marketing channel in terms of the firms involved. A supply chain includes suppliers that provide raw material inputs to a manufacturer as well as the wholesalers and retailers that deliver finished products to consumers. The management process is also different.

Page 422

Supply chain management is the integration and organization of information and logistics activities *across firms* in a supply chain for the purpose of creating and delivering products and services that provide value to consumers. The relation among marketing channels, logistics management, and supply chain management is shown in **Figure 15–8**. An important feature of supply chain management is its application of sophisticated information technology that allows companies to share and operate systems for order processing, transportation scheduling, and inventory and facility management.

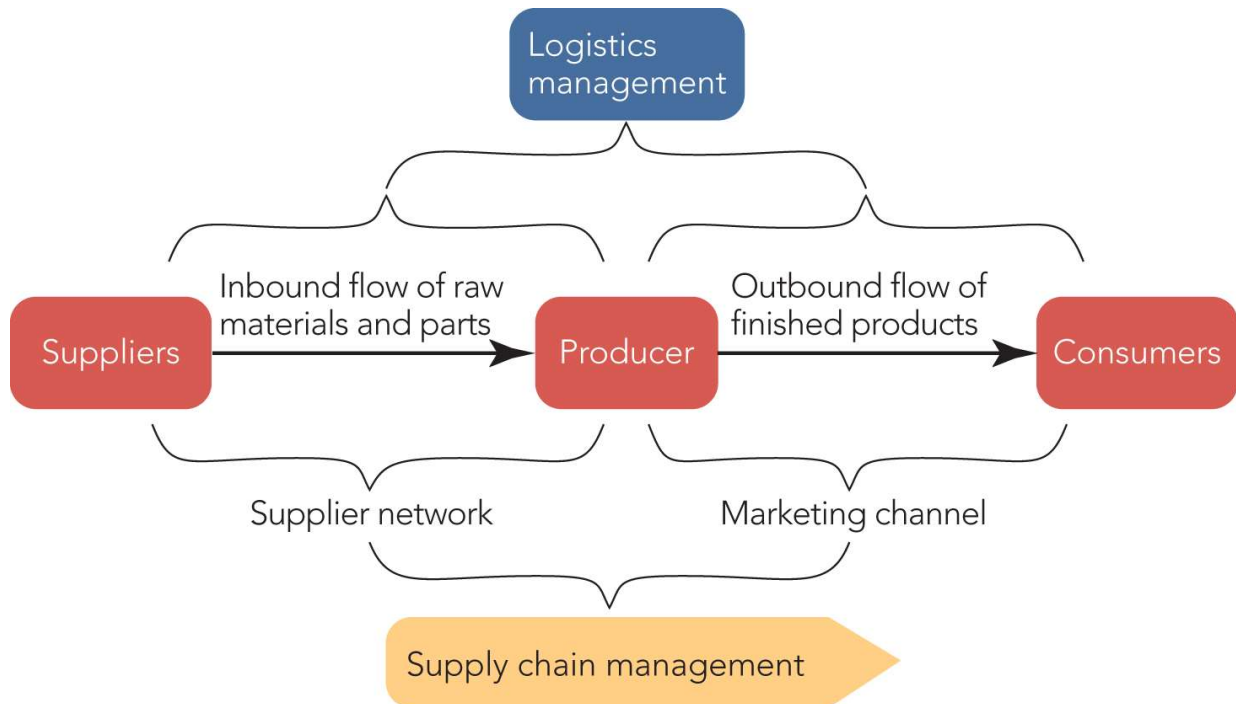


Figure 15–8 Relating logistics management and supply chain management to supplier networks and marketing channels.

Sourcing, Assembling, and Delivering a New Car: The Automotive Supply Chain

All companies are members of one or more supply chains. A supply chain is essentially a series of linked suppliers and customers in which every customer is, in turn, a supplier to another customer until a finished product reaches the ultimate consumer. Even the simplified supply chain diagram for carmakers shown in **Figure 15–9** illustrates how complex a supply chain can be.¹² A carmaker's supplier network includes thousands of firms that provide the 2,000 functional components, 30,000 parts, and 10 million lines of software code in a typical automobile. They provide items ranging from raw materials, such as steel and rubber, to components, including transmissions, tires, brakes, and seats, to complex subassemblies such as chassis and suspension

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systems that make for a smooth, stable ride. The process of coordinating and scheduling the flow of materials and components for their assembly into actual automobiles by carmakers is heavily dependent on logistical activities, including transportation, order processing, inventory control, materials handling, and information technology. A central link is the carmaker's supply chain manager, who is responsible for translating customer requirements into actual orders and arranging for delivery dates and financial arrangements for automobile dealers.

Page 423

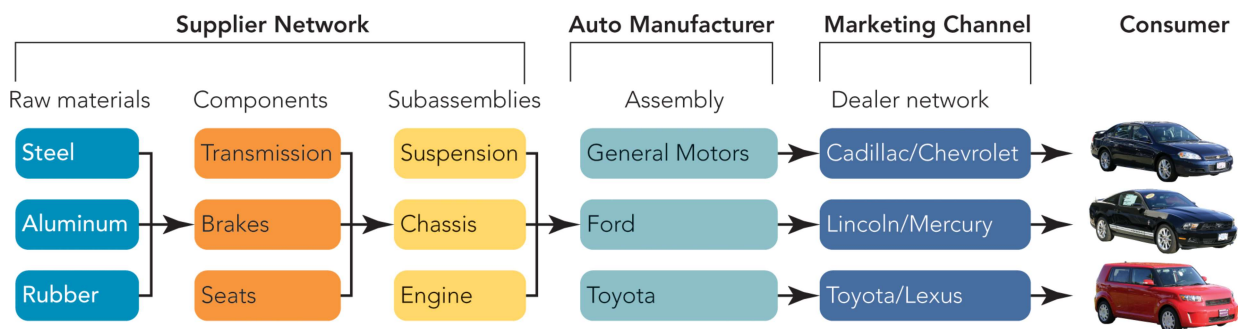


Figure 15–9 The automotive supply chain includes thousands of firms that provide the functional components, software codes, and parts in a typical car.

Car photos: © Mike Hruby

Logistical aspects of the automobile marketing channel are also an important part of the supply chain. Major responsibilities include transportation (which involves the selection and oversight of external carriers—trucking, airline, railroad, and shipping companies—for cars and parts to dealers), the operation of distribution centers, the management of finished goods inventories, and order processing for sales. Supply chain managers also play an important role in the marketing channel. They work with car dealer networks to ensure that the right mix of automobiles is delivered to each location. In addition, they make sure that spare and service parts are available so that dealers can meet the car

maintenance and repair needs of consumers. All of this is done with the help of information technology that links the entire automotive supply chain. What does all of this cost? It is estimated that logistics costs represent 25 to 30 percent of the retail price that you pay for a new car.

Supply Chain Management and Marketing Strategy

VIDEO 15-2

IBM

kerin.tv/13e/v15-2

The automotive supply chain illustration shows how information and logistics activities are integrated and organized across firms to create and deliver a car to you, the consumer. What's missing from this illustration is the linkage between a specific company's supply chain and its marketing strategy. Just as companies have different marketing strategies, they also design and manage supply chains differently. The goals to be achieved by a firm's marketing strategy determine whether its supply chain needs to be more responsive or efficient in meeting customer requirements.

Aligning a Supply Chain with Marketing Strategy

There are a variety of supply chain configurations, each of which is designed to perform different tasks well. Marketers today recognize that the choice of a supply chain follows from a clearly defined marketing strategy and involves three steps:¹³

- 1. Understand the customer.** To understand the customer, a company must identify the needs of the customer segment being served. These needs, such as a desire for a low price or convenience of purchase, help a company define the relative importance of efficiency and responsiveness in meeting customer requirements.
- 2. Understand the supply chain.** Second, a company must understand what a supply chain is designed to do well. Supply chains range from those

that emphasize being responsive to customer requirements and demand to those that emphasize efficiency with a goal of supplying products at the lowest possible delivered cost.

3. *Harmonize the supply chain with the marketing strategy.* Finally, a company needs to ensure that what the supply chain is capable of doing well is consistent with the targeted customer's needs and its marketing strategy. If a mismatch exists between what the supply chain does particularly well and a company's marketing strategy, the company will need to either redesign the supply chain to support the marketing strategy or change the marketing strategy. Read the Marketing Matters box to learn how IBM overhauled its complete supply chain to support its marketing strategy.¹⁴

Marketing Matters

customer
value

IBM's Integrated Supply Chain—Delivering a Total Solution for Its Customers

IBM is one of the world's great business success stories because of its ability to reinvent itself to satisfy shifting customer needs in a dynamic global marketplace. The company's transformation of its supply chain is a case in point.

IBM has built a single integrated supply chain that can handle raw material procurement, manufacturing, logistics, customer support, order entry, and customer fulfillment across all of IBM—something that has never been done before. Why would IBM undertake this task? According to IBM's former CEO, Samuel J. Palmisano, "You cannot hope to thrive in the IT industry if you are a high-cost, slow-moving company. Supply chain is one of the new competitive battlegrounds. We are committed to being the most efficient and productive player in our industry."



© Peter Probst/Alamy

The task is not easy. IBM's supply chain management organization works out of 360 locations in 64 countries, tracking more than 1.5 million assets for both IBM and its clients. The organization also deals with about 23,000 suppliers in nearly 100 countries. Yet with surprising efficiency, IBM's supply chain is linked from raw material sourcing to postsales support.

Today, IBM is uniquely poised to configure and deliver a tailored mix of hardware, software, and service to provide a total solution for its customers. Not surprisingly, IBM's integrated supply chain is heralded as one of the best in the world!

How are these steps applied and how are efficiency and responsiveness considerations built into a supply chain? Let's look at how two well-known companies—Dell and Walmart—have harmonized their supply chain and marketing strategy.¹⁵

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Dell: A Responsive Supply Chain

Page 424

The Dell marketing strategy primarily targets customers who desire having the most up-to-date computer systems customized to their needs. These customers are also willing to (1) wait to have their customized computer system delivered in a few days, rather than picking out a model at a retail store, and (2) pay a reasonable, though not the lowest, price in the marketplace. Given Dell's customer segment, the company has the option of adopting an efficient or responsive supply chain.

An efficient supply chain may use inexpensive, but slower, modes of transportation, emphasize economies of scale in its production process by reducing the variety of system configurations offered, and limit its assembly and inventory storage facilities to a single location. If Dell opted only for efficiency in its supply chain, it would be difficult to satisfy its target customers' desire for rapid delivery and a wide variety of customizable products with its assembly and storage facilities confined to its headquarters in Austin, Texas.

Dell instead has opted for a responsive supply chain. It relies on more expensive express transportation for receipt of components from suppliers and delivery of finished products to customers. The company achieves product variety and manufacturing efficiency by designing common platforms across several products and using common components. Also, Dell has invested heavily in information technology to link itself with suppliers and customers.



© R Heyes Design / Alamy

Walmart: An Efficient Supply Chain

Now let's consider Walmart. Walmart's marketing strategy is to be a reliable, lower-price retailer for a wide variety of mass consumption consumer goods. This strategy favors an efficient supply chain designed to deliver products to 245 million consumers each week at the lowest possible cost. Efficiency is achieved in a variety of ways. For instance, Walmart keeps relatively low inventory levels, and most of it is stocked in stores available for sale, not in warehouses gathering dust. The low inventory arises from Walmart's use of *cross-docking*—a practice that involves unloading products from suppliers, sorting products for individual stores, and quickly reloading products onto its trucks for a particular store. No warehousing or storing of products occurs, except for a few hours or, at most, a day. Cross-docking allows Walmart to operate only a small number of distribution centers to service its vast network of Walmart stores, Supercenters, Neighborhood Markets, Marketside stores, and Sam's Clubs, which contributes to efficiency.

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Walmart has invested much more than its competitors in information technology to operate its supply chain. The company feeds information about customer requirements and demand from its stores back to its suppliers, which manufacture only what is being demanded. This large investment has improved the efficiency of Walmart's supply chain and made it responsive to customer needs.

Page 425

Three lessons can be learned from these two examples. First, there is no one best supply chain for every company. Second, the best supply chain is the one that is consistent with the needs of the customer segment being served and complements a company's marketing strategy. And finally, supply chain managers are often called upon to make trade-offs between efficiency and responsiveness on various elements of a company's supply chain.

TWO CONCEPTS OF LOGISTICS MANAGEMENT IN A SUPPLY CHAIN

The objective of logistics management in a supply chain is to minimize total logistics costs while delivering the appropriate level of customer service.

Total Logistics Cost Concept

For our purposes, **total logistics cost** includes expenses associated with transportation, materials handling and warehousing, inventory, stockouts (being out of inventory), order processing, and return products handling. Note that many of these costs are interrelated so that changes in one will impact the others. For example, if a firm attempts to reduce its transportation costs by shipping in larger quantities, it will increase its inventory levels. While larger inventory levels will increase inventory costs,

they should also reduce stockouts. It is important, therefore, to study the impact on all of the logistics decision areas when considering a change.

Customer Service Concept

Because a supply chain is a *flow*, the end of it—or *output*—is the service delivered to customers. Within the context of a supply chain, **customer service** is the ability of logistics management to satisfy users in terms of time, dependability, communication, and convenience. As suggested by **Figure 15–10**, a supply chain manager's key task is to balance these four customer service factors against total logistics cost factors.

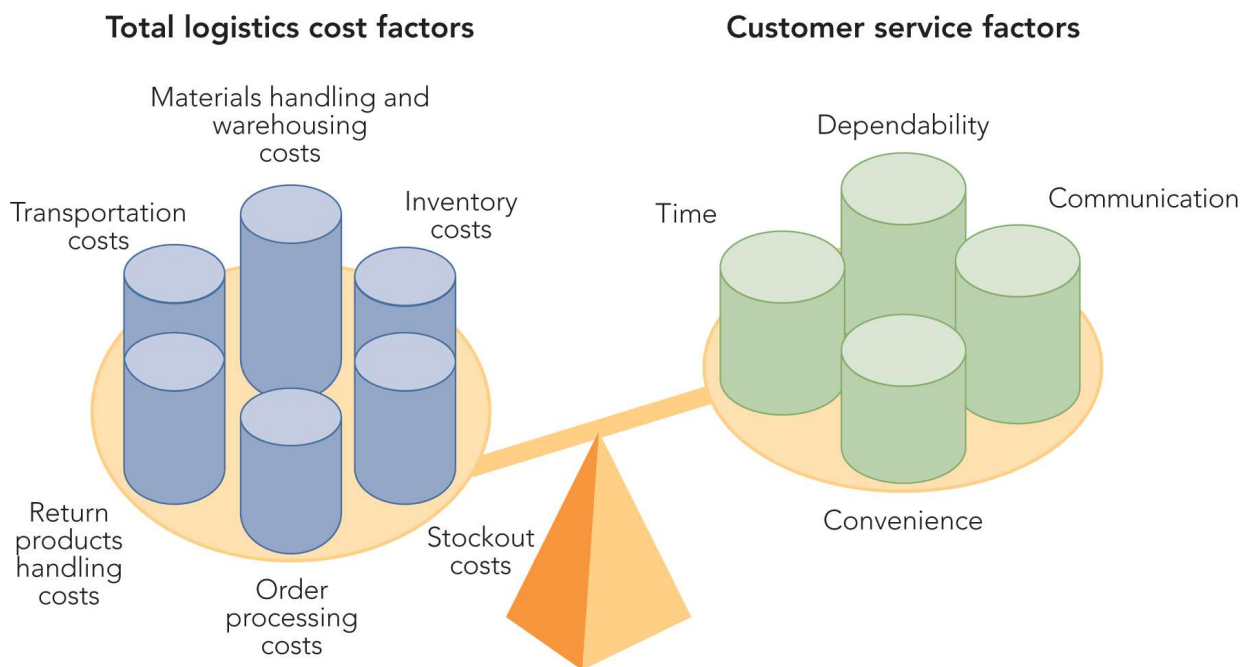


Figure 15–10 Supply chain managers balance total logistics cost factors against customer service factors.

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Time

Page 426

In a supply chain setting, time refers to *order cycle* or *replenishment* time for an item, which means the time between the ordering of an item and when it is received and ready for use or sale. The various elements that make up the typical order cycle include recognition of the need to order, order transmittal, order processing, documentation, and transportation. A current emphasis in supply chain management is to reduce order cycle time so that the inventory levels of customers may be minimized. Another emphasis is to make the process of reordering and receiving products as simple as possible, often through inventory systems called *quick response* and *efficient consumer response* delivery systems. For example, at Saks Fifth Avenue, point-of-sale scanner technology records each day's sales. When stock falls below a minimum level, a replenishment order is automatically produced. Vendors such as Donna Karan (DKNY) receive the order, which is processed and delivered within 48 hours.¹⁶

Dependability

Dependability is the consistency of replenishment. This is important to all firms in a supply chain—and to consumers. How often do you return to a store if it fails to have in stock the item you want to purchase? Dependability can be broken into three elements: consistent lead time, safe delivery, and complete delivery. Consistent service allows planning (such as appropriate inventory levels), whereas inconsistencies create surprises. Intermediaries may be willing to accept longer lead times if they know about them in advance and can thus make plans.

Communication

Communication is a two-way link between the buyer and supplier that helps in monitoring service and anticipating future needs. Status reports on orders are a typical example of communication between the buyer and seller.

Convenience

The concept of convenience for a supply chain manager means that there should be a minimum of effort on the part of the buyer in doing business with the seller. Is it easy for the customer to order? Are the products available from many outlets? Will the seller arrange all necessary details, such as transportation? This customer service factor has promoted the use of **vendor-managed inventory (VMI)**, whereby the *supplier* determines the product amount and assortment a customer (such as a retailer) needs and automatically delivers the appropriate items.

Campbell Soup's system illustrates how VMI works.¹⁷ Every morning, retailers electronically inform the company of their demand for all Campbell products and the inventory levels in their distribution centers. Campbell uses that information to forecast future demand and determine which products need replenishment based on upper and lower inventory limits established with each retailer. Trucks leave the Campbell shipping plant that afternoon and arrive at the retailer's distribution centers with the required replenishments the same day.

CLOSING THE LOOP: REVERSE LOGISTICS

The flow of products in a supply chain does not end with the ultimate consumer or industrial user. Companies today recognize that a supply chain can work in reverse. **Reverse logistics** is a process of reclaiming recyclable and reusable materials, returns, and reworks from the point of consumption or use for repair, remanufacturing, redistribution, or disposal. The effect of reverse logistics can be seen in the reduced waste in landfills and lowered operating costs for companies. The Making Responsible Decisions box describes the successful reverse logistics initiative at Hewlett-Packard.¹⁸

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Page 427

Making Responsible Decisions Sustainable

Reverse Logistics and Green Marketing Hewlett-Packard: Recycling e-Waste

About 53 million tons of electronics and electronic equipment find their way to landfills around the world annually. Americans alone discarded over 400 million analog TV sets and computer monitors and Japanese consumers trashed more than 610 million cell phones in 2014. The result? Landfills are seeping lead, chromium, mercury, and other toxins prevalent in digital debris into the environment.

Fortunately, Hewlett-Packard has taken it upon itself to act responsibly and address this issue through its highly regarded reverse logistics program. Hewlett-Packard has recycled computer and printer hardware since 1987 and is an industry leader in this practice. The company's recycling service is available today in more than 73 countries, regions, and territories. By early 2015, Hewlett-Packard will have recycled over 2 billion pounds of used electronic products and supplies to be refurbished for resale or donation or for recovery of materials.



Source: Hewlett-Packard Development Company, L.P.

The recycling effort at Hewlett-Packard is also part of the company's Design for Supply Chain program. Among other initiatives in this program, emphasis is placed on product and packaging changes to reduce reverse supply chain and environmental costs. For example, more than 75 percent of the company's ink cartridges and 24 percent of its LaserJet toner cartridges are now manufactured with recycled plastic.

VIDEO 15-3

UPS

kerin.tv/13e/v15-3

Companies such as Motorola and Nokia (return and reuse of mobile phones) and Caterpillar, Xerox, and IBM (remanufacturing and recycling) have implemented acclaimed reverse logistics programs. Other firms have enlisted third-party logistics providers such as UPS, FedEx, and Penske Logistics to handle this process along with other supply chain functions. GNB Technologies, Inc., a manufacturer of lead-acid batteries for automobiles and boats, has outsourced much of its supply chain activity to UPS Supply Chain Services.¹⁹ The company contracts with UPS to manage its shipments between plants, distribution centers, recycling centers, and retailers. This includes movement of both new batteries and used products destined for recycling and covers both truck and railroad shipments. This partnership, along with the initiatives of other battery makers, has paid economic and ecological dividends. By recycling 90 percent of the lead from used batteries, manufacturers have kept the demand for new lead in check, thereby holding down costs to consumers. Also, solid waste management costs and the environmental impact of lead in landfills are reduced.

learning review

- 15-9. What is the principal difference between a marketing channel and a supply chain?
- 15-10.** The choice of a supply chain involves what three steps?
- 15-11.** A manager's key task is to balance which four customer service factors against which six logistics cost factors?

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LEARNING OBJECTIVES REVIEW

LO 15-1 *Explain what is meant by a marketing channel of distribution and why intermediaries are needed.*

A marketing channel of distribution, or simply a marketing channel, consists of individuals and firms involved in the process of making a product or service available for use or consumption by consumers or industrial users. Intermediaries make possible the flow of products from producers to buyers by performing three basic functions. The transactional function involves buying, selling, and risk taking because intermediaries stock merchandise in anticipation of sales. The logistical function involves the gathering, storing, and dispensing of products. The facilitating function assists producers in making products and services more attractive to buyers. The performance of these functions by intermediaries creates time, place, form, and possession utility for consumers.

LO 15-2 *Distinguish among traditional marketing channels, electronic marketing channels, and different types of vertical marketing systems.*

Traditional marketing channels describe the route taken by products and services from producers to buyers. This route can range from a direct channel with no intermediaries, because a producer and the ultimate consumer deal directly with each other, to indirect channels where intermediaries (agents, wholesalers, distributors, or retailers) are inserted between a producer and consumer and perform numerous channel functions. Electronic marketing channels employ the Internet to make

products and services available for consumption or use by consumer or business buyers. Vertical marketing systems are professionally managed and centrally coordinated marketing channels designed to achieve channel economies and maximum marketing impact. There are three major types of vertical marketing systems (VMSs). A corporate VMS combines successive stages of production and distribution under a single ownership. A contractual VMS exists when independent production and distribution firms integrate their efforts on a contractual basis to obtain greater functional economies and marketing impact than they could achieve alone. An administered VMS achieves coordination at successive stages of production and distribution by the size and influence of one channel member rather than through ownership.

LO 15-3 *Describe factors that marketing executives consider when selecting and managing a marketing channel, including legal restrictions.*

Marketing executives consider three questions when selecting and managing a marketing channel and intermediaries. (1) Which channel and intermediaries will provide the best coverage of the target market? Marketers typically choose one of three levels of market coverage: intensive, selective, or exclusive distribution. (2) Which channel and intermediaries will best satisfy the buying requirements of the target market? These buying requirements fall into four categories: information, convenience, variety, and pre- or postsale services. (3) Which channel and intermediaries will be the most profitable? Here marketers look at the margins earned (revenues minus cost) for each channel member and for the channel as a whole.

LO 15-4 *Explain what supply chain and logistics management are and how they relate to marketing strategy.*

A supply chain refers to the various firms involved in performing the various activities required to create and deliver a product or service to consumers or industrial users. Supply chain management is the integration and organization of information and logistics across firms for the purpose of creating value for consumers. Logistics involves those activities that focus on getting the right amount of the right products to the right place at the right time at the lowest possible cost. Logistics management includes the coordination of the flows of both inbound and outbound products, an

emphasis on making these flows cost effective, and customer service. A company's supply chain follows from a clearly defined marketing strategy. The alignment of a company's supply chain with its marketing strategy involves three steps. First, a supply chain must reflect the needs of the customer segment being served. Second, a company must understand what a supply chain is designed to do well. Supply chains range from those that emphasize being responsive to customer requirements and demands to those that emphasize efficiency with the goal of supplying products at the lowest possible delivered cost. Finally, a supply chain must be consistent with the targeted customer's needs and the company's marketing strategy. The Dell and Walmart examples in the chapter illustrate how this alignment is achieved by two market leaders.

LEARNING REVIEW ANSWERS

15-1 What is meant by a marketing channel?

Answer: A marketing channel consists of individuals and firms involved in the process of making a product or service available for use or consumption by consumers or industrial users.

15-2 What are the three basic functions performed by intermediaries?

Answer: Intermediaries perform transactional, logistical, and facilitating functions.

15-3 What is the difference between a direct and an indirect channel?

Answer: A direct channel is one in which a producer of consumer or business products and services and ultimate consumers or industrial users deal directly with each other. An indirect channel has intermediaries that are inserted between the producer and ultimate consumers or industrial users and perform numerous channel functions.

15-4

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Why are channels for business products typically shorter than channels for consumer products?

Page 429

Answer: Business channels are typically shorter than consumer channels because business users are fewer in number, tend to be more concentrated geographically, and buy in larger quantities.

15-5 What is the principal distinction between a corporate vertical marketing system and an administered vertical marketing system?

Answer: A corporate vertical marketing system combines successive stages of production and distribution under a single ownership. An administered vertical marketing system achieves coordination by the size and influence of one channel member rather than through ownership.

15-6 What are the three questions marketing executives consider when choosing a marketing channel and intermediaries?

Answer: The three questions to consider when choosing a marketing channel and intermediaries are: (1) Which will provide the best coverage of the target market? (2) Which will best satisfy the buying requirements of the target market? (3) Which will be the most profitable?

15-7 What are the three degrees of distribution density?

Answer: intensive; exclusive; selective

15-8 What is meant by exclusive dealing?

Answer: Exclusive dealing exists when a supplier requires channel members to sell only its products or restricts distributors from selling directly competitive products. It is

strictly prohibited under the Clayton Act when it lessens competition or creates monopolies.

15-9 What is the principal difference between a marketing channel and a supply chain?

Answer: A marketing channel consists of individuals and firms involved in the process of making a product or service available for use or consumption by consumers or industrial users. A supply chain differs from a marketing channel in terms of membership. It includes suppliers who provide raw materials to a manufacturer as well as the wholesalers and retailers—the marketing channel—that deliver the finished goods to ultimate consumers.

15-10 The choice of a supply chain involves what three steps?

Answer: (1) Understand the customer. (2) Understand the supply chain. (3) Harmonize the supply chain with the marketing strategy.

15-11 A manager's key task is to balance which four customer service factors against which six logistics cost factors?

Answer: The four customer service factors are time, dependability, communication, and convenience. The logistics cost factors are transportation costs, materials handling and warehousing costs, inventory costs, stockout costs (being out of inventory), order processing costs, and return products handling costs.

FOCUSING ON KEY TERMS

channel conflict , 419

customer service , 425
disintermediation , 419
dual distribution , 413
exclusive distribution , 416
intensive distribution , 416
logistics , 421
marketing channel , 408
multichannel marketing , 413
reverse logistics , 426
selective distribution , 417
supply chain , 421
total logistics cost , 425
vendor-managed inventory (VMI) , 426
vertical marketing systems , 414

APPLYING MARKETING KNOWLEDGE

1. A distributor for Celanese Chemical Company stores large quantities of chemicals, blends these chemicals to satisfy the requests of customers, and delivers the blends to a customer's warehouse within 24 hours of receiving an order. What utilities does this distributor provide?
2. Suppose the president of a carpet manufacturing firm has asked you to look into the possibility of bypassing the firm's wholesalers (who sell to carpet, department, and furniture stores) and selling direct to these stores. What caution would you voice on this matter, and what type of information would you gather before making this decision?
3. What type of channel conflict is likely to be caused by dual distribution, and what type of conflict can be reduced by direct

distribution? Why?

4. How does the channel captain idea differ among corporate, administered, and contractual vertical marketing systems with particular reference to the use of the different forms of influence available to firms?
5. List the customer service factors that would be vital to buyers in the following types of companies: (a) manufacturing, (b) retailing, (c) hospitals, and (d) construction.

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BUILDING YOUR MARKETING PLAN

Does your marketing plan involve selecting channels and intermediaries? If the answer is “no,” read no further and do not include this element in your plan. If the answer is “yes”:

1. Identify which channel and intermediaries will provide the best coverage of the target market for your product or service.
2. Specify which channel and intermediaries will best satisfy the important buying requirements of the target market.
3. Determine which channel and intermediaries will be the most profitable.
4. Select your channel(s) and intermediary(ies).
5. If inventory is involved, (a) identify the three or four major kinds of inventory needed for your organization (retail stock, finished products, raw materials, supplies, and so on), and (b) suggest ways to reduce their costs.
6. (a) Rank the four customer service factors (time, dependability, communication, and convenience) from most important to least important from your customers' point of view, and (b) identify actions

for the one or two factors that are the most important in regard to your product or service.

Video Case 15 Biggest Selection!

Video Case 15: Amazon: Delivering the Earth's



VIDEO 15-4

Amazon Video Case

kerin.tv/13e/v15-4

“The secret is we are on our seventh generation of fulfillment centers and we have gotten better every time,” explains Jeff Bezos, CEO of Amazon.com, Inc. The global online retailer is a pioneer of fast, convenient, low-cost shopping that has attracted millions of consumers. Of course, while Amazon has changed the way many people shop, the company still faces the traditional and daunting task of creating a seamless flow of deliveries to its customers—often millions of times each day.

THE COMPANY

Bezos started Amazon.com with a simple idea: use the Internet to transform book buying into the fastest, easiest, and most enjoyable shopping experience possible. The company was incorporated in 1994 and launched its website in July 1995. At the forefront of a huge growth of dot-com businesses, Amazon pursued a get-big-fast business strategy. Sales grew rapidly and Amazon began adding products and services other than books. In fact, Amazon soon set its goal on being “Earth’s most customer-centric company, where customers can find and discover virtually anything they might want to buy online.”

Today Amazon.com continues to grow by providing low prices, vast selection, and convenience. Its selection of products covers a broad range of categories including:

Books; Movies, Music & Games; Electronics & Computers; Home, Garden & Tools; Beauty, Health & Grocery; Toys; Clothing, Shoes & Jewelry; Sports & Outdoors; and Automotive & Industrial. In addition, Amazon offers digital music, an appstore for Android, Amazon Cloud Drive, Kindle e-readers, Kindle Fire tablets, Amazon Fire TV, and the Amazon Fire phone. Other services allow customers to:

- Search for a product or brand using all or part of its name.
- Place orders with one click using the “Buy Now with 1-Click” button on the website, and the “Mobile 1-Click” button for phones.
- Receive personalized recommendations based on past purchases through opt-in e-mails.

These products and services have attracted millions of people around the globe. Further, the company’s growth has made Amazon.com, along with its international sites in Australia, Brazil, Canada, China, France, Germany, India, Italy, Japan, Mexico, Spain, and the United Kingdom, the world’s largest online retailer.

Amazon’s e-commerce platform is also used by more than 2 million small businesses, retail brands, and individual sellers. For example, programs such as Selling on Amazon, Fulfillment by Amazon, Amazon Webstore, and Checkout by Amazon allow small businesses to use Amazon’s e-commerce platform to facilitate sales. Online retailers store their products at Amazon’s fulfillment centers and when they sell a product, Amazon ships it! Amazon.com also operates retail websites for brands such as bebe, Marks & Spencer, Lacoste, and AOL’s Shop@AOL. Individual sellers use the Amazon network to reach millions of potential customers. These business partnerships all contribute to Amazon’s sales, which now exceed \$75 billion.

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The screenshot shows the Amazon.com product page for the Xbox One Assassin's Creed Unity 500GB Bundle. The page includes the Amazon logo, search bar, navigation menu, and product details. The main product is the Xbox One Assassin's Creed Unity 500GB Bundle, priced at \$348.99 (a 13% discount from the list price of \$399.99). The page also features several bundle options, such as the 'Assassin's Creed 500GB Bundle' and the 'Halo Master Chief 1TB Bundle'. The right side of the page contains purchase options, including 'Buy new', 'Add to Cart', and 'Buy now with 1-Click®'. The bottom of the page includes a 'Sell yours for a Gift Card' option.

Source: Amazon.com, Inc.

Bezos defines Amazon by its “big ideas, which are customer centricity, putting the customer at the center of everything we do, and invention—we like to pioneer, we like to explore.” Amazon’s success is also the result of an intense focus on cost and efficiency that leads to lower prices. More specifically, Amazon is exceptional at managing the elements of its supply chain, which make up one of the most complex and expensive aspects of the company’s business.

SUPPLY CHAIN AND LOGISTICS MANAGEMENT AT AMAZON.COM

What happens after an order is submitted on Amazon's website but before it arrives at the customer's door? A lot. Amazon.com maintains huge distribution, or "fulfillment," centers where it keeps inventory of millions of products. This is one of the key differences between Amazon.com and some of its competitors—it actually stocks products. Bezos describes how they have improved: "Years ago, I drove the Amazon packages to the post office every evening in the back of my Chevy Blazer. My vision extended so far that I dreamed we might one day get a forklift. Fast-forward to today and we have 96 fulfillment centers." So Amazon must manage the flow of products from its 15 million-plus suppliers to its U.S. and international fulfillment centers with the flow of customer orders from the fulfillment centers to individuals' homes or offices.

The process begins with the suppliers. Amazon collaborates with its suppliers to increase efficiencies and improve inventory turnover. For example, Amazon uses software to forecast purchasing patterns by region, which allows it to give its suppliers better information about delivery dates and volumes. After the products arrive at the fulfillment center they are scanned and placed on shelves in what often appear to be haphazard locations. That is, books may be on the same shelf next to toys and kitchen utensils. Dave Clark, vice president of worldwide operations and customer service at Amazon, explains: "If you look at how these items fit in the bin, they are optimized to utilize the available space, we have computers and algorithms that tell people the areas of the building that have the most space to put the product that's coming in at that time." Clark observes that one of its 1-million-square-foot fulfillment centers (the size of more than 20 football fields) represents a "physical manifestation of earth's biggest selection."

At the same time, Amazon has been improving the part of the process that sorts the products into the individual orders. Once an order is placed in the computer system, sophisticated software generates a map of the location of each product and a "pick ambassador" walks the aisles to select the products. Each item is scanned as it is selected so that inventory levels and locations are always up-to-date. Packers ensure that all items are included in the box before it is taped and labeled. The boxes then travel along a conveyor belt and are diverted into groups based on the delivery location. A network of trucks and regional postal hubs then conclude the process with delivery of the order. Amazon actually uses more trucks than planes!

The success of Amazon's logistics and supply chain management activities may be most evident during the year-end holiday shopping season. Amazon received orders for 36.8 million items on Cyber Monday (the Monday following Thanksgiving), including orders for Xbox and PlayStation gaming consoles that reached more than 1,000 units per minute. During the entire holiday season Amazon shipped orders to 185 countries. Well over 99 percent of the orders were shipped and delivered on time.

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CONTINUOUS IMPROVEMENT AT AMAZON

Page 432

In a recent letter to Amazon shareholders Bezos reported that Amazon employees are “always asking how do we make this better?” He also described the Amazon Kaizen program (named for the Japanese term meaning “change for the better”) and how it is used to streamline processes and reduce defects and waste. As a result there are many new changes and improvements under way at Amazon, many of which are related to its supply chain and logistics management approach.

One example of a new service at Amazon is Amazon Fresh, its online, same-day-delivery service for groceries. The service has been in trial stage in Seattle for several years and recently expanded to Los Angeles and San Francisco. The success of the service in these cities is likely to influence how quickly Amazon expands into other cities. Another new service at Amazon is based on its agreement with the United States Postal Service to offer Sunday delivery to select cities. The demand for this service in the trial cities will also influence how quickly it is rolled out to other cities. Finally Amazon received a lot of attention when it revealed that it is developing unmanned aerial drones that could fly small shipments to customers within 30 minutes. “We can carry objects up to 5 pounds which covers 86 percent of the items that we deliver,” explains Bezos. The Federal Aviation Administration granted Amazon permission to fly drones experimentally in early 2015.

Amazon.com has come a long way since 1995. Its logistics and supply chain management activities have provided Amazon with a cost-effective and efficient distribution system that combines automation and communication technology with superior customer service. To continue its drive to increase future sales, profits, and

customer service, Amazon continues to use its inventive spirit to encourage innovation. According to Bezos, “what we are doing is challenging and fun—we get to work in the future.”²⁰

Questions

1. How do Amazon.com’s logistics and supply chain management activities help the company create value for its customers?
2. What systems did Amazon develop to improve the flow of products from suppliers to Amazon fulfillment centers? What systems improved the flow of orders from the fulfillment centers to customers?
3. Why will logistics and supply chain management play an important role in the future success of Amazon.com?

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