

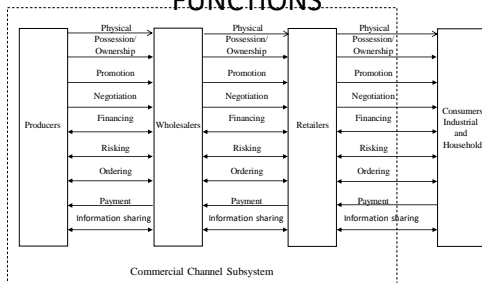
Chapter 3: Channel Analysis: Auditing Marketing Channels

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Auditing Marketing Channels

- Auditing what channel functions get performed by each channel member in the existing channel system, by whom, at what levels, and at what cost, provides several important benefits:
 1. Diagnose and remedy shortcomings in the provision or price of service outputs to targeted segments.
 2. An audit may identify gaps in service outputs desired by targeted end-user segments.
 3. Knowing which channel members have incurred the costs of performing which channel functions helps members allocate channel profits equitably.

CHANNEL AUDIT CRITERIA: CHANNEL FUNCTIONS



Physical possession

- Physical possession refers to channel activities pertaining to the storage of goods, including transportation between channel members.
- The costs of running warehouses and transporting products from one location to another are physical possession costs.
- For product returns ,physical possession and its management drive the channel function's very shape, including who its members are and where the product ultimately will wind up

Ownership

- When a channel member takes title to goods, it bears the cost of carrying the inventory; its capital is tied up in product (whose opportunity cost is the next highest value use of that money).
- In many distribution systems, physical possession and ownership move together through the channel, but this pairing is neither necessary nor universal.

Inventory holding costs

- Inventories refer to stocks of goods or the components used to make them, and they exist for several reasons:
 - Demand surges outstrip production capacity
 - Economies of scale exist in production and transportation.
 - Transportation takes time,
 - Supply and demand are uncertain.

Promotion

- **Promotion** functions take many forms: personal selling by an employee or outside sales force (e.g., brokers and registered investment advisors for mutual funds), media advertising, sales promotions (trade or retail), publicity, and other public relations activities.
- Promotional activities seek to increase awareness of the product being sold, educate potential buyers about products' features and benefits, and persuade potential buyers to purchase.
- A third-party reverse logistics specialist helps manufacturers achieve this promotional goal when it refurbishes returned products and sells them through new channels (e.g., eBay);

Negotiation

- The negotiation function is present in the channel if the terms of sale or the persistence of certain relationships are open to discussion.
- The costs of negotiation are measured mainly as personnel's time to conduct the negotiations, and, if necessary, the cost of legal counsel.

Financing

- Financing costs are inherent to any sale that moves from one level of the channel to another or from the channel to the end-user.
- Typical financing terms for a business-to-business purchase require payment within 30 days and may offer a discount for early payment.

Risk

- There are many sources of risk:
 - Price guarantees
 - Warranties, insurance
 - After-sales service activities

Ordering

- **Ordering** and payment costs are those incurred during the actual purchase of all payment for the product.
- They may seem unglamorous, but innovations are radically altering the performance of these functions today.
 - *Automatic replenishment*

Information sharing

- Information sharing takes place among and between every channel members both routine and specialized ways.
- Retailers share information with their manufacturers about sales trends and patterns through electronic data interchanges
- If used properly, this information can reduce the costs of many other channel functions.

AUDITING CHANNELS USING THE EFFICIENCY TEMPLATE

- The efficiency template describes
 1. The types and amounts of work done by each channel member to perform the marketing functions.
 2. The importance of each channel function to the provision of end-user service outputs, and
 3. The share of total channel profits that each channel member should reap.

| | Importance Weights for functions: | | | Proportion function Performance of channel member | | | | Total |
|------------------------|-----------------------------------|---------------------------------------|--------------|---|-----|-----|--------------|-------|
| | Costs | Benefit Potential (High, Medium, Low) | Final Weight | 1 | 2 | 3 | 4 (End-user) | |
| Physical possession | | | | | | | | 100 |
| Ownership | | | | | | | | 100 |
| Promotion | | | | | | | | 100 |
| Negotiation | | | | | | | | 100 |
| Financing | | | | | | | | 100 |
| Ordering | | | | | | | | 100 |
| Payment | | | | | | | | 100 |
| Information sharing | | | | | | | | 100 |
| Total | 100 | N/A | 100 | N/A | N/A | N/A | N/A | N/A |
| Normative profit share | N/A | N/A | N/A | | | | | 100 |

The efficiency template

- It is a useful tool for codifying the costs borne and the value added to the channel by each channel member, including end-users.
- It can reveal how the costs of particular functions get shared among channel members
- It can be a powerful explanatory tool and justification for current channel performance or changes to existing operating channels.
- For products sold through multiple channels, their efficiency templates can be compared to find any differences in the costs of running the different channels.

Evaluating Channels: The Equity Principle

- Definition of the equity principle:
 - A member’s level of compensation in the channel system should reflect its degree of participation in the marketing functions and the value created by such participation. That is, compensation should mirror the normative profit shares of each channel member.

- The equity principle further asserts that it is appropriate to reward each channel member in accordance with the value it creates.
- Not only is this equivalence fair and equitable, but it also creates strong incentives for channel members to continue generating value.

Evaluating Channels: Zero-Based Channel Concept

- **Zero-based channel**, that is, one that meets the target market segment’s demands for service outputs by performing necessary channel functions to produce those service outputs at a minimum cost.

Managing inventory holding costs

- Avoid items that sell slowly
- Lengthen the life of goods
- Find a vendor who resupplies faster
- Locate a cheaper warehouse.
- Develop better demand forecasts

Bullwhip effect.

- In a supply chain, the end-user constitutes the handle of the whip, because it determines the base of demand throughout the chain. Moving up the whip, we find the retailer who sells the product, the wholesaler who supplies the retailer, and the manufacturer who makes the item. Each party must forecast the end-user's demand, but the farther away the channel member is, the harder that process becomes.

- Establishing a zero-based :
 - What less or nonvalued functions (e.g., excessive sales calls) can be eliminated without damaging customer or channel satisfaction?
 - Are there any redundant activities? Which could be eliminated and thus lower costs for the entire system?
 - Is there a way to eliminate, redefine, or combine certain tasks to minimize the steps for a sale or reduce its cycle time?
 - Is it possible to automate certain activities and thereby reduce the unit costs required to get products to market, even though if fixed costs increase?
 - Are there opportunities to modify information systems to reduce the costs of prospecting, order entry, quote generation, or similar activities?
 - For new channel designs, the planner also is likely to face managerial or environmental barriers to establishing a zero-based channel. If a channel already exists, it might not be a zero-based channel.

AUDITING CHANNELS USING GAP ANALYSIS

- Sources of Channel Gaps:
 - Service gaps and costs gaps
- Environmental bounds and managerial bounds

Service Gaps

- Service gaps can arise in two ways:
 - If the amount of a service supplied is less than the service demanded ($SS < SD$)
 - If the amount of service supplied is greater than the amount demanded ($SS > SD$).
- *Free riding*

Cost Gaps

- A cost gap exists when the total cost of performing all channel functions is too high,
- Holding the level of service outputs constant, if a lower cost way' to perform the channel function in question exists, a cost gap exists too.

Evaluating channels: gap analysis template

| Segment Name/Descriptor | Bulk Breaking | Spatial Convenience | Delivery/Waiting Time | Assortment/Variety | Customer Service | Information Sharing | Major Channel for this segment |
|-------------------------|---------------|---------------------|-----------------------|--------------------|------------------|---------------------|--------------------------------|
| 1. | | | | | | | |
| 2. | | | | | | | |
| 3. | | | | | | | |
| 4. | | | | | | | |
| 5. | | | | | | | |

| Segment name | Bulk breaking | Spatial Convenience | Delivery/Waiting time | Assortment Variety | Customer Service | Information Sharing | Major Channel For this segment |
|-------------------------|---------------|--|--|--------------------|------------------|---------------------------------------|--|
| 1. Small business buyer | H (SS=SD) | Original equipment: M (SS=SD) Postsale service: H (SS=SD) | Original equipment: M (SS>SD) Postsale service: H (SS=SD) | M (SS>SD) | H (SS=SD) | H (both presale and postsale (SS=SD)) | Value-added reseller such as CDW or retailer |
| 2. Large business buyer | L (SS=SD) | Original equipment: H (SS=SD) Postsale service: L (SS>SD) | Original equipment: M (SS>SD) Postsale service: L (SS>SD) | M/H (SS=SD) | M (SS=SD) | L (SS>SD) | Manufacture direct or large reseller such as CDW |
| 3. Government/education | L (SS=SD) | Original equipment: H (SS=SD) Postsale service: H (SS=SD) | Original equipment: M (SS>SD) Postsale service: M (SS>SD) | M/H (SS=SD) | H (SS=SD) | H (both presale and postsale (SS=SD)) | Manufacture direct or approx.20% from small business |

L=low, M=medium, H=high

The end!

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