Master of Business Administration

(Open and Distance Learning Mode)

Semester – II

Marketing Management - II

Centre for Distance and Online Education (CDOE)

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1.0 OBJECTIVES

After studying this unit, you should be able to;

- Define Industrial Marketing
- Explain the nature of Industrial Marketing
- Discuss the scope of Industrial Marketing
- Highlights the characteristics of Industrial Marketing

1.1 INTRODUCTION

Industrial marketing is also known as Business marketing is a dynamic and challenging area that presents opportunities for the application of marketing concepts and principles. To market effectively in an industrial market, we must understand the nature of industrial marketing which function differently, in many respects, from consumer marketing. It is therefore necessary to study industrial marketing for those who are planning a career in industrial marketing.

Industrial marketing also known as organizational marketing due to its nature of functioning. The business transaction is mainly between various types of industries and business houses and service organization. Hence, it is invariably formal arrangement with detailed terms and conditions by way of contract or purchase order. In large number of cases of project work, heavy machinery and high value and high volume sales the purchase documentation with detailed terms and conditions and may run to be in hundreds of pages. This is essential to bind both the parties at every stage of the project for flow of money on one side and work progress on the other side.

Industrial marketing deals with technology, quality evaluation, and deferred payments and after sales services. Domestic and global competition is part of the business and ups and downs for 'capital goods' is common

1.2 MEANING/DEFINITIONS

Industrial marketing is the marketing of product and services to business organization. Business organization includes manufacturing companies, government undertaking, private sector organization, educational institutions, hospitals, distribution and dealers. Business organization buy product and services to satisfy many objectives like production of goods and services, making profits, reducing costs, and so on. In contrast, consumer marketing is the marketing of product and services to individuals, families and households. The consumers buy product and services for their own consumption.

Further, industrial marketing consists of all activities involved in the marketing of products and services to organizations that use products and services in the production of consumer or industrial goods and services, and to facilitate the operation of their enterprises. The companies/selling organizations that sell steel, machine tools, computers, courier services, and other goods and services to business firms/buying organizations need to understand the buyers‘ needs, purchasing power/resources, policies, and buying procedures. They have to create value (benefit) for the buying organizations (customers) with products and services and focus on buying organizational needs and objectives. For example, a company manufacturing and marketing precision steel tubes to bicycle, a manufacturer is doing business marketing. Industrial marketer of the precision steel tube company must understand the needs of bicycle manufacturers such as Hero Cycle and Atlas Cycle, in terms of their quality requirements, applications of tubes, availability or delivery on daily or weekly basis, and so on. Similarly, a small and proprietary firm, giving technical advice (or services) to paint manufacturers is also doing business marketing.

1.3 NATURE AND SCOPE OF INDUSTRIAL MARKETING

Industrial marketers face many unique marketing situation not normally encountered in the consumer market. They must react proactively to changing markets, develop products to meet those changes and market them in uniquely specialized ways to sophisticated industries while maintaining corporate objectives and profits.

The individual market account for a sub stainable amount of economic activity in most economies since industrial revolution. There are market where customers are primarily distinguished by the fact that they are purchasing in order to further objectives of their organizations, rather than for personal motives and use.

The important of a marketing culture and the general principles of marketing apply to the industrial markets, hence the need to study "Industrial marketing" by business school graduates and those who are planning a career in industrial marketing.

1.4 DIFFERENCES BETWEEN INDUSTRIAL MARKETING AND CONSUMER MARKETING

Industrial marketing is more a responsibility of general management in comparison to consumer marketing. Sometimes, it is difficult to separate industrial marketing strategy from the corporate (company) strategy. But in case of consumer marketing, many times the changes in marketing strategy are carried out within the marketing department, through changes in advertising, sales promotion, and packaging strategies. However, the changes in industrial marketing strategy generally have company-wide implications. The differences between industrial and consumer marketing are as shown in Table

Areas	Industrial Markets	Consumer Markets
Market Characteristics	Geographically concentrated Relatively fewer buyers	Geographically Disbursed Mass Markets
Product Characteristics	Technical Complexity Customised	Stadardised
Service Characteristics	Service, timely delivery and availability very important	Service, Delivery, and availability somewhat important
Buyer behavior	Involvement of various functional areas in both buyer and supplier firms. Purchase decisions are mainly made on rational /performance basis. Technical Interpersonal relationship between buyers and sellers	Involvement of family member Purchase decisions are mostly made on physiological/social/psychological needs Less technical expertise Non – Personal relationship
Channel Characteristics	More direct Fewer intermediaries/ middlemen	Indirect Multiple Layer of intermediaries
Promotional Characteristics	Emphasis on personal selling	Emphasis on advertising
Price Characteristics	Competitive bidding and negotiated prices. List prices for standard products	List prices or maximum retail price(MRP)

1. Market Characteristics

Basically, the significant differences exist between industrial and consumer market characteristics that affect the nature of industrial marketing. These differences are:

- Size of market
- Geographic concentration; and
- Competitive nature of the markets.

Size of the Market

Compared to the great number of households that constitute the mass market for consumer goods and services, In the case of industrial markets, it is common to find less than 20 companies to represent the total market for an industrial product or service. In fact, only three or four customers may comprise the major portion of a total market. For example, for a consumer product like toothpaste or soap, a mass market, consisting of all the households in India, exist. Further, in industrial arena, oligopolistic selling organization (very large firms) tend to dominate many markets such as, large power transformers or high-tension switchgears, there are limited numbers of customers-mainly State Electricity Boards, large private and public sector organizations. There are situations of relatively few industrial sellers and few customers, and all of them (vendors as well as the purchasers) having larger size, the sales will follow a pattern of purchasing larger quantities, or engaging in volume purchases on a repeat basis.

Geographical Concentration

Industrial customers also tend to be concentrated in specific areas of India such as Andaman Nicobar, the Leh Hills. Such concentration occurs mainly because of natural resources and manufacturing processes. For example, the geographic location of natural resources explains the concentration patterns of most energy-producing firms. Only a handful of counties in California, Oklahoma,. Texas, and Louisiana produce the bulk of our gas and oil. Manufacturers whose production processes add weight to their products tend to locate near customers, while those whose processes subtract weight tend to locate near sources of input. Manufacturers of computers and other advanced electronic products present an interesting case of plant location. They tend to concentrate in areas that have advanced teaching and research facilities and desirable living locales such as the Silicon Valley in Bangalore. Such locations are chosen to facilitate the attraction of intelligent, educated employees, who seek both intellectual challenges and physical pleasures.

Competitive Nature

An additional difference between the two markets is the nature of oligopsonistic buying. In the industrial arena, oligopsonistic buying organizations, organizations that are very large firms, tend to dominate many markets. For instance, the small number of large automobile producers in the United States purchase 60 percent of all synthetic rubber, 60 percent of all lead, and 72 percent of all plate glass produced in the United States. These oligopsonists' reactions to changes in one another's buying practices affect industrial marketing strategy decisions. Due to the fact that technological or cost-effective advantages override geographical considerations, industrial organizations are more directly involved in international purchasing. Therefore, the major finished goods exports of industrialized nations tend to be industrial rather than consumer goods manufacturers. Industrial demand as well as industrial supply, therefore, is more apt to cross international boundaries than are demand and supply in the consumer market. However, because of increasing improvements in foreign technology and marketing skills, subsidized by government policies, worldwide competition makes it more difficult for Indian suppliers of industrial goods to compete not only in foreign markets, but domestically as well. Industrial marketers, then, are more subject to world political, economic, and competitive changes than are their consumer counterparts.

2. Product Characteristics

In industrial marketing, the products or services are generally technically complex and not purchased for personal use. They are purchased as components parts of the products and services to be produced or serve the operations of the organizations. Because of the importance given to the technical aspects of products, the purchases are made based on the specifications evolved by the buyers.

The real risk in falling in love with the technical aspects of a product in industrial marketing is to ignore the flexibility in responding to customer's needs in a competitive market. Some companies, as a result, commit the serious mistake of trying to change the customer to fit the product. For example, the quality control manager of a "cold rolled (C.R.) steel strip" manufacturing company informed an important customer (who used C.R. steel strip for the manufacture of luggage bags) that the customer was not justified in rejecting his company product, as it was as per the relevant Indian standard specifications and that the customer's product specifications were more rigorous than the Indian standard specifications. However, the customer refused to accept the product, as it was failing at the shop floor operations. The customer, therefore, not only returned the entire rejections but also cancelled the balance orders. Subsequently, other competitors supplied the product as per the needs and specifications of the customer, who placed orders with them. As compared to consumer marketing, industrial customers place a greater importance on service, that is, timeliness, certainly delivery or availability of product, because any delay in supply will have a significant impact on the production or operations.

3. Buyer Behavior

In industrial marketing, the buying process is more difficult as compared to consumer marketing. The purchase decisions in industrial marketing are based on many factors, such as compliance with product specifications product quality, availability, timely supply, acceptable payment and other commercial terms cost effectiveness, after-sales service, and so on rather than on social and psychological needs. The buying decisions generally take a longer time and involve many individuals from technical, commercial/materials, and finance departments. After the initial offer made by a seller, there are negotiations and exchange of information between both the prospective buyer and the seller's organization. Therefore, inter-organizational contacts take place and interpersonal relationships are developed. The relationships between the sellers and buyers are highly valued and they become stable in the long run because of a high degree of interdependence. Changes are few and occur relatively slowly. Buyers charge problems in searching out and qualifying suppliers. The cost of selecting a supplier who cannot meet delivery requirements or who delivers an unsatisfactory product can be high. Thus, the purchasing firm must be certain of a potential supplier's technical, administrative, and financial capabilities. In contrary, in consumer marketing the relationship between a buyer and a seller is non-personal. Consumers change their purchasing habits frequently and the buying decisions are always based on physiological, social and psychological needs of the members of a family household.

4. Channel Characteristics

Inventory or stock control is very much important factor in the business organizations therefore the distribution channels are needed more direct from the manufacturer to the customer in industrial marketing. There are a few channel alternatives, which are feasible in the industrial market than the consumer market

5. Promotional Characteristics

In consumer marketing, the emphasis is given on advertising whereas, in industrial (or business) marketing, the importance is given to the personal selling through the company's sales force. As a result, a much larger expenditure budget is provided for advertising in consumer marketing in comparison to industrial marketing. Advertising is used to lay a foundation for the sales call rather than serve as the primary communication tool. Sales people act more as consultants and technical problem solvers, utilizing in-depth product knowledge and technical understanding of the buyers' needs, whereas industrial advertising normally stresses more factual and technical data. Some industrial advertisers use mainly the internet and lesser of television to reach potential consumers, the primary means of reaching the market is through business magazines, traditional trade journals, and direct mail. Sales promotion activities tend to center on trade shows, trade fairs, catalogs and conducting technical seminars.

6. Price Characteristics

The products are sold through the intermediaries/middlemen to the consumers based on the "Price List" of the manufacturer or the maximum retail price (MRP) for the packaged products in consumer marketing. Sometimes, the retailer reduces the price by passing on to the consumer a part of his discount due to different degrees of intensity of the competition. In industrial marketing, price is less critical factors for purchase decisions. Competitive bidding and price negotiations are very common in industrial marketing and financing arrangements are often considered part of pricing package. When there are no price negotiations in certain Government tenders, the competitive bidding (i.e. quoting a competitive price against a tender enquiry) becomes very important, as only the lowest bidders are considered for placement of orders. Almost private sector and some Government organizations, price negotiations are held to decide the prices and the volume of orders to be placed on various supplier firms. The payment and other commercial terms are also negotiated at the time of price negotiation. Dealer discounts, and volume discounts on the price list of standard industrial products are widely used in industrial marketing. The above discussion clarifies that there are many basic differences exist between consumer and industrial marketing. But, these differences in terms characteristics do not make a complete analysis. Therefore, it is necessary to understand the concept of industrial demand in the market to analyze completely.

Demand in Industrial Market

The demand for industrial products and services does not survive by itself. It is derived from the ultimate demand for consumer goods and services. Therefore, industrial demand is called derived demand. Sometimes, the demand for industrial product is called joint demand, when the demand for a product depends upon its use along with the existence of other product or products. Cross elasticity of demand exists for some substitute products in industrial market.

These concepts are detailed as follows:

Derived Demand

The single most important force in marketing of industrial products and services is derived demand. Industrial customers buy goods and services for making the use in producing other goods and services and finally produced product/service sold to the consumers. In industrial marketing, the demand for industrial goods and services is derived from consumer goods and services. For example, the demand for precision steel tubes does not exist in market. It is demanded for the production of bicycles, motorcycles, scooters, and furniture (steel tables and chairs), which are consumed by the consumers. Thus, the demand for precision steel tubes is derived from the forecast of consumer demand for bicycles, motorcycles, scooters, and furniture. In case of capital goods, such as machinery and equipment (e.g. machine tools, textile machinery, leather machinery, etc.) that are used to produce other goods, the purchases are made not from the current accounts, but from capital accounts with the assumption of profit flow in the usage of such capital goods over a certain period of time. If businessmen feel that there may be a recession in near future, their purchases will be drastically curtailed. On the other hand, if the attitude of businessmen is favorable (i.e. they feel the business is on the upswing) their investment in capital goods and other industrial products will increase. Thus, the attitude of businessmen is very important, as it reflects the optimism or pessimism about the future. During the periods of recession, or reduced consumer demand, industrial firms reduce their inventories/stocks, or reduce the production, or do both. On the other hand, during the period of prosperity, there is an increased production and sales of consumer goods, which results in an increased demand for industrial goods.

This may be the right time for price increases and building stocks as ready availability and shorter delivery period becomes very important. An industrial marketing firm should be in close touch of information regarding customer's purchase, finance, quality, R&D and marketing departments, so as to get information on changes in customer's sales, new product development, financial condition, and the quality of its products.

Joint Demand

Joint demand is common in the industrial market, because it occurs when one specific industrial product is required along with usage of another product. In other words its demand positively is linked to usage of another product. For example, a pumpsets cannot be used for pumping water, if the electric motor or diesel engine is not availab1e. Similarly, the department of telecommunication (DoT), which requires a complete kit, consisting of different items, for joining the under ground telecom cables, cannot buy only some of the items from a supplier as all of them are to be bought to make the product effective. Thus, some industrial products do not have industrial demand, but are demanded only if the other products are available from the industrial supplier.

Cross-Elasticity of Demand

Simply, elasticity is the change in demand from a change in price. The demand for most of the industrial goods can be inelastic (i.e. insensitive to changes in prices) for a particular industry, but at the same time, highly elastic (i.e. sensitive to changes in prices) for individual suppliers. This is because, the total industry demand comes from the united needs of all the customers rather than price, and hence it is relatively inelastic. Though, between the various suppliers, a slight change in the price by one firm may create a major change in the quantity of another and thereby, be highly elastic for any other firm. Cross-elasticity of demand is the reaction of the sales of one product to a price change in another product. This fact is true for both consumer and industrial marketing, but it is more profound in industrial marketing as it can have a dramatic impact on the marketing strategy of an industrial firm. For example, the demand for aluminum is related to the prices of wood and steel for the doors and window frames, as they are close substitutes. Apart from other advantages of aluminum doors and windows, the cost comparison with steel and wooden door and window frames play an important role in the purchase decisions in the construction of houses, commercial offices, factories, hotels, hospitals, and so on. Aluminum extrusion companies regularly collect the information on cost of steel and wood, and advertise the advantages of use of aluminum in terms of negligible maintenance cost, elegant looks, environment, friendly in comparison to wood, and so on. Whenever there is a change in the price of aluminum due to changes in excise duty or other input costs, there is an impact on the sales of doors and windows made out of wood or steel. The reverse is applicable for changes in the prices of steel or wood. Thus, the marketing persons working in the aluminum extrusion companies should recognize that the cross-elasticity of demand exists for their products. If the cross-elasticity of substitute products is high, it indicates that these products compete in the same market. An industrial marketer must know how the demand for his products is likely to be affected by the changes in the prices of substitute products. Because of the unique characteristics of derived demand, the industrial marketing persons would anticipate any increase or decrease in the demand for their products, based on the changes in the demand for their customers' products. They must know that existence of cross elasticity of demand for their products so as to recognize both direct and indirect competition.

It ought to be clear after going through this lesson that industrial marketing is more multifarious than consumer marketing and the marketing success depends on understanding the intricacies involved in it. Industrial marketing strategy has company-wide implications and is, therefore, more of a general management function, affecting the various departments or functions in an organization.

1.5 CHARACTERISTICS OF INDUSTRIAL MARKETING

Industrial market is characterized by the following:

1. The industrial marketers deal with very few numbers of buyers when compared with consumer market.
2. Business or industrial markets are more geographic concentrated than consumer markets. Availability of natural resources, raw materials, labours, managerial and technical expertise and capital may warrant geographical concentration. For instance, in Nigeria industries are concentrated more in Lagos. Nnewi, Aba, Kano, Port-Harcourt, Kaduna, Onitsha, benin city, Ibadan, than others.
3. Industrial buyers are geographically concentrated.
4. Many industrial products have inelastic demand. This implies that demand for many industrial products is not affected by changes in price mostly in the short run. Demand for some industrial products is price insensitive.
5. Business or industrial product faces derived demand. The demand for industrial products is by demand for another industrial or consumer product. For instance, the rate of demand for steel by an automobile company is necessitated by demand for cars.
6. Industrial products have joint demand: the demand for industrial products goes with the demand for additional one or more products. Without these additional products

the industrial product will not be useful or effective. For instance, the demand for vehicle requires demand for diesel, engine oil, gear oil. etc.

7. Industrial purchase requires well-trained experts or professional and knowledgeable buyers.

8. Business market involves formalized buying process. Business normally asks for detailed product specification, purchase order, bidding or bargain, supplier sourcing and formal approval. This is unlike consumer buying which does not undergo this process.

9. Direct Distribution: Most industrial products are distributed directly to the buyer/ user especially where the order size is large and special delivery arrangement is made.

10. Complex Decision: Purchase of industrial products involves huge amount of money, complex and technical considerations, economic consideration, etc, thus, making buying decision complex.

11. Buyer-seller reciprocity: This is a situation where industrial marketer and his customer agree to purchase each other's product based on agreed terms.

12. Dependency of Marketer and customer: Industrial marketing brings long-term business relationship between the seller and the buyer.

13. More Decision Participants: More people tend to involve in making buy-decision than in consumer marketing. Those involves in buying decision are well trained, professional and knowledgeable individuals who pool ideas together so as to get the right product, at the right price, from the right source, at the right time and quantity.

14. Industrial products are easily identifiable

15. It involves more technically complex products.

16. Requires after sales services.

17. There is a greater tendency for rationality in industrial purchasing.

1.6 NOTES

1.7 SUMMARY

In this unit, we have understood industrial marketing or business marketing are the marketing of goods and services to business organizations. The business organization include manufacturing companies, service organizations, institutions and middlemen in private and public sector organizations and Government undertakings. The differences between industrial and consumer marketing exist in certain characteristics such as market, product, buyer behavior, channel, promotional and price.

Unlike consumer products, the demand for industrial products is derived from the ultimate demand for consumer goods and services. It is, therefore, called as derived demand. Joint demand occurs when one industrial product is required, if other products also exist. Cross elasticity of demand is the responsiveness of the sales of one product to a price change in another product.

1.8 KEY WORDS

- Industrial Marketing
- Product
- Market
- Price
- Promotional

1.9 SELFASSESSMENT QUESTIONS

1. What is industrial marketing?
2. Explain the nature and scope of industrial marketing
3. Discuss the difference between industrial marketing and consumer marketing
4. Highlights the characteristics of industrial marketing

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UNIT - 2: CLASSIFICATION OF INDUSTRIAL GOODS

Structure:

2.0 OBJECTIVES

After studying this unit, you should be able to;

- Define industrial goods
- Explain the classification of industrial goods
- Discuss the various type of industrial market

2.1 INTRODUCTION

Individuals and organizations that acquire goods and service to be used directly or indirectly, in the production of other goods and services or to be sold. Classification of Industrial products is necessary as it helps decision making for the organization. Industrial goods are classified on the basis of their relative cost and where they enter the production process.

To develop an effective marketing plan, an industrial marketer needs to understand industrial markets. The industrial market is composed of commercial enterprises, governmental organizations, and institutions whose purchasing decisions vary with the type of industrial good or service under consideration. Effective marketing programs thus depend upon a thorough understanding of how marketing strategy should differ with the type of organization being targeted and the products being sold. The industrial market is characterized by wonderful diversity both in customers served and products sold. Component parts, spare parts, accessory equipment, and services are example of the types of products purchased by the variety of customers in the industrial market. Industrial distributors or dealers who in turn sell to other industrial customers, commercial businesses, government, and institutions buy a variety of products that, in one way or another, are important to the functioning of their business endeavors. Knowing how this immense array of industrial customers purchase and use products and what criteria are important in their purchasing decision is an important aspect of industrial marketing strategy. For the purpose, industrial sellers understand the types of industrial buyers.

2.2 CLASSIFICATION OF INDUSTRIAL GOODS / PRODUCTS

There are many methods by which industrial products and service are classified. The method that is most accepted classifies product and services based on how products or services enter the production process, and their relative costs. Based on this methods, industrial products and services are classified into three broad groups:

1. Material and Parts

2. Capital Items

3. Supplies and Services

1. MATERIALAND PARTS:

Goods that enter the product directly consists of raw material, manufactured materials, and components parts. The costs of these items are treated by the purchasing company as part of manufacturing cost.

Raw materials

These are the basic products that enter the production process with little or no alternations. They may be marketed to OEMs or user customers. For instance, when a large bakery purchases natural gas to fire the ovens which are used to product cakes, it is a user customer. When the same firm purchases sugar for processing the cakes, it is an OEM.

Manufactured Materials and Components Parts: Manufactured materials include those raw materials that are subjected to some amount of processing before entering the manufacturing process. Acids, fuel oil, and steel are the examples of manufactured or processed materials that are the basic ingredients of many manufacturing activities. For instance, an aluminum extrusion unit buys aluminum billets to manufacture aluminum extruded products such as door and window frames, by using an extrusion press. Thus, aluminum billets are called manufactured materials.

Components parts such as electric motors, batteries and instruments can be installed directly into products with little or no additional changes. When these products are sold to customers who use them in their production processes, they are marketed as OEM goods. The components parts are also sold to the dealers or distributors, who resell them to the replacement market. For examples, MICO spark plugs are sold to a truck or car manufacturer, as well as to automotive dealers/distributors throughout India.

2. CAPITAL ITEMS

Capital items are those which are used in the production processes and they wear out over certain time frame. They are normally treated as “user” customers. Capital items are classified into three groups

A. Heavy equipment/installations

B. Accessories/ light equipment

C. Plant and building

A. Heavy equipment/Installation: These are major and long term investment items such as general purpose and special purpose machines, turbines, generators, furnaces, and earth moving equipment. These items are shown in the balance sheet as plant and equipment, and are fixed assets to be depreciated over a period of years if they are purchased outright.

However, if these are leased, the cost is treated for tax purpose as expenses by the purchaser. As the unit purchase price of capital items are high, these items are financed by borrowing money for a period of time, which is roughly equivalent to the expected life of the fixed assets.

B. Accessories/Light Equipment: Light equipment and tools which have lower purchase price and are not considered as part of heavy equipment, are power operated hand tools, small electric motors, dies, jigs, typewriters and computer terminals. Purchases of accessories are either considered as current expenses with purchase prices taken as operating expenses in the year purchased, or they may be considered as fixed assets and therefore, depreciated over a period of few years.

C. Plant and Building: These are the real estate property of a company. It includes the firm's offices, plants, warehouses, housing, parking lots, and so on.

3. SUPPLIESAND SERVICES

Supplies and services support the operation of the purchasing organization. They do not become a part of the finished product. They are treated as operating expenses for the periods they are consumed.

Supplies: Items such as paints, soaps, oils and greases, pencils, typewriter ribbons, stationery and paper clips belongs to this category. These items are generally standardized and are marketed to a wide cross section of industrial users.

Services: Companies need a wide range of services like building maintenance services, auditing services, legal services, courier services, marketing research services and others.

2.3 TYPES OF INDUSTRIAL MARKET/CUSTOMERS

Industrial customers are generally classified into four groups

1. Commercial Enterprises
2. Government Customer
3. Institutional Customer
4. Cooperative Societies

1. Commercial Enterprises:

As the term indicates the category of customer are giving large volume and profit making business. For purposes other than selling directly ultimate customers. They purchases products for different uses and it is more useful from a marketing points of view to define them in such a way as to understand their purchasing needs so that an effective marketing can be designed. This category can be further divided into

- User

- Dealers
- Distributors
- OEM

User: the particular market uses the industrial product to facilitate its operation of business for example when a lathe machine of Lakshmi Machinery Works(LMK), Coimbatore is used by HMT to manufacture its products. HMT would be the user market. HMT will use it only to manufacture its out put not include the Industrial machinery "Inside" or "Into" the final output. Other such product could be drilling machine, typewriters, computer and grinding wheels.

Dealers and Distributors: Organization which purchases the industrial goods and in turn resell them comes under this category. They are members of channel through which the goods reach the customers. Even though the channel members remain independent of manufacture free to seek their own goals. Both parties agree to work together for common goals and even greater profits either would achieve independently.

OEM (Original Equipment Manufacturer): These industrial customers purchase industrial goods to incorporate them into the products they produce. For instance, a tyre manufacturer (say MRF), who sell tyres to a truck manufacturer (say telco) would consider the truck manufacturer as on OEm. Thus, the product of the industrial marketer(MRF) becomes a part of the customer's(TELCO's) product.

Government Customer

The largest purchases of industrial products in India are Central and state government departments, undertakings, and agencies, such as railways, department of telecommunication, defence, Director General of supplies and Disposal (DGS&D), state transport undertakings, state electricity boards, and so on. These government units purchase almost all kind of industrial products and services.

Institutions

Public and private institutions such as hospital, schools, colleges, universities, and prisons, are classified as institutional customers. Some of these institutions have rigid purchasing rules and others have more flexible rules. An industrial marketing person needs to understand the purchasing practice of each institute so as to be effective in marketing the products or services.

Cooperative Societies

This category is unique and was a part of the cooperative movement in India. An association of person form a cooperative society. It can be manufacturing units (e.g. cooperative sugar mills) or non- manufacturing organizations (e.g. cooperative banks, cooperative housing societies.

2.4 FEATURES OF INDUSTRIAL MARKETING

Fewer; But Large Market

Business buyers will be very less as compared to consumer buyers; but they purchase in bulk or more quantities.

Close Relation

Relation between seller and buyer have to be kept very close and professional because once the relations are build, can't be changed easily as it reflects huge profit.

Complex Buying Process

Very complex procedure is adopted by business buyers; because before purchasing, the approval is required from different officials and authorities.

Continuous sales calls

To finalize the deal, it requires constant fallow ups and continuous sales calls.

Expertise selling skills

Sharp selling skill is required to sell the product to industrial buyers. As they are purchasing in bulk, they will not be easily convinced. Deep product knowledge is required.

Influences

To finalize the product, different authorities and officials will interfere the decision to purchase the product.

Geographically concentrated buyer

More than half of the nation's industrial buyers are concentrated in seven states; New York, California, Pennsylvania, Illinois, Ohio, New jersey, and Michigan. Industries, such as petroleum, rubber, and steel, show even greater geographic concentration. Most agricultural output comes from a relatively small member of states. This geographical concentrated of producers helps to reduce the costs of selling to them. Industrial market will want to watch any tendencies towards or away from geographies concentration.

Derived Demand

The demand for industrial goods is ultimately derived from the demand for consumer goods. Thus animal hides are purchased because consumers buy shoes, purses, and other leather goods. If the demand for these consumer goods slackens, so will demand for all the industrial goods entering into their production.

Inelastic Demand

The total demand for many industrial goods and services is not much affected by price changes. Shoe manufacturers are not going to buy much more leather if the price of leather falls. Nor are they going to buy much less leather if the price of leather rises unless they can find satisfactory leather substitutes. Demand is especially in elastic in the short run because producers cannot make many changes in their production methods.

Fluctuating Demand

The demand for industrial goods and services tends to be more volatile than the demand for consumer goods and services. This is especially true of the demand for new plants and equipment.

Professional Purchasing

Industrial goods are purchased by professionally trained purchasing agents, who spend their work lives learning how to buy better. Many belong to the national association of purchasing agents, which seeks to improve the effectiveness and status of professional buyers.

2.5 NOTES

2.6 SUMMARY

In this unit, the industrial customers are classified into four group- commercial enterprises. Government customers, Institutional customers and cooperative societies. The industrial goods and services are also classified into three broad types- materials and parts, capital items and suppliers and services. The various types of industrial customers and products have certain marketing implications. The purchasing practices of industrial customer vary for different types of customers and it is important that industrial markets understand the purchasing practices followed by their major industrial customer.

2.7 KEY WORDS

♦ Industrial distributor ♦ Capital item ♦ Accessories ♦ Equipments ♦ Dealer

2.8 SELFASSESSMENT QUESTIONS

1. Define industrial marketing. Explain the features of industrial marketing
2. Explain the classification of industrial goods and services
3. Discuss the various type of industrial market

2.9 REFERENCES

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UNIT - 3: INDUSTRIAL MARKETING ENVIRONMENT

Structure:

3.0 OBJECTIVES

After studying this unit, you should be able to;

- Define Environment
- Explain the internal factors of Environment
- Discuss the external factors of Environment
- Explain the B2B Marketing
- Highlights the recent trends in B2B Marketing

3.1 INDUSTRIAL MARKETING ENVIRONMENT

Industrial buyers and sellers operate in a dynamic environment which changes continuously. However, much of the discussions on environment are about ecological environment like air and water pollution, disposal of solid waste and conserving natural resources.

The success of the organization hinges on monitoring and adapting to or developing strategies to withstand environmental changes. Marketers need to gather and analyze information on forces in the environment and implement strategies to adapt to environmental demands.

3.2 INTERNAL ENVIRONMENT

The purpose of carrying out the internal environment analysis is to identify periodically the specific strengths and weaknesses of a company.

The following points highlight the seven factors that determine internal environment of a business firm. The factors are:

(1) Value System

(2) Mission and Objectives

(3) Organization Structure

(4) Corporate Culture and Style of Functioning of Top Management

(5) Quality of Human Resources

(6) Labor Unions, and

(7) Physical Resources and Technological Capabilities.

Value System

The value system of an organization means the ethical beliefs that guide the organization in achieving its mission and objective. The value system of a business organization also determines its behavior towards its employees, customers and society at large. The value system of the promoters of a business firm has an important bearing on the choice of business and the adop-tion of business policies and practices. Due to its value system a business firm may refuse to produce or distribute liquor for it may think morally wrong to promote the consumption of liquor.

The value system of a business organization makes an important contribution to its success and its prestige in the world of business. For instance, the value system of J.R.D. Tata, the founder of Tata group of industries, was its self-imposed moral obligation to adopt morally just and fair business policies and practices which promote the interests of consumers, employees, shareholders and society at large. This value system of J.R.D. Tata was voluntarily incorporated in the articles of association of TISCO, a premier Tata company.

Infosys Technologies which won the first national corporate governance award in 1999 attributes its success to its high value system which guides its corporate culture. To quote one of its reports, “our corporate culture is to achieve our objectives in environment of fairness, honesty, transparency and courtesy towards our customers, employees, vendors and society at large” Thus value system of a business firm has an important bearing on its corporate culture and determines its behavior towards its employees, shareholders and society as a whole.

Mission and Objectives:

The objective of all firms is assumed to be maximization of long-run profits. But mission is different from this narrow objective of profit maximization. Mission is defined as the overall purpose or reason for its existence which guides and influences its business decision and economic activities.

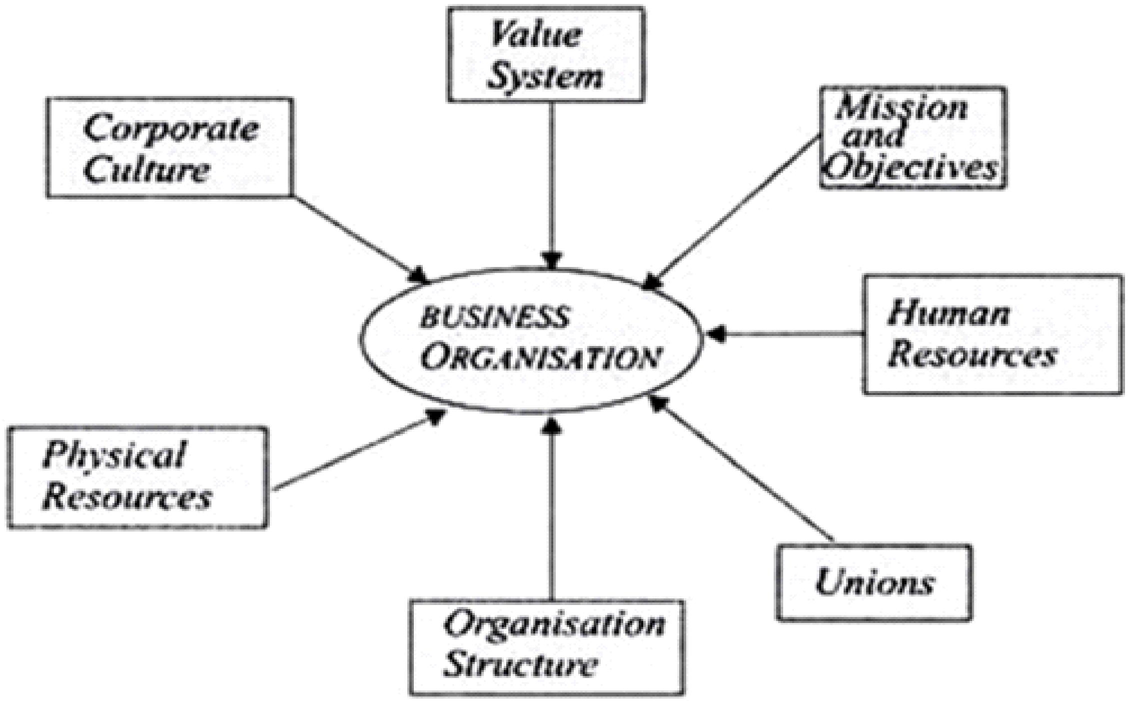
The-choice of a business domain, direction of its development, choice of a business strategy and policies are all guided by the overall mission of the company. For example, “to become a world-class company and to achieve global dominance has been the mission of ‘Reliance Industries of India’. Similarly “to become a research based international pharma company” has been stated as mission of Ranbaxy Laboratories of India.

Organization Structure:

Organization structure means such things as composition of board of directors, the number of independent directors, the extent of professional management and share -holding pattern. The nature of organizational structure has a significant influence over decision making process in an organization. An efficient working of a business organization requires that its organization structure should be conducive to quick decision making. Delays in decision making can cost a good deal to a business firm.

The board of directors is the highest decision making body in a business organization. It takes general policy decisions regarding direction of growth of business of the firm and supervises its overall functioning. Therefore, the managerial capability of the board of directors is of crucial importance for the functioning of a business firm and for achievement of its overall mission and objectives.

For efficient and transparent working of the board of directors in India it has been suggested that the number of independent directors be increased. Many private corporate firms in India are managed by family members of their promoters which is not conducive to the efficient working of these firms.



Internal Environment

It is therefore highly desirable to increase the extent of professional management of private corporate companies. The share holding pattern has also an important implication for business management. In some Indian companies the majority of shares is held by the promoters of the company themselves.

In some others share-holding pattern is quite diversified among the public. In India financial institutions such as UTI, LIC, GIC, IDBI, IFC etc. have large share holdings in promi-nent Indian corporate companies and the nominees of these financial institutions play a critical role in making major business policy decisions of these corporate companies.

Technically, shareholders elect directors who make up the board of directors. The directors then appoint company's top managers who take various business decisions. However, most of the sharehold-ers delegate the voting rights to the management or do not attend the general body meeting.

Thus most of the shareholders regard ownership of the company as a purely financial investment. However, in recent years in developed countries like the United States the shareholders have come to wield a great influence.

The bankruptcy of business giants such as Enron, World Com. in the United States have created great awareness as well as mistrust among shareholders. In the last few years there has been frequent law suits filed by shareholders against directors and managers for ignoring the interests of shareholders or in fact cheating them by not declaring dividends. That is why there is worldwide debate on proper corporate governance of business firms.

Corporate Culture and Style of Functioning of Top Management:

Corporate culture and style of functioning of top managers is important factor for determining the internal environment of a company. Corporate culture is generally considered as either closed and threatening or open and participatory.

In a closed and threatening type of corporate culture the business decisions are taken by top-level managers, while middle level and work-level managers have no say in business decision making. There is lack of trust and confidence in subordinate officials of the company and secrecy pervades throughout in the organisation. As a result, among lower level managers and workers there is no sense of belongingness to the company.

On the contrary, in an open and participatory culture, business decisions are taken at lower levels of management, and top management has a high degree of trust and confidence in the subordinates. Free communication between the top level management and lower-level managers is the rule in this open and participatory type of corporate culture. In this open and participatory system the participa-tion of workers in managerial tasks is encouraged.

Closely related to corporate culture is the style of functioning of top management. Some top managers believe in just giving orders and want them to be strictly followed without holding consul-tations with lower level managers. This style of functioning is not conducive to the adaptability and flexibility in dealing with the changing external environment of business.

Quality of Human Resources:

Quality of employees (i.e. human resources) of a firm is an important factor of internal environment of a firm. The success of a business organisation depends to a great extent on the skills, capabilities, attitudes and commitment of its employees. Employees differ with regard to these characteristics.

It is difficult for the top management to deal directly with all the employees of the business firm. Therefore, for efficient management of human resources, employees are divided into different groups. The manager may pay little attention to the technical details of the job done by a group and encourage group cooperation in the interests of a company. Due to the importance of human resources for the success of a company these days there is a special course for managers how to select and manage efficiently human resources of a company.

Labor Unions:

Labor unions are other factor determining internal environment of a firm. Unions collectively bargain with top managers regarding wages, working conditions of different categories of employees. Smooth working of a business organization requires that there should be good relations between management and labor union.

Each side must implement the terms of agree-ment reached. Sometimes, a business organization requires restructuring and modernization. In this regard, the terms and conditions reached with the labor union must be implemented in both letter and spirit if cooperation of workers is to be ensured for the reconstruction and modernization of business.

Physical Resources and Technological Capabilities:

Physical resources such as plant and equipment, and technological capabilities of a firm determine its competitive strength which is an important factor determining its efficiency and unit cost of production. R and D capabilities of a company determine its ability to introduce innovations which enhance productivity of workers.

It is however important to note that rapid technological progress, especially unprecedented growth of information technology in recent years has increased the relative importance of 'intellec-tual capital and human resources as compared to physical resources of a company. The growth of Bill Gates Microsoft Company and Murthy's Infosys Technologies is mostly due to the quality of human resources and intellectual capital than to any superior physical resources.

3.3 EXTERNAL ENVIRONMENT

Successful companies recognize the importance of continuously scanning the external environment factors. Both macro and micro external environmental factors change continuously. These changes spin out new opportunities and threats. Based on the analysis of the external environmental factors and the resulting opportunities and threats, industrial firms determine their objectives and strategies. it is important for an industrial firm to understand that all the environment factors are not relevant and hence, each firm should identify the relevant environment factors for its business and monitor the relevant environmental factors. It is not adequate to analyze and measure the current status of the relevant environmental factors. It is required that the future estimates or forecasts of economy, technology, market demand, government regulations, etc are made. These forecasts are used as the basis for strategic planning and short term marketing plans.

- Economic Factors
- Technological Factors
- Government, Political and Legal Factors
- Socio-Cultural factors
- Competition

Economic Factor

Changes in economic environment need to be monitored as it affects the willingness and ability of the industrial organizations to buy and sell. If industrial marketer serve domestic and international market, it would be necessary for them to examine the changes in the economic environment, both at home and overseas markets.

The various economic factors that need to be monitored are business cycle, interest rates, currency rates, fiscal policies, investment, and industrial production and so on.

If the economy shows recessionary trends, the consumers will have a lower purchasing power to buy consumer products. As a result, due to the derived nature of industrial demand, the demand for industrial raw material, components and capital goods will decrease. However, the demand for industrial goods and services does not get affected equally due to the change in economic conditions, and that there is a variation in the degree of impact among various industrial products and services.

For example, during the recessionary period in the Indian economy from 1996 to 1998, the demand for capital goods, steel, and aluminum fell much more than other goods such as computer software, paper, chemicals, and pharmaceutical. Hence, the industrial marketers, marketing their goods and services to many industrial market segments need to find out the degree of impact of demand in their market segments.

Technological Factor

Technological developments and changes have major impact on both industrial buyers and sellers. There are rapid technological changes in some of the industries such as telecommunication, computers, and semi conductors. Technological breakthrough can affect markets by starting new industries and radically change existing industries.

Rapid changes in technology are forcing industrial firms to

1. Recognize limits to their existing technologies
2. Know which new technologies are emerging
3. Decide when to incorporate new technologies in their products

There is also a need for working like a team among marketing, R&D, production engineering, and manufacturing for responding effectively to the technological changes.

Government, Political and Legal Factor

As the global competition increase, industrial marketers have to understand the actions of their governments as well as those of the government around the world. The major functions of the government are to protect the consumers, companies, and the society from unfair business practices and guide their industries towards growth. These functions are achieved by the government through political and legal system.

Industrial marketers are benefited by anticipating and influencing government actions. Before governmental regulations and laws are enacted, the captains of industries can influence governmental actions by discussions with the concerned ministry through industry associations like Confederation of India Industries and Federation of Indian Chamber of Commerce and Industries.

Political environment includes the stability of governments, their policies towards business and international trade restrictions. In many countries, protection against foreign imports is brought about through use of import tariffs or imposition of artificial barriers or enacting anti dumping laws.

The US imposed unilaterally Super 301 sanction against certain countries on the pretext of 'human right violations'.

In India, the government has enacted Monopolies and Restrictive Trade Practices(MRTP) Act tp protect companies from unfair business practices.

Japan imposes 15-20 per cent commodity tax on sales in Japan, which is waived for exports from Japan.

Socio-Cultural Factor

The impact of changes in cultural and social environment is felt more for consumer markets than industrial markets. However, if industrial firms decide to have joint venture with foreign companies or decide to set up factories abroad, there is a need to study the cultural and social aspects of the societies in those countries to ensure better compatibility.

Competition

In today's markets, understand competition is as important as understanding customers. An industrial marketer needs to gather information on competitors' strategies, objectives, strength and weakness, and reaction patterns. The company marketing executives should be able to obtain complete and reliable information about competitors. Competitors' information influences the decision on the various elements of marketing strategy like target market segments, pricing, product mix, distribution, and so on.

3.4 B2B MARKETING

Business-to-business (**B2B**) refers to a situation where one business makes a commercial transaction with another. This typically occurs when:

- A business is sourcing materials for their production process (e.g. a food manufacturer purchasing salt).
- A business needs the services of another for operational reasons (e.g. a food manufacturer employing an accountancy firm to audit their finances).
- A business re-sells goods and services produced by others (e.g. a retailer buying the end product from the food manufacturer).

B2B is often contrasted against business-to-consumer (B2C). In B2B commerce it is often the case that the parties to the relationship have comparable negotiating power, and even when they don't, each party typically involves professional staff and legal counsel in the negotiation of terms, whereas B2C is shaped to a far greater degree by economic implications of information asymmetry.

B2B marketing techniques rely on the same basic principles as consumer marketing, but are executed in a unique way. While consumers choose products based not only on price but on popularity, status, and other emotional triggers, B2B buyers make decisions on price and profit potential alone.

Finding new ways to foster relationships through social media is currently a hot topic in the B2B marketing world. Social media platforms have opened up two way conversations between businesses. A survey organized by Chadwick Martin Bailey and iModerate, showed that businesses are more likely to buy from companies they track through social media.

B2B marketing refers to the techniques and best practices used by companies with products and services sold to other businesses. Unlike many B2C marketing efforts, B2B initiatives must consider that a number of executives likely weigh in on a single purchase decision, so campaigns must address multiple audiences within the same enterprise. Additionally, B2B marketing must cater to (generally) long transaction periods.

When businesses are in the market for new solutions or methods aimed at improving their operations, the demonstration of value of is vitally important. While trade events are often cited as a top avenue for B2B marketing, internet marketing is also becoming vital as recent figures show that 93 percent of business buyers start their product research on search engines.

Objectives of B2B Marketing

The objectives of B2B Marketing are:

- Increase sales
- Build brand awareness
- Grow market share
- Launch new products or services
- Target new customers
- Enter new markets internationally or locally
- Improve stakeholder relations
- Enhance customer relationships
- Improve internal communications
- Increase profit

3.5 RECENT TRENDS IN B2B MARKETING

The following are the recent trends in B2B marketing are as follows:

- Customer Experience
- Advocate Marketing

- Sales Enablement
- Marketing Apps
- Social Media
- Email Marketing

Customer Experience

Customer experience has been receiving a lot of attention over the last few years, primarily among B2C companies and retailers. It involves the combination of people, process and technology to understand, anticipate and consistently deliver exceptional personalized experience across all touch points. In a recent white paper, Forrester Research predicted that " In 2016, leaders will understand and anticipate individual needs to deliver personalized experiences, sharply increasing their lead in the market".

As today's B2B buyer are increasingly influenced by their consumer experiences and have begun to demand similar experiences in their professional lives, firms are recognizing how customer experience can be a driver of both business differentiation and profitability. For marketer this will mean a much more systematic and intentional focus on the entire experience for a customer, delivering a seamless and consistent experience, regardless of channel or device and in a way that is consistent with your brand promise.

Advocate Marketing

B2B marketers tend to focus a lot of time and effort on the pre purchase end of the customer journey. But increasingly, firms are realizing success by also concentrating their efforts on providing value beyond the sale, with the aim of turning a client into a promoter an advocate who is wiling to refer people to and provide references for your business. Referrals have long been considered one of the most valuable forms of marketing, delivering qualified leads that tend to become client and remain loyal over a long period of time. While loyalty programs have been a staple in the retail world for quite some time, we're starting to see B2B firms leverage their own version.

Advocate marketing software platforms such as influitive and customer Advocacy help marketers build advocate relationship with client at scale by increasing social media engagement, generating more reviews and capturing referrals. These platforms use customized portals where firms invite their best customers to participate in challenges and provide feedback to earn rewards for things like badges, special event invitations, gift cards and award ceremonies at conferences.

Sales Enablement

Oracle Marketing Cloud describes sales enablement as “Providing sales with insights into buyer motivations, behavior, and activity to help boost their results”. For many B2B firms, especially those that are services oriented, marketing is a support role for business development and sales activities. Ultimately, the goal of sales enablement is to ensure that every seller has the required knowledge, insights, content and processes to optimize every interaction with prospects and clients.

Today’s complex buyer’s journey and the evolving role of the sales function demands that marketing does more than simple help their firms generate new leads. They also need to be focused on helping to convert those leads into opportunities and opportunities into revenue. Sales enablement includes demand generation, lead nurturing and related activities, but it primarily focuses on leveraging technology to provide better buyer insights, predictive analytics and proactive content support. Sales enablement forces marketing to get into the minds of sales people and think about their sales process and approach, in addition to the decision process of the buyer.

Marketing Apps

Whether mobile apps or on site web apps, in 2016 more B2B firms will find ways to incorporate apps as part of their marketing strategy. Web apps are applications built into a website, as opposed to something you have to download and install on your computer or mobile phone. They can turn a static web page into something more functional and interactive that better engages users and can help to convert user into leads. Apps may include calculators, assessments, estimate builders, interactive white papers or some other utility that turns content into something users will interact with because it’s helpful and interesting.

In addition to web apps, mobile apps are also going to pick up steam in B2B marketing as well. If your firm invests heavily in content marketing, produces content frequently, and has a loyal audience, a mobile app can be great way to deliver content into the hands of your audience. Other B2B firms are creating apps for tradeshows, events and networking. For more product oriented B2B firms, apps can be used for sales as well.

Example, Atlas Copco Construction uses mobile app to showcase their products and service and make it easy for customer to request quotes, access contact information or find the nearest location.

Social Media

Consumer wants to be able to communicate directly with brands, and as they demand more real time engagement, social media will become even more important. Social media can help organization relate to and engage more intelligently with buyers, indeed, 61% of those companies that use it report a positive impact on revenue growth.

Email Marketing

Email marketing is directly sending a commercial message, typically to a group of people, using email. In its broadest sense, every email sent to a potential or current customer could be considered email marketing. It usually involves using email to send ads, request business, or solicit sales or donations, and is meant to build loyalty, trust, or brand awareness. Email marketing can be done to either sold lists or a current customer database. Broadly, the term is usually used to refer to sending email messages with the purpose of enhancing the relationship of a merchant with its current or previous customers, to encourage customer loyalty and repeat business, acquiring new customers or convincing current customers to purchase something immediately, and adding advertisements to email messages sent by other companies to their customers.

3.6 NOTES

3.7 SUMMARY

Industrial marketing is having good or adverse effect of various environmental factors. These factors are internal and external.

Internal environment is known to us which represents technological functional and business capacities of the firm. External environment represents the customer and their loyalty, competition and their strength, subcontractor and suppliers and their quality, reliability and business capacity and role of agent, dealers and the overall company image in public mind.

3.8 KEY WORDS

- Competition
- Mobile app
- Advocate marketing
- Email marketing

3.9 SELFASSESSMENT QUESTIONS

1. What is industrial environment? Explain the significance of industrial environment
2. Discuss the internal factors of environment
3. Explain the external environment factors affecting industrial marketing
4. Write a note on B2B marketing
5. Examine the recent trends of B2B Marketing

3.10 REFERENCES

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6. R.V. Badi and N.V Badi, Industrial Marketing

UNIT - 4: INDUSTRIALMARKET SEGMENTATION

Structure:

4.0 OBJECTIVES

After studying this unit, you should be able to;

- Define market segmentation
- Explain the advantages of market segmentation
- Discuss the factors affecting market segmentation
- Examine the criteria used for selection of market segmentation
- Discuss the Concept of Targeting, Segmenting and positioning

4.1 INTRODUCTION

One of the most important decisions an industrial organization makes is to select its customer or market which it can serve effectively. A firm should decide whether it can effectively serve the entire market. If it does not have the adequate resources, it can best serve parts or segment of the market much better than its competitors.

Market segmentation is the process of dividing the total market for a product or service into several segments or distinct group of buyers. Each group of buyer or segment is homogeneous and may require separate benefits from the product. Market segmentation, in both industrial and consumer marketing, is carried out in certain steps.

Market segmentation in the industrial arena has not been pursued as vigorously as it has in the consumer area because, not only is there great diversity among end users, but differences also exist in product application, customer characteristics, drying patterns, and benefits sought. But there are organizations for whom; a well through out policy of segmentation plays a pivotal role in the determination of success.

4.2 MEANING

Market segmentation is the process of dividing the total market into several segments or distinct group of buyers. Each group of segment requires separate benefits from the product.

The decision of the industrial marketer on segmenting, targeting and positioning is considered as an important strategic long term marketing decision.

It is the process of dividing the entire market into small units.

4.3 ADVANTAGES OF MARKET SEGMENTATION

The following are the advantages or benefits of market segmentation

- The organization can create a more fine-tuned product or service offer and price it appropriately for the target.
- Choice of distribution channels and communication channels becomes much easier.
- The organization can identify the marketing opportunities existing in the market by analyzing each segment
- The marketing programmes can be created separately for each segments thus guaranteeing higher success rate
- Freedom to choose and concentrate on those segments where the company faces fewer competitions.
- It enables the industrial marketer to compare marketing opportunities of different market segments by studying the customer needs and potential, competition and satisfaction levels of customers in each market segment.
- The budgeted allocation of resources can be done effectively to various segments, and hence, marketing resources can be used more effectively.

4.4 CRITERIA USED FOR SELECTION OFSEGMENTATION VARIABLES

The selection of variables used for segmentation of industrial markets should meet major criteria in order to achieve effective segmentation.

1. Measurable
2. Differentiable
3. Substantial
4. Accessible
5. Appropriate
6. Stable

1. Measurable: The variables used should measure sales potential or quantity of product required by customers, and other customer information. The information on variables should exist so that the same can be obtained by marketing research. For example, market segmentation for precision steel tubes was done based on segmentation variable of end users, such as bicycles, two wheelers, furniture, boiler, bus body builders. The information on sales potential, product needs, type of buying situation and buying practices was available for the different end user industries. This information was obtained through primary data and secondary data.

2. Differentiable: The segments should be distinguishable and should respond differently to separate marketing plans or strategies. For instance, if scooter, motorcycle, and moped manufacturers respond similarly (in terms of product requirement, pricing and buying directly from suppliers) while purchasing steel, then they do not form separate segments. They are combined to become a two wheeler segment which is a homogeneous group, because of the similarities among the customer of the group.

3. Substantial: The segments should be large enough in terms of sales potential and profits. Only then a separate marketing plan or strategy for each segment is justified. For example, by using "company size" as the segmentation variable, a large company, manufacturing and marketing electric motors, segmented the market. The company selected large and medium sized customer as the target markets.

4. Accessible: Not all profitable segments are positively exploited as the in house expertise and finance must permit the organization in this case.

5. Appropriate: It should be appropriate to the organization's objectives and resources.

6. Stable: This would ensure that its behavior in the future can be predicted with a sufficient degree of confidence.

4.5 TARGETING

After segmentation, the market into various potential segments, the company should evaluate the various segment, thereafter it should select the target segment and decide which market strategy it will adopt.

An industrial market should evaluate the different market segment by using following 4 factors

1. Size and growth
2. Profitability Analysis
3. Competitive Analysis
4. Company objectives and resources

1. Size and growth: A company should find, what is the size of each market segment by using demand forecasting methods such as

- Time series Analysis
- Regression Analysis

- Econometric Models
- Sales force estimates
- Expert opinion

Growth characteristics of market segment worked out once a long term demand (Market potential). This analysis will indicate what is the size and the estimated market growth of each segment.

2. Profitability Analysis: There are 3 elements involved in profit. They are as follows:

- Quantity and value of product of total market for a specific period of time
- Sales forecast- Sale
- Profitability- Difference between estimated sales revenue and market cost

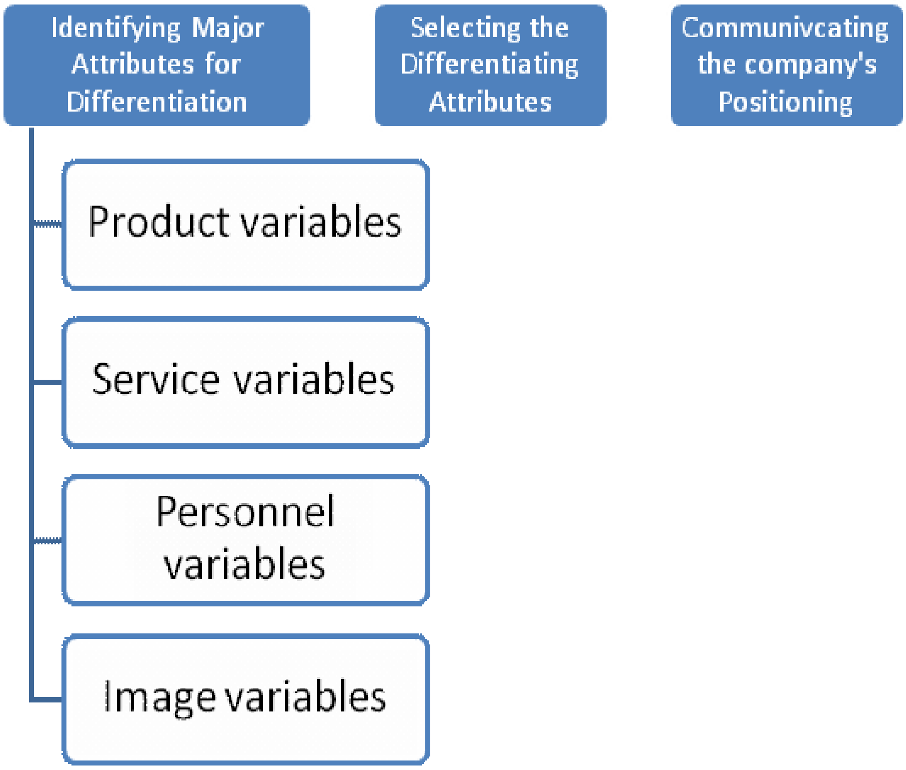
3. Competitive Analysis: Profit potential and the ability of an industrial marketer to penetrate a particular market segment depends on a careful analysis of the strengths and weaknesses of existing and or potential competitors must be assessed in each market segment with respect to areas of manufacturing, R&D, finance, technical services, product quality, delivery performance, sales force, advertising, distribution, technology and organization/management reputation.

4. Company Objectives and Resources: An industrial firm should ask itself whether each potential segment is in line with the firm's long term objectives. If not, such segment should be eliminated. Besides, a company will succeed in a segment if it has certain resources which are superior to competitors. This strength should be in line with the success factors for each segment.

4.6 POSITIONING

Positioning is a marketing strategy that aims to make a brand occupy a distinct position, relative to competing brands, in the mind of the customer. Companies apply this strategy either by emphasizing the distinguishing features of their brand (what it is, what it does and how, etc.) or they may try to create a suitable image (inexpensive or premium, utilitarian or luxurious, entry-level or high-end, etc.) through advertising. Once a brand is positioned, it is very difficult to reposition it without destroying its credibility. It is also called product positioning.

Positioning is one of the most powerful marketing concepts and the meaning of positioning was rather limited in the earlier years when marketing was just getting started which focused on the concept of reputation. Positioning then became "the place a brand occupies in the mind of its target audience". Under this meaning many companies now use the concept of positioning as a part of their everyday marketing activities or strategies and is also used as a tool for explaining how consumers can relate to foreign markets easier.



Procedure for Developing a Positioning S trategy

1. Identifying Major Attributes for Differentiation: The purpose of doing marketing research is to understand which are the major factors or attributes the target customer organizations consider important while making buying decisions for a product. The industrial firm should also understand the customer's perceptions regarding the various competing products with respect to the major attributes. An industrial marketer can use several variables to differentiate its products from competing products. These are

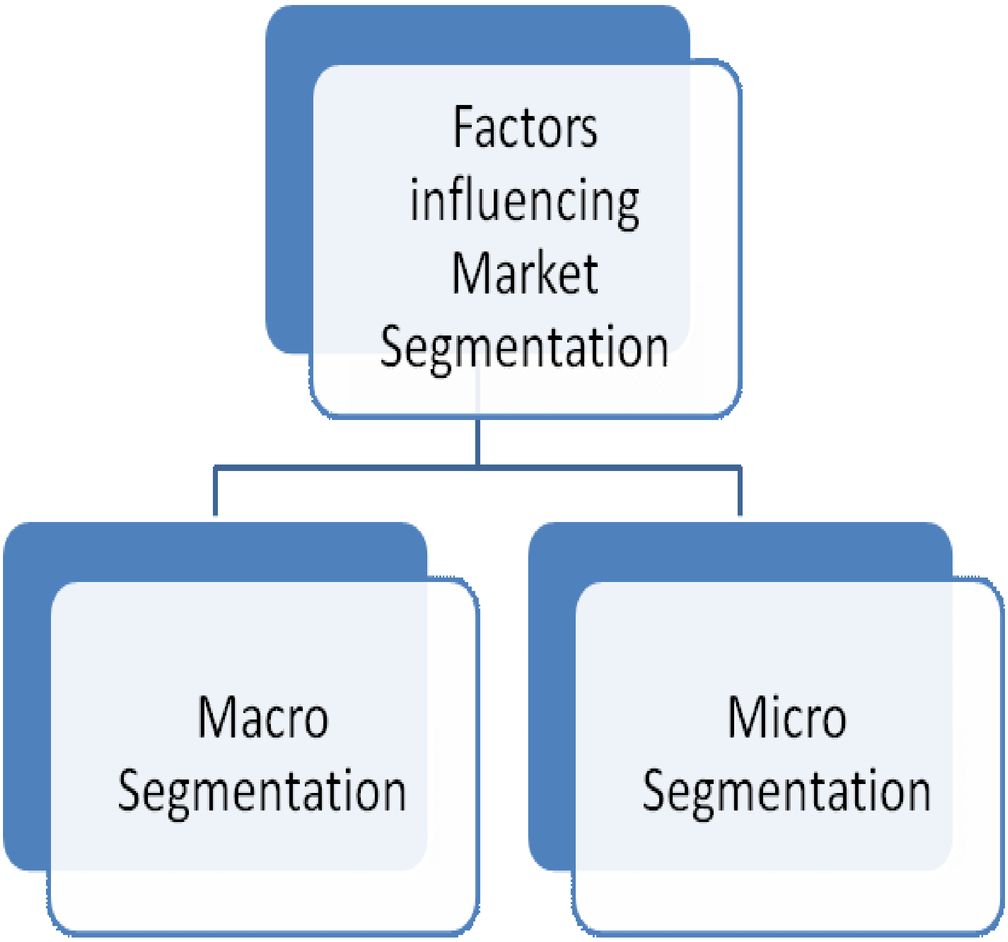
- Product variables
- Services variables
- Personnel variables
- Image variables

2. Selecting the Differentiating Attributes: The industrial marketer has to decide how many and which attributes should be selected in order to differentiate the company or the product from its competitors. Many companies select one benefits or attribute, like, "best quality" or "best Service" or "most advance technology". However, some companies believe in double benefits positioning, and there are few companies who promote three benefits.

In deciding the positioning strategy the industrial marketer should consider three important factors after conducting marketing research. First, which are the most important attributes that target customers consider while deciding to place orders for a product or services? Second, how the target customers perceive the company's product or service with respect to the important attributes. Third, how the target customers perceive the competitors product or services with respect to the same attributes.

3. Communicating the Company's positioning: Industrial marketers not only decide the positioning strategy, but also endeavor to communicate the same effectively to the target markets. Communication plays an important role in positioning the industrial market.

4.7 FACTORS INFLUENCING BUSINESS MARKET SEGMENTATION



1. Macro Segmentation

Macro segmentation approach consists of identifying the macro variables on the basis of industry characteristics or organizational characteristics such as type, size, geographic location, or product application. Most of the macro segmentation variables are easy to identify. The information on macro variables can be obtained through secondary sources of information such as trade directories, business magazines, government publications and company sources. Some of the macro variables used for industrial market segmentation are classified into

A. Industry characteristics

b. Organizational characteristics

A. Type of industry or Customer: Many industries firms market their product or services to different "type of industries". These industries are classified by Standard Industries Classification (SIC) by government publications.

For example, a marketing research firm decided to segment is market based on "industry type" so as to develop special industry- wise knowledge and information for giving better value to its customers in a competitive market. The company used the SIC codes to club different industries into homogeneous group such as engineering industries, chemical, petrochemicals and fertilizers industries, agricultural and food processing industries, service organization such as banks, hotel, trade associates and tourism. Each industrial group was looked after by a separate team to achieve the objectives stated earlier.

Significant differences such as product or service requirement may also be present within an industry. In such instances, further subdividing of individual industries may be necessary to obtain a more detailed segmentation scheme.

Type of customers like Government, commercial, cooperative and institutions.

B. Organizational Characteristics: The "size" of the customer organization is an important macro-variable used to segment the market. Large organizations have different purchasing requirement and will respond differently to marketing strategies or programmes as compared to smaller firms that purchase in smaller quantities. Similarly, large firms may avoid buying from small scale organizations as their large volume needs may not be met by the small firms.

Another important segmentation variable is "Customer location". In industrial marketing, the geographical location of customers is an important factors in serving the needs of on time delivery due to factors like transportation time, inventory control, availability of warehouse facilities, or prompt after sales services. Some industrial marketers may avoid those customers or markets which are too away or too dispersed, considering the high cost of marketing efforts such as deployment of sales force, ware housing facility or service centers.

2. Micro Segmentation

Micro segments are homogenous group of customer within the macro segments. Thus, industrial marketers subdivide macro segments into micro segments only if necessary. Micro segment variables are based on the purchasing decision. The data of information required for developing micro segmentation is more difficult and costly as it has to be obtained through company sales persons or by conducting market surveys.

A. Buy Phases: Micro segmentation is also done based on customer interaction needs for complex products such as computer hardware and software, and capital goods. The duration and involvement of buyer seller discussions will depend on whether buyers are capable of determining their own needs or are seeking help of suppliers. The resource allocation of people, time and money will vary on customer interaction needs.

B. organizational Capabilities: Micro segmentation is also based on organizational capabilities, such as financial, technical, or operational. For example, companies that are financially weak may be attracted by longer credit terms or volume discounts as compared to product quality or delivery factors. Companies that are technically not strong depend on technical information and support from suppliers. Organizations that operate on tight inventories may look for suppliers who give prompt and quick deliveries.

C. Purchasing Policies: Purchasing policies is another micro segment variable used to segment customers based on their purchasing policies or practices. The government organizations have a standard purchase policy of tender bidding and orders are placed based on lowest price bids. Large and small organizations in the private sectors have different purchasing policies.

D. Purchasing Criteria: The markets can also be segmented on the basis of purchasing criteria used by buyer organizations. For example, if products are standard, economic criteria such as price, payment terms, inventory carrying costs, inspection and rejection costs, dominate in purchase decisions. For non standard, complex or new products, performance and application criteria dominate in purchase decision.

E. Personal Characteristics: Personal characteristics should be focus on customer based on the personal characteristics of buying center members such as risk takers, risk avoiders or personal motives.

4.8 NOTES

4.9 SUMMARY

One of the most important strategic marketing decisions an industrial markets makes is with respect to market segmentation, target marketing, and positioning.

In market segmentation a business firm decides whether it can serve the entire market or a part of the whole market more effectively than the competitors. Major variables used for segmenting industrial markets are macro variables and micro variables.

For each selected target segment, a firm decides the positioning strategy by clearly differentiating its products or services in the relation to the competitors.

4.10 KEYWORDS

- Market
- Segmentation
- Targeting
- Positioning
- Variables

4.11 SELFASSESSMENT QUESTIONS

1. What is industrial market segmentation?
2. Explain the strategies of market segmentation
3. Discuss the Factors affecting industrial market segmentation
4. Explain the concept of Targeting and positioning

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MODULE – II
ORGANISATIONAL BUYING

UNIT - 5 : CHARACTERISTICS OFORGANISATIONAL BUYING

Structure:

5.0 Objectives

5.1 Intoduction

5.2 Characteristics of Organisational Buyers

5.3 Organisational Buying Situations

5.4 Meaning of Organisational Buying

5.5 Features of Organisational Buying

5.6 Objectives of Organisational Buying

5.7 Definitions of Organisational Buying

5.8 Nature of Buying

5.9 Factors Influencing Organisational Buying

5.10 Notes

5.11 Summary

5.12 Key Words

5.13 Self Assessment Questions

5.14 ReferenceS

5.0 OBJECTIVES

After studying this unit, you should be able to;

- Define organizational buying.
- Explain the organizational buying situations.
- Highlight the characteristics of organizational buyers.
- Discuss the features of organizational buying.
- Evaluate the factors influencing organizational buying.

5.1 INTRODUCTION

Organizations buy to satisfy rational needs that result from their desire to be successful in their markets; however, it is individuals within organizations who make the buying decisions. Those individuals have a stake in the outcome of the purchase decisions and desire to influence the decision process.

Organizational buying adds extensions and entirely new dimensions to the traditionally studied consumer buying process. In marketing decisions, purchasing managers must coordinate with numerous people with diverse organizational responsibilities who apply different criteria to purchasing decisions. Developing effective marketing strategy to reach organizational buyers rests on the industrial marketer's understanding of the nature of organizational buying.

Effective industrial marketing strategy must begin with an understanding of industrial buying behavior. This entails knowledge of the different types of buying situations that organizations encounter, the process that organizational buyers go through in reaching purchasing decisions, how those decisions are affected by different members of the firm and the criteria they apply in making purchasing decisions.

Organizational buying is the decision-making process by which formal organizations establish the need for purchased products and services and identify, evaluate, and choose among alternative brands and suppliers.

The buying is done by an individual consumer or his family as well as by various types of formal organizations. In Indian context such organizations are government, semi-government institutions, various departments of government like post offices, railways, public sector undertakings, public and private limited companies in the private sector (whether in manufacturing or service sectors), NGO (mostly organized under Indian Societies Registration

Act), cooperative societies and autonomous bodies like electricity boards, development authorities and corporations.

Numbers of international organizations like World Bank, ILO, WHO, FAO are also operating in India besides there are offices of foreign diplomatic missions. All these and other organizations have to buy both consumable and non-consumable items. Though their share in purchases of various items is not known, they play a dominant role in certain sectors like government, railways, and electricity boards.

These organizations buying behavior is much different than that of consumers. They go more by price, quality and performance and other factors which influence general consumers play very little role. Therefore, it has certain distinct features and their decisions are more rational. The role of psychology in organizational and industrial buying is very limited.

Hence organizational buying behavior is studied separately. The organization buying behavior refers to decision making processes in formal organizations". In the earlier models the research was confined to study vendor selection. But now the scope has been widened and includes strategic alliances, communication between vendor and buyer, processes of selection of product.

It includes intra-firm processes and sourcing process and the role of the technicians and executives of the buying firm. There are many authors who have com-pletely ignored organizational buying behavior and many others have dealt it casually with very little description. But in today's economic system organizations are big buyers for many consumer products including fast moving products like food items (hotels, caterers, office canteens), office stationery, refrigerators, and many services like courier, transport, insurance for employees and their assets and so forth. Moreover, it should not be forgotten that organizations buying decisions are also influenced by brand image and other factors.

5.2 CHARACTERISTICS OFORGANIZATIONAL BUYERS

1. Consumer market is a huge market in millions of consumers where organizational buyers are limited in number for most of the products.

2. The purchases are in large quantities.

3. Close relationships and service are required.

4. Demand is derived from the production and sales of buyers.

5. Demand fluctuations are high as purchases from business buyers magnify fluctuation in demand for their products.

6. The organizational buyers are trained professionals in purchasing.

7. Several persons in organization influence purchase.

8. Lot of buying occurs in direct dealing with manufacturers.

5.3 ORGANIZATIONAL BUYING SITUATIONS

5.3.1 Straight Rebuy

In this buying situation, only purchasing department is involved. They get an information from inventory control department or section to reorder the material or item and they seek quotations from vendors in an approved list.

The "in-suppliers" make efforts to maintain product and service quality. The "out-suppliers" have to make efforts to get their name list in the approved vendors' list and for this purpose they have to offer something new or find out any issues of dissatisfaction with current suppliers and promise to provide better service.

5.3.2 Modified Rebuy

In this buying situation, there is a modification to the specifications of the product or specifications related to delivery. Executives apart from the purchasing department are involved in the buying decisions. The company is looking for additional suppliers or is ready to modify the approved vendors list based on the technical capabilities and delivery capabilities.

5.3.3 New task buy

In this situation, the buyer is buying the product for the first time. As the cost of the product or consumption value becomes higher, more number of executives are involved in the process. The stages of awareness, interest, evaluation, trial, and adoption will be there for the products of each potential supplier. Only the products which pass all the stages will be on the approved list and price competition will follow subsequently.

5.3.4 Systems buy

System buying is a process in which the organization gives a single order to a single organization for supplying a full system. The buying organization knows that no single party is producing all the units in the system. But it wants the system seller to engineer the system, procure the units from various vendors and assemble, fabricate or construct the system.

5.4 MEANING OF ORGANISATIONAL BUYING

Organizational buying refers to the buying behavior of organizations that buy products for business use, resell or to make other products.

Organizations consist of business, industries, retailers, government, and non-government organizations.

Business and industries buy products for business use or to produce other products.

Resellers buy products to resell at a profit.

Government buys products for use in offices and development projects or to provide service to people.

Non-government organizations buy products to provide service to their clients. They can be hospitals, educational institutions, and political parties, religious and social organizations.

5.5 FEATURES OF ORGANISATIONAL BUYING

- **Buyers:** Fewer buyers buy large volume in geographically concentrate areas.
- **Demand:** The total demand is inelastic. It is not affected by price changes. The demand is derived from the demand for consumer goods. The demand is known as Derived Demand. It keeps on fluctuating because a small change in consumer demand results in major shift in organizational demand.
- **Relationship:** The relationship between supplier and customer is close. This is due to few and large customers.
- **Professionalism:** Professional and trained people make purchase. Purchase policies require buying instruments like quotations, tenders, contracts etc.
- **Channel:** Organizations generally buy direct from manufacturers. Purchasing agents are also used.
- **Buying Influences:** More participants influence buying decisions. Buying committees and evaluation committees are used. Personal selling is important.
- **Rationality:** Buyers are informed and are more rational in making buying decisions. The buying criteria can be value, quality or service.

5.6 OBJECTIVES OF ORGANISATIONAL BUYING

Organizational buyers have the following several distinct objectives in purchasing goods and services:-

- Availability of items-buyer is able to obtain items throughout the year or whenever necessary.
- Seller reliability-based on fairness to organizational consumers in allocating items in high demand.

- Consistency of quality-being able to purchase items of proper quality on a regular basis.
- Delivery goals-minimized and stabilized length of time from order placement to delivery.
- Price is only one of several considerations for organizational consumers.
- Availability, quality, service, and so on is more important.
- Manufacturers stress quality standards and may want a variety of suppliers.
- Wholesalers and retailers are interested in saleability and exclusive

  buying arrangements to limit competition.

5.6.1 Organizational Buying Structure

- Organizational Buying structure refers to the level of formality and specialization used in the purchase process
- A firm's buying structure depends on an organization's size, resources, diversity, and format.
- Manufacturers and wholesalers often have purchasing agents.

5.6.2 Organizational Constraints on Purchases

- The major constraint on purchase behaviour is derived demand.
- Availability, ability to pay, financing availability, and risk are other constraints.
- Government consumers are constrained by the budgeting process.

5.7 DEFINITION OFORGANISATIONAL BUYING

The organizational buying according to Scott Word Professor at the University of Pennsylvania, Frederick E. Webster Jr. Professor at the Dartmouth University "is the decision making process by which formal organizations establish the need for purchase of products and services, and identify, evaluate, and choose among alternative brands and suppliers".

This implies that:

(1) There should be need,

(2) There should be identification of suppliers,

(3) Different suppliers and brands should be evaluated and finally,

(4) A vendor should be selected as per procedure of the organization.

According to another author "industrial buying behavior is an explicit or implicit transactional decision making interaction".

It has following steps:

1. Need must be felt for product or service.
2. Search has to be made for suppliers and potential suppliers have to be identified.
3. Evaluate the marketing mix, product, price, promotion and distribution of potential identified suppliers.
4. Negotiate for (which may include offers, tenders) price and other purchase terms like deliv-ery, terms of payment etc.
5. Place of purchase order.
6. Receive the ordered product/service.
7. Evaluate the supplies.

Above definition is limited to industrial organizations but there are other organizations who are buyers; most of them work for profits but there are social and political organizations also who are buyers for various products required for the administrative purposes, social organizations buy many items for distribution to weaker sections of the society.

Another important feature of organizational buying behavior is that they are much more demand-ing. They expect much more complete and better response from vendors and in many cases or in case of certain items much greater reliance is placed on quality and delivery. But the price should also be competitive so that the organization may be able to produce its final product at competitive price.

For instance, a manufacturer of biscuits needs three basic inputs – wheat flour (Maida), vegetable oil and sugar. In order to produce good quality biscuits it is necessary to ensure that the quality of inputs is good. Secondly, inputs most be supplied as per delivery schedule so that production schedule of the company is not affected adversely.

There are many instances especially in Japan and now in India also where ancillary units are established to supply inputs specially in case of engineering products. But this is also true for many other inputs for other industries like textiles, tires, chemicals, consumer products etc.

In such cases great emphasis is placed on proper vendor selection and ones vendor is selected there is long buyer, seller relations. Sometimes buyer regularly visits the vendor's works to ensure that goods are being produced as per specifications and on time. Sometimes, with the passage of time these relations are converted into joint ventures.

In India Maruti Udyog has established a number of joint ventures to supply inputs. Escorts have developed a number of ancillary vendors. Thus the buying behavior of organizations is much different than that of individual consumers.

5.8 NATURE OF BUYING

Many consumer purchases (i.e., buying decisions) are spur of the moment, often associated with the availability of funds to make the purchase. While consumers seldom conduct a conscious value evaluation, by making the purchase they have decided that the value they are about to receive is greater than the value they are giving up (i.e., their costs). If this were not the case, the exchange would not take place. The value assigned by the customer is influenced by many factors beyond the serviceability of the core product or service. The nature of the buyer decision process in a business-to-business environment is not unlike the consumer process, though the steps are often thought to be more visible and theoretically more quantifiable.

5.8.1 Industrial Buying On the Internet

Advancement in information and communication technology has brought tremendous change to business-to-business (industrial) marketing process. Before the advent of modern world (information and communication technologies), all businesses were transacted on face-to-face interactions. But today, technology has made it possible for transaction to take place without the buyer knowing the face of the seller. One of such technologies is the internet. Thus, on-line purchasing also called, e-procurement has advanced rapidly. There are associated advantages of on-line procurement.

(i) It has given buyers more access to new supplies and suppliers.

(ii) It has reduced administrative, operation and purchasing costs.

(iii) It facilitates order processing and delivery.

(iv) It creates greater opportunity for information accessibility.

(v) It builds sound customer relationship.

(vi) It reduces paper work associated with traditional ordering and re-ordering procedures and also reduces order lead-time.

However, e-purchasing or e-procurement poses a security threat to organizations.

5.8.2 Distribution of Industrial Products

Basically, two marketing channels exist for industrial products, namely direct, and indirect marketing channels. Direct marketing channel of distribution involves a platform on which industrial products are delivered directly to the buyer rather than engaging the services of middlemen.

Products involve in this type of channel are bulky, expensive and can be purchased by few buyers. Indirect marketing channel involves the activities of middlemen and company representatives in pushing the user.

5.8.3 Pricing in Industrial Marketing

Pricing has been given serious and extensive deliberation in this book. Pricing in consumer market is similar to pricing in industrial market. For elaborate explanations see "Pricing" in chapter four.

Factors Determining the Price of Industrial Products

(i) The cost of the product (considering variable, marginal and fixed costs).

(ii) Degree of competition.

(iii) Ability, readiness and willingness of customer to pay.

(iv) Activities of marketing intermediaries.

(v) Government legislation.

(vi) Company's pricing policies and objectives.

5.8.4 Pricing Objective

Pricing objectives are the targets or ends a firm seeks to achieve through its pricing practices. Below are pricing objectives which an industrial marketer can purse:

- Profit maximization
- Satisfactory rate or return [Rate of return on investment (ROI) or rate of return on capital employed (ROCE)].
- Price stabilization
- Customer welfare
- Early cash recovery or payback period
- Increased sales or market penetration
- Market share objective.
- Destroy or prevent competition.

- Promotional pricing.

5.9 FACTORS INFLUENCING ORGANIZATIONAL BUYING

5.9.1 ENVIRONMENTAL FACTORS

Environment factors affect organizational buying behavior. This includes economic, technological, political-legal, social responsibility and competition.

1. Economic factors: Economic factors affect organizational buying behavior. This includes level of demand and economic health. The level of demand includes capacity and desire for buying goods. This is affected by income distribution and price of product. Prosperity, recession and recovery are included in economic health. The prosperity condition is economically good condition. Recession is economically bad condition.

2. Technological factors: Technological factors also affect organizational behavior. This includes level of technology, pace of technology, technology transfer etc. E-commerce as well as information technology has got revolutionary change. It has directly affected organizational buying behavior.

3. Political and legal factors: Political and legal factors also affect organizational buying process directly. Political factors include political system, political situation, and political thought, government policies etc. whereas constitution, laws, rules and regulations etc. are included in legal factors.

4. Social responsibility: A business organization should consider social responsibility while buying any goods or services. Indigenous goods should be given preference in buying and interest of society should be protected. Interest of different pressure group of the society also should be considered while buying goods or services.

5. Competition: Competition also affects buying behavior. This competition includes pure competition, monopolistic competition and oligopoly competition.

Expected demand for the product that the buying organization is selling, expected shortages for the item, expected changes in technology related to the item etc. are the other environmental factors that will have an effect.

5.9.2 ORGANIZATIONAL FACTORS

Organizational factors also affect organizational buying behavior. This includes objectives, policies, procedures, organizational structure and system.

1. **Objectives:** Buying objective is determined according to organizational goal. Goods should be purchased according to organizational objective. As goods or services need to be purchased according to organizational goal, buying is affected by objective.

2. Policies: Purchasing or buying policy also effects organizational buying behavior. Goods should be purchased according to buying policy of the organization. If the organization has the policy of buying indigenous goods, the buyer cannot buy foreign goods. If the purchasing policy is silent in this matter, whichever goods, foreign or indigenous, can be purchased as desired.

3. Procedures: The methods and process adopted by an organization to buy goods or services is called procedure. Goods or services can be purchased directly through agreement, or through tender, demanding catalogue etc. Any of the method can be adopted to buy goods or services. Whichever procedure the organization has adopted, the buyer should follow it.

4. Organizational structure: Organizational structure defines authority and relations which directly affects buying behavior. In some organizations, goods or services are purchased by direct order of chief executive while in some other organizations, goods or services are bought through purchase department. So, buying behavior is affected by organizational structure.

5. System: Purchasing system also directly affects buying behavior. An organization can adopt any one or more such as centralized system, decentralized system, huge quantity purchase system and others.

Changes in purchasing department organization like centralized purchasing, decentralized purchasing and changes in purchasing practices like long-term contracts, relationship purchasing, zero-based pricing, vendor-performance evaluation are the other organization factors of importance to marketers.

5.9.3 INTERPERSONAL FACTORS

Interpersonal factors also affect buying behavior. This includes authority, status, interest etc.

1. Authority: The personnel whom the organizational structure gives authority to order for purchase, no goods can be purchased without his order. Buying decision of such authority plays an important role in buying.

2. Status: The persons to purchase goods or services and to give order for purchase may be different in an organization. As much the behavior of the person issuing purchase order affects behavior of the buyer. If the status or level of the buyer is high, his buying decision becomes rational and quick. His/her behavior becomes mature.

3. Interest: Users, influencers, buyers, decider and gate keeper are involved in organizational buying process. Their interest affects organizational buying process. As their interest becomes different, buying process may be complicated.

5.9.4 PERSONAL FACTORS

Personal factors also affect buying behavior. This includes age of person, education, level of job, personality etc.

1. Age: Age of person also affects selection and priority. Younger persons make buying decision and supplier selection quicker than older aged persons. Similarly, the younger persons try to find new suppliers whereas older persons try to give continuation to the same who is supplying. So this also affects buying process.

2. Education: Education makes person able to analyze good or bad. So, an educated person takes buying decision rationally whereas uneducated person makes buying decision at hit and miss/ or hunch. Educated person selects goods or services carefully. So, buyer's education also affects organizational buying behavior.

3. Job position: Job position also shows a person's status. Buyer's position or status also affects his buying behavior. Buyer's status may be low or high.

4. Personality: Personality of person working in an organization may be different. Personality affects selection of quality, brand, price etc. So, buyer's personality also affects organizational buying behavior.

5. Risk attitude: Risk bearing capacity of men becomes different. Some can bear more risk and others like to take less risk. Similarly, some like to avoid risk and some others like to face. The capacity and attitude to bear risk also affect buying behavior. The buyers having the capacity to take high risk become aggressive. But those having less risk bearing capacity and having no risk bearing capacity do not do so.

5.10 NOTES

5.11 SUMMARY

Insight into how industrial organizations purchase goods and services enables the industrial marketer to reach the right influencers with information that satisfies their various needs. Organizational purchasing is a problem-solving process that evolves in sequential steps. The level of a firm's experience with purchasing problems is the key to how the marketer should define the buying situation. In this unit, has pointed out that each purchasing situation new task, modified, or straight rebuy requires a different type of response from the industrial marketer. In developing marketing strategy, industrial marketers must be aware of the concept of "creeping commitment" and recognize that some phases in the purchasing process are more critical than others. Influencers involved in these phases tend to have more power in affecting the final choice. Marketing efforts must, therefore, be concentrated at these critical phases, and marketers must be continually on the search for who is making what decisions based on which criteria.

5.12 KEYWORDS

- ♦ Straight rebuy
- ♦ Modified rebuy
- ♦ New task rebuy
- ♦ Environmental factors
- ♦ Personal factors
- ♦ Organizational factors
- ♦ Interpersonal factors
- ♦ Buying influences
- ♦ Professionalism

5.13 SELFASSESSMENT QUESTIONS

1. Define organizational buying.
2. Briefly explain the organizational buying situations.
3. What are the factors influencing organizational buying? Explain.
4. Discuss the features of organizational buying.
5. What are the characteristics of organizational buyers?

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UNIT - 6 MODELS OF BUYER BEHAVIOUR

Structure:

6.0 OBJECTIVES

After studying this unit, you should be able to;

- Outline the models of buyer behavior.
- Discuss the buying phases.
- Assess the buyer center roles.
- Explain the buying center concept.

6.1 INTRODUCTION

Organization buying is the decision-making process by which formal organizations establish the need for purchased products and services and identify, evaluate, and choose among alternative brands and suppliers.

Organizational, Buying depends on

1. Buying objectives
2. Buying structure, and
3. Purchase constraints.

Understanding buyer behaviors plays an important part in marketing. Considerable research on buyer behavior both at conceptual level and empirical level has been accumulated. There are two types of buyers:

- Industrial (organizational) buyer
- Individual consumer

Organizational buying behavior has many distinctive features "

- First, it occurs in a formal organization which is caused by budget and cost.
- Second, in some conditions, joint decision-making process may occur, and this is not possible in individual buying behavior.
- Finally, conflict occurs and they are hard to avoid in the joint decision making process.

  In order to understand the organizational buying behavior, we first consider who will be involved in the buying process and what their expectations are. At least, purchasing agents, engineers, and final consumers will participate in the buying process.

  The potential of different decision maker are different in different situations. In this model, there are five different sets of variables determining the expectations of the individual

The individuals' background, information sources, vigorous search, the selective bend of the information based on their previous information and expectations, satisfaction with previous purchase.

Except the perceptual distortion, the other four variables that is easy to gather information.

The second part of the model is regarding the industrial buying processes " Independent decision which means that the decision is delegated to one department, joint decision processes.

The product-specific factors (the perceived risk, the type of purchase, and time pressure) and the company-specific factors (company orientation, company size, and degree of centralization) will determine the type of factor.

The greater the apparent risk, the more preferred to joint decisions. If it is a life-time capital buy, the more likely the joint decision will take place.

If the decision has to be made at an emergency, it is likely to entrust to one party. A small and privately-owned company with product or technology orientation will lean towards independent decisions.

While a large public company with decentralization will tend to have joint decision process.

6.1.1 ECONOMIC MAN MODEL

In this model, consumers follow the principle of maximum utility based on the law of diminishing marginal utility. Economic man model is based on the following effects "

- **Price Effect** " Lower the price of the product more will be the quantity purchase.
- **Substitution Effect** " Lower the price of the substitute product; lower will be the utility of the original product purchase.
- **Income Effect** " When more income is earned, or more money is available, quantity purchased will be more. The economic theory of buyer's decision-making was based on the following assumptions:

As consumer resources are limited, he would allocate the available money which will maximize the satisfaction of his needs & wants.

Consumers have complete knowledge about the utility of each product and service, i.e., they are capable of completing the accurate satisfaction that each item is likely to produce.

As more units of the same item are purchased the marginal utility or satisfaction provided by the next unit of the item will keep on decreasing, according to the law of diminishing marginal utility.

Price is used as a measure of sacrifice in obtaining the goods or services. The overall objective of the buyer is to maximize his satisfaction out of the act of purchase.

The dynamic economic conditions are affecting buyer behaviour, their perceptions and attitudes. Buyers are changing their behaviour in several different ways, situations and various primary attitudes and values which express these changes. It is vital for us to re-look at the buyer and bring back our understanding to well alter the marketing strategies.

Not all the buyers react to the environmental changes in the same way. Different buyers have different reactions to the economic challenges. Reduction may be reflected in different tangible and psychological ways or modes.

Manufacturers also need to offer a variety of different solutions and propositions to meet these changes in their behaviour. Therefore, different consumer segments may be affected at different levels and growth may vary from segment to segment.

A stressed economic situation not only changes the buyer, but also changes the sellers. Consumers are normally more close to the brand than the retail store, hence their first option is not to change the brand, but try to find the brand at a cheaper price at another store.

With more time at hand and greater incentive to economize, more consumers are likely to shop at overexcited markets than the pricier supermarkets and ease stores. The search for value and bargains will also turn the shoppers to online shopping – the only channel that will grow even faster than overexcited markets.

6.1.2 LEARNING MODEL

This model suggests that buyer behavior is based on some core concepts " the drives, stimuli, cues, responses and reinforcements which determine the human needs and wants and needs satisfying behavior.

- **Drive** – Drive is a strong internal stimulus which compels action.
- **Stimuli** " Stimuli are inputs which are capable of arousing drives or motives.
- **Cues** " Cues is a sign or signal which acts as a stimulus to a particular drive.
- **Response** – Response is the way or mode in which an individual reacts to the stimuli.

If the response to a given stimulus is "rewarding", it reinforces the possibility of similar response when faced with the same stimulus or cues. Applied to marketing if an informational cue like advertising, the buyer purchases a product (response); the favorable experience with the product increases the probability that the response would be repeated the next time the need stimulus arises (reinforcement).

6.1.3 THE PSYCHOANALYTIC MODEL ” the model suggests that human needs operate at various levels of consciousness. His motivation which is in these different levels, are not clear to the casual observer. They can only be analyzed by vital and specialized searching.

6.1.4 SOCIOLOGICALMODEL – This model is concerned with the society. A buyer is an element of the society and he may be a member of many groups and institutions in a society. His buying behavior is influenced by these groups. Primary groups of family friend's relatives and close associates extract a lot of influence on his buying. A buyer may be a member of a political party where his dress norms are different from different member. As a member of an elite organization, his dress needs may be different, thus he has to buy things that confirm to his lifestyle in different groups.

Word-of-mouth can be a powerful pressure on buying behavior, and marketing strategies are designed to influence word-of-mouth. The increasing status, power and use of social media helps marketers to take more benefit to reference groups in helping them to spread messages about their products and services.

In general, buyer searches to increase satisfaction and evade pain. They wish to reduce the risk of decisions they make and will spend more time in researching the purchase decisions that signify a higher level of risk.

For example, low-cost and low-involvement products like shampoo will require less efforts and worry on the part of consumers than high-cost and high-involvement products like cars, computers or homes.

Buyer involvement influences how consumers collect, understand and convey information, make buying decisions and make post-purchase evaluation. As the level of consumer participation increases, the consumer has better motivation together, comprehend, elaborate, justify and understand the information. Thus, a marketer needs to understand the process in a proper manner and design his marketing mix in a manner that can trigger the involvement process in his favor.

Example ofABC Fancy Dream Stores

Three facts were discovered by a survey done on a Fancy store which was particularly disturbing which are as follow “

People found ABC Fancy Stores to be less friendly and helpful, as customers were generally not allowed to search by themselves. Children got bored and hence parents often left the store within few minutes after finishing their necessary shopping. They never browsed, searched or spent spare time at Fancy Dreams stores, which could actually help in promoting more sales.

With lots of choices available in the market, consumers stopped up treating Fancy Dreams stores as unique and exclusive anymore.

6.1.5 STIMULUS-RESPONSE MODEL

Organizations are increasingly concerned in retaining existing customers while targeting non-customers. Measuring customer satisfaction provides an indication of how successful the organization is at providing products and/or services to the market place.

With the advent of technology, consumers now have access to all kinds of information regarding every product and service they want to avail. Consumers have become smarter, their tastes and preferences have changed. What used to be the luxuries of life has now become the necessity.

The competition has increased and brands are struggling to beat the competition. Let us examine some of the issues in the field of consumer behaviour that has emerged these days because of the overall advancement of technology and people.

A well-developed and tested model of buyer behaviour is known as the stimulus-response model. In this model, marketing and other stimuli enter the customers "black box" and produce certain responses. Marketing management must try to work out what goes on the in the mind of the customer – the "black box". The Buyer's characteristics influence how he or she perceives the stimuli; the decision-making process determines what buying behaviour is undertaken.

6.1.6 BLACK BOX MODEL

The black box model shows the interaction of stimuli, consumer characteristics, and decision process and consumer responses. It can be distinguished between interpersonal stimuli (between people) or intrapersonal stimuli (within people). The black box model is related to the black box theory of behaviourism, where the focus is not set on the processes inside a consumer, but the relation between the stimuli and the response of the consumer. The marketing stimuli are planned and processed by the companies, whereas the environmental stimulus is given by social factors, based on the economical, political and cultural circumstances of a society. The buyer's black box contains the buyer characteristics and the decision process, which determines the buyer's responses.

6.2 BUY PHASES

In the **first phase** that is recognition of problem, the buying process starts when person in organization identifies problem or need that can be met by obtaining goods and services. The buying centre examines their organizational needs and search for options that are available to address those needs. The definition stage includes several activities such as recognizing and defining the organizational problem, defining the outlines of the solution and specifying product or service that can satisfy organizational needs (Webster & Wind 1996).

Phase two include description of need which involves determination of traits and quantities needed. The common attributes include reliability, durability and price. Activities in this stage are searching of potential suppliers, proposal solicitation, and evaluation of offers and finally selection of most appropriate supplier. It must be established that in case of straight rebuy, organization will probably decide the same supplier (resort, travel agency), even if it is not the cheapest one, but because of the awareness of service and safety. However, in a new-task situation, the company is willing to seek carefully, considering both financial and service factors (Vitale et al., 2010).

Phase three is product specification or delivery solution stage which is obtaining the inputs from previous stage. The buying organization has to develop the technical specification of the required products. In this stage product is divided into two items. The specification about product and items are listed.

Phase four is supplier search among the potential sources. The marketers have to ensure that the supplier is in the list of potential suppliers.

In **fifth phase** of Proposal solicitation, the list of capable supplier is shortened on the basis of critical factors. After that purchasing department ask for proposals sent by each supplier. After evaluation, some companies are invited to give presentation. Proposal must include all specification such as price, delivery period, charges and taxes.

Phase six consist of supplier selection. Each of the supplier's presentation is rated as per definite evaluation model. Buying organizations try to negotiate with chosen supplier for reasonable price and terms and conditions for final selection. Various parameters such as reliability, delivery, flexibility, price and services are considered for supplier selection.

In order to routine specification, the buyer negotiates the final order, listing the technical specification; the quantity needed and expected time of delivery.

Final phase of purchase decision process consist of formal and informal review and feedback of product performance as well as merchant performance. The buyer may contact customer and collect their responses

6.3 BUYING CENTRE

The concept of buying centre was first originated by Robinson, et, al. It entails to all those members being a part of buying process. The main feature of industrial buying is a group activity. Usually people from various areas of business and of different status contribute to the final purchase decision. Group of individuals with a stake in the buying decision is called buying centre Anderson and Kozulya affirmed that developing relationship with buying centre defines the victory of partnership between marketers and corporate customers in general.

There are four vital things for the sellers to realize:

(i) Who are the members of buying centre?

(ii) What kind of decisions are they responsible for?

(iii) What influence degree they obtain?

(iv) What assessment criteria they use?

Johnston and Bonoma developed five structural and interactive dimensions of the buying centre that can be specified and determined.

The buying center is a collection of individuals with a stake in the buying decision, individuals who contribute to the final purchase decision. Members of the buying center determine, within their own specialties, the organization's needs and the methods the organization uses to satisfy them. Buying center complexity changes depending on the complexity of the need. Contrary to what the term implies, a buying center is not one central location where buying decisions are made. The term is simply marketing jargon for the representatives of the various independently operating portions of an organization (finance, production, purchasing, engineering, etc.) that influence the selection of the best solution for the organization's needs.

Depending on the size and complexity of the organization, influencers (stakeholders) in the decision may be physically located a great distance across locally, nationally, internationally, etc.) from each other. One of the major tasks of the business marketer is to simultaneously but individually influence all stakeholders by satisfying their individual professional and personal needs.

The needs of the organization are determined by customer needs, internal goals and objectives, and by external environmental factors. Stakeholders are accountable for the development of buying requirements that satisfy all of these influences.

Depending on the intended market and customers of the organization, influences may include government agencies and independent standards-setting organizations and publics, as well as the quantifiable and relationship needs of the vendor and the customer.

The professional needs of engineering or technical specialists in the buying center are related to the physical performance of the product that is being supplied. Their concerns center on how well the component will meet design requirements and reliably perform in their application. Production or manufacturing specialists in the buying center are concerned with how well the component will integrate into their manufacturing process.

Service professionals are interested in how and what service the component will require when the product is in the field. If the purchase is a significantly large investment, the customer's finance organization is concerned with alternatives to fund the purchase. Each member of the buying center has a concern unique to his responsibilities and presents an opportunity for the business marketer to demonstrate a unique value of the offering his company seeks to provide.

6.3.1 MEANING

The concept of the buying center provides rich insights into the role of group forces in organizational buying behavior. The buying center consists of individuals who participate in the purchasing decision and share the goals and risks arising from the decision. The size of the buying center varies, but an average buying center includes more than 4 persons per purchase; the number of people involved in all stages of one purchase may be as many as 20.

The composition of buying center may change from one purchasing situation to another and is not prescribed by the organizational chart. A buying group evolves during the purchasing process in response to the information requirements of the specific situation. Because organizational buying is a process rather than an isolated act, different individuals are important to the process when product specifications are being established; others may assume a more dominant role in later phases.

The buying center is large, slow to decide, uncertain about its needs and the appropriateness of the possible solutions, more concerned about finding a good solution than getting a low price or assured supply, more willing to entertain proposals from "out" suppliers and less willing to favor "in" suppliers, more influenced by technical personnel and less influenced by purchasing agents.

6.3.2 BUYING CENTRE CONCEPT

Webster and Wind in the model they proposed to describe organizational buying process identified the organizational buying process as a team process and called the team or the buying decision-making unit of the organization as buying center. The buying center consists of all persons of the organizations who are involved in the buying process playing one or the other seven roles: Initiators, Users, Influencers, Deciders, Approvers, Buyers, and Gatekeepers.

A marketer can also predict the composition of the buying center by projecting the effect of the industrial product on various functional areas in the organization. If the procurement decision will affect the marketability of a firm's product (for example, product design, price), the marketing department will be active in the process. Engineering will be influential in decisions about new capital equipment, materials and components; setting specifications; defining product performance requirements; and qualifying potential vendors. Manufacturing executives will be included for procurement decisions that affect the production mechanism (for example, materials or parts used in production). When procurement decisions involve a substantial economic commitment or impinge on strategic or policy matters, top management will have considerable influence.

6.4 BUYING CENTER ROLES

Members of the buying center assume different roles throughout the procurement process. Frederick Webster Jr. and Yoram Wind have given the following labels to each of these roles: users, initiators, buyers, deciders and gatekeepers.

- **Initiators:** Initiators are the persons who request the purchase. The safety officer may initiate the request for the purchase.
- **Users:** Users are the persons who use the item. Say for safety gloves the operators. As the role name implies, users are the personnel who use the product in question. Users may have anywhere from inconsequential to extremely important influence on the purchase decision. In some cases, the users initiate the purchase action by requesting the product. They may even develop the product specifications.
- **Influencers:** Persons who held define specifications. In this case of safety gloves, the safety officer may himself define specifications. If an industrial engineer is in the organization, he may also be consulted. There can different gloves for different working situations and industrial engineer may be more aware of specific requirements due to his special nature of work - human effort engineering.

Influencers affect the purchasing decision by supplying information for the evaluation of alternatives or by setting buying specifications. Typically, those in technical departments, such as engineering, quality control, and R&D, are significant influencers on the purchase decision. Sometimes, outside individuals can assume this role. For high-tech purchases, technical consultants often assume an influential role in the decision process and broaden the set of alternatives being considered.

- **Deciders:** Deciders are the people who decide on product requirements and suppliers. It is the final approval for product specifications and suppliers' list. Deciders actually make the buying decision, whether or not they have the formal authority to do so. The identity of the decider is the most difficult role to determine: Buyers may have formal authority to buy, but the president of the firm may actually make the decision. A decider could be a design engineer who develops a set of specifications that only vendor can meet.

The buyer has formal authority to select a supplier and implement all procedures connected with securing the product. More powerful members of the organization often usurp the power of the buyer. The buyer's role is often assumed by the purchasing agent, who executes the administrative functions associated with a purchase order.

One person could assume all roles, or separate individuals could assume different buying roles. To illustrate, as users, personnel from marketing, accounting, purchasing, and production may all have a stake in which information technology system is selected. Thus, the buying center can be a very complex organizational phenomenon.

- **Approvers:** Approvers are the persons who approve the purchase. In the case of safety gloves, the personal manager may have the power to approve.
- **Buyers:** They are the persons who actually do the buying transaction.
- **Gatekeepers:** Gatekeepers control access to personnel in a company, e.g., the receptionist, the secretaries etc. Gatekeepers control information to be reviewed by other members of the buying center. They may do so by disseminating printed information, such as advertisements, or by controlling which salesperson speaks to which individuals in the buying center. To illustrate, the purchasing agent might perform this screening role by opening the gate to the buying center for some sales personnel and closing it to others.

6.5 NOTES

6.6 SUMMARY

Industrial buying behavior is an intricate practice which involves many persons, multiple goals and potentially incompatible decision criteria. This process denotes to the purchase and use behavior of industrial/business goods users as well as the thoughts and decision process which take place before, during and after product buying. Thorough understanding the organizational buying process is main requirement for the development of business marketing strategy. Different models are developed to explain the notion of industrial buying behavior. Industrial buyers are more expected to purchase products directly from suppliers or manufacturers and in larger quantities, than consumers. Buying decisions of a consumer market is simple where it purely depends on the wish of consumer.

6.7 KEY WORDS

Economic man model	learning model	psychoanalytic model
Sociological model	stimulus-response model	buy phases
Influencers	gatekeepers	approvers

6.8 SELFASSESSMENT QUESTIONS

1. Explain the Economic man model. How does it affect the buyer behavior?
2. What do you mean by buy phases?
3. Explain the buy phases.
4. Describe the buyer centre roles.
5. Give a description of Learning model.

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UNIT - 7 :INDUSTRIAL BUYING

Structure:

7.0 OBJECTIVES

After studying this unit, you should be able to;

- Discuss the process of industrial buying.
- Evaluate the buyer behavior.
- Outline the industrial process.
- Explain the concept of buyer behavior.

7.1 INTRODUCTION

The stages of business buying includes recognizing the problem, developing product specs to solve the problem, searching for possible products, selecting a supplier and ordering the product, and finally evaluating the product and supplier performance. Buying B2B products is risky. Usually, the investment sums are high and purchasing the wrong product or service, the wrong quantity, the wrong quality or agreeing to unfavorable payment terms may put an entire business at risk. Making a riskier investment can yield to high returns. However, there is also a greater chance that they could lose their investment as well. This can be seen in this diagram. Those involved in the decision buying process need to weigh the risks against the expected returns. In order to entice and persuade a consumer to buy a product, marketers try to determine the behavioral process of how a given product is purchased. Understanding the nature of customers' buying behavior is important to a marketing firm if it is to market its product properly.

7.2 STEPS IN INDUSTRIAL BUYING

7.2.1 Problem recognition: The purchasing decision process is triggered by the recognition of a problem, need or potential opportunity. Such recognition may originate within the buying organization, especially when products become outmoded, equipment breaks down, or existing materials are unsatisfactory in quality or availability. It may also originate outside the buying organization with a marketer who recognizes and reveals opportunities for potential performance improvement. The marketer who initiates or becomes involved in the buying process at this phase, particularly in a new task situation, will have a distinct advantage in influencing the final decision and, thus, a greater probability of being selected as a supplier. Since research has shown that new task/problem recognition phase also offers the marketer a differential advantage over competitive suppliers.

7.2.2 General need description: Once a problem has surfaced, organizational members must determine specifically how the situation may be resolved; that is, the problem and solution alternatives must be narrowed and precisely analyzed. Thus, the firm will seek answers to such questions as: "what performance specifications need to be met?" "What are the application requirements?" "What types of goods and services should be considered?" and "what quantities will be needed?"

In the case of technical products, either the user department or engineering will usually prepare performance specifications. For nontechnical items, the user department might determine that products currently on the market could solve the problem. The narrowing of the problem and alternatives is, thus, a task internal to the user department. While influencers from outside the department may be used as additional sources of information, critical decisions and information needs at this phase lie chiefly within the user department.

7.2.3 Product specification: This is often a critical phase for the marketer. It is during this phase that those influencers who prepare or affect specifications enter the purchasing process. During this phase, buying influencers may change from department heads to engineers and manufacturing personnel. It is at this phase, too, that buying influencers begin to look outside the firm for suppliers and product information and for assistance in developing product specifications.

Many suppliers do not become aware that a buying situation is in progress until the firm begins its outside search for information. Because of the opportunity to develop a close working relationship with organizational influencers prior to other competitors coming on the scene, a definite advantage accrues to the marketer who triggered the need, or who is aware of the need at this point of time.

7.2.4 Supplier search: Once solutions have been identified and precisely described, a buying organization begins to search for alternative sources of supply. This leads to the qualification of suppliers. However, qualifications sought will vary with the type of buying organization, the specific buying situation, and the buying influencers involved. For example, a firm may have made its new task decision based primarily on price, with the accounting department acting as the major decision influencer. The important end result of phase 4 is that decision makers have determined which suppliers will be considered as potential vendors.

7.2.5 Proposal solicitation: When qualified suppliers have been identified, requests for specific proposals will be made. Phases 4 and 5 may occur simultaneously in a straight rebuy – buyers may merely check a catalog or contact suppliers to obtain up-to-date information about prices and deliveries. However, in more complex situations, phases 4 and 5 are separate and distinct. Many months may be spent in exchanging proposals and counterproposals. In such purchase situations, the need for information is extensive, and a great deal of time is given to analyzing proposals and comparing products, services, and costs. Thus, phase 5 emerges as a distinct component of the purchasing process.

7.2.6 Supplier selection: Various proposals of competing suppliers are weighed and analyzed. If a firm is facing a make-or-buy decision, proposals are compared to the cost of producing the needed item within the buying firm. If the buying firm decides it can produce the needed item more economically, the buying process terminates. If the firm is not facing a make-or-buy decision, one or more offers from competing suppliers are accepted. Further negotiation may continue with selected suppliers on terms, prices, deliveries, or other aspects of supplier's proposals.

7.2.7 Order routine specification: Order routine are established by forwarding purchase orders to the vendors and status reports to the using department and by determining the levels of inventory that will be needed over various time periods. While this phase begins with the placement of an order, the purchase process is not actually completed until the ordered item is delivered and accepted for use. The user department, where the need originated, does not view its problems solved until the specified product has been received and is available for use. The effectiveness of suppliers in handling this phase is, therefore, critical.

7.2.8 Supplier performance review: The final phase in the purchasing process consists of a formal or informal review and feedback regarding product performance, as well as vendor performance. This phase involved a determination by the user department as to whether the purchased item solved the original problem. If it did not, suppliers that were screened earlier may be given further consideration. Feedback that is critical of the chosen vendor or product can cause the various members of the decision-making unit to reexamine their positions. Research indicates that when, this occurs, views regarding previously rejected alternatives become more favorable.

Understanding the stages of business buying and the nature of customers' buying behaviour is important to a marketing firm if it is to market its product properly. In order to entice and persuade a consumer to buy a product, marketers try to determine the behavioural process of how a given product is purchased.

7.3 RISKS

Buying one can of soft drink involves little money, and thus little risk. If the decision for a particular brand of soft drink was not right, there are minimal implications. The worst that could happen is that the consumer does not like the taste and discards the drink immediately. Buying B2B products is much riskier. Usually, the investment sums are much higher. Purchasing the wrong product or service, the wrong quantity, the wrong quality or agreeing to unfavourable payment terms may put an entire business at risk. Additionally, the purchasing office / manager may have to justify a purchasing decision. If the decision proves to be harmful to the organization, disciplinary measures may be taken or the person may even face termination of employment.

7.4 BUYER BEHAVIOUR

In marketing process, there is a need to understand why customer or buyer purchases goods and services. Current literature associated with industrial buyer behavior that has tended to focus on modeling and mapping the industrial buyer behavior (Parkinsson and Baker, 1986). Though, limited research has been found on how the industrial buyer performs when faced with a drastic product innovation. Buyer behavior is associated with the operations and decision processes involved to select between alternatives, procuring and using products or services. It is occasionally suggested that buyer behavior is only of interest to marketers because they desire to influence and change it. Such a statement consistently raises the matter as to whether marketing is a moral profession. Industrial buyer behavior is in quintessence of understanding of how industrial organizations purchase products and services (Dwyer and Tanner, 2001). It is also identified as organizational buying process or business buying process. This field is essential to comprehend customer's needs. It is imperative to be conscious of the differences between consumer buying and industrial buying because the industrial buyer behavior varies from consumer buying in many facets such as using more variables and greater difficulty to identify process participants (Moriarty, 1984). Parkinsson and Baker (1986) explained as the buy of a product which is made to please the entire organization instead of satisfying just one individual. Industrial buying behavior is a basic concept when evaluates buyer behavior in all types of organizations. Also, in industrial buying situations there is an insight of greater use of marketing information, greater exploratory objective in information collection and greater formalization (Deshpande and Zaltman, 1987).

Process of the industrial market is totally different because the forces of market influence industrial demand. The executives of industrial market must respond in a dissimilar way to modify the markets, develop products to accommodate in changing nature of market and sell them in completely different ways to the target and new customers while retaining corporate policies. Therefore, industrial marketers face many distinct marketing situations not normally encountered in the consumer market. Additionally, the industrial market is dynamic and challenging in any nation's monetary growth and development.

7.4.1 Concept It is important to understand the reason of buying in market. Parkinsson & Baker (1986) construed that the industrial buying is the buy of a product which is made to satisfy the entire organization instead of satisfying just one individual. Industrial buying behavior is considered as being a basic concept when investigating buyer behavior in organizations. In industrial buying situations, there is an awareness of greater use of marketing information, bigger exploratory objective in information collection and greater formalization (Deshpande and Zaltman, 1987). In industrial marketing, the buying process is more complex in comparison to consumer marketing. The buying decisions in industrial marketing are based on numerous factors that include compliance with product specifications product quality, availability, timely supply, acceptable payment and other commercial terms cost efficacy, after-sales service rather than on social and psychological wants. The buying decisions usually take more time and engage many individuals from technical, commercial, and finance departments. After the initial offer made by a retailer, there are negotiations and exchange of information between the experts and representatives from both the purchaser and the seller organizations. Therefore, inter-organizational contacts take place and interpersonal relationships are developed. The relationships between the sellers and consumer are highly valued and they become stable in the long run because of a high level of interdependence. Webster and Wind asserted that factors that influence industrial buyer behavior can be structured in to two variables such as tasks and non-tasks. Tasks are directly associated with buying problems whereas non-tasks variable include the aspects beyond the particular buying issues.

The common model of Webster and Wind has been disapproved on the basis that it is not always possible to categorize a given set of variables as completely task and non-task. Rather any given set of variables will tend to have task and non-task dimensions (Agbonifoh, et al., 2007).

Another model which explained the industrial buying behaviour is The Robinson, Faris and Wind model. It is considered to be one of the earliest and most extensively used models to describe organizational buyer behavior differences (Agbonifoh, et al., 2007). The model puts forwards that the industrial buying process is a succession of stages which may vary depending on which buying situation (called classes) the particular buying firm is confronted with. The model analyses organizational buying behavior as depending on the amount of experience the buyer has with product class, the amount of information sought and the time spent on the decision. A cross-tabulation of the phases with the buy classes result in a buy-Grid-framework.

The Nelson box model mingles constituents of organizational buyer behavior with consumer behavior. The model is based on two important assumptions: a) that decisions at different levels of the organization neither always involve the same individuals or identical work. b)

That decision taken at one level forms the basis for all subsequent decision. The Nelson model depicts four levels of decision making in an organization. They are:

1. The general buying decision which comprises of the decision to begin a project. It may contain the establishment of a new building, or new product.

2. The actual buying decision which include selection of a definite project, including the objectives, and project specifications.

3. The decision which is associated with the most suitable suppliers/vendors and products.

4. The technical buying decision which engages decisions linked to the actual mechanics of transportation, drawing up of contracts, final price and payment negotiations and the stipulation of other feature.

Other influential model is The Hobbesian organizational buyer model formulated by Thomas Hobbes. The assumption of this model is that the purchasing officer's interest to do his best for the organization is obstructed by his interest to do the best for himself that at any given time the organizational buyer pursues both personal and group goals. The Hobbesian model evidently describes why an organizational buyer may utilize a vendor offering a higher price or slightly less quality instead of a seller offering a lower price for the same value.

Johnston and Lewin (1996) demonstrate that extensive researches conducted consolidated the existence and significance of three important dimensions when analysing industrial buyer behavior.

1. How the buyer decision process looks like when organizations stands in front of different buying situations.
2. The buying decision centre and factors influencing the buying process within the organization
3. The different criterion's used by industrial buyers when buying a product/service.

7.4.2 Industrial buyer process

Marketers gain Industrial marketing efficacy through deep understanding the nature of industrial buying as well as comprehending the industrial buying behavior. Industrial buying behavior is a complex procedure which cannot be explained by single descriptive variable such as price, total cost, reciprocity, or ego enhancement. Any rationally complete model of industrial buying behavior must be able to deal with the intricacy of industrial buying decisions which involve many people (users, deciders, influencers and buyers) are technical in nature, are made over long periods of time, and need multifaceted interaction of personal, interpersonal, organizational and environmental factors to determine buyer response to marketing effort. Numerous scholars explain the industrial buying behavior with different models that they have developed; which include the technical aspects and psychological aspects of many individuals (Webster & Wind 1972). Webster (1965) stated that in studying the industrial buying process, it is necessary to understand both industrial and individual feature of decision making.

Prof. Jagdish and N Sheth proposed the Sheth model in 1973. Sheth describes that all buying decisions do not result from organized process of decision making. Some unplanned situational factors also affect the buying decision, such as unpredicted situation like damage to machinery. It has been documented in literature that industrial buyer behavior is the process of procurement and significant phases are searching information and quantifying suppliers (Sheth, 1973). Another feature of industrial buyer behavior is the decision making group within organization. The Sheth interactive model focuses on information search and recognizes that the expectations of purchasing agents, engineers, users and others, who are directly involved in that act of buying and regarded as constituting the buying centre, can be influenced by their experience. To develop this model, Sheth segregated organizational buyer behavior into three different aspects:

1. The psychological world of the individual engrossed in organizational buying. This characteristic recognizes that purchase decision in an organization is not made by a single individual, but by members of different departments and that the psychological make-up of the decision makers is critical (Iruka, 2001).

2. The condition which precipitates joint decision making. Not all decisions are made together. The model gives six factors which establish whether a specific buying decision will be joint or autonomous. Three of these factors are related to the characteristics of the product or service and the other three are related to the characteristics of the buyer organization.

3. The Process of Joint Decision Making: The Sheth interactive model delineated the process of joint decision making to include the following steps: (a) Initiation of the decision to buy; (b) Gathering of information; (c) Evaluation of alternative suppliers, and (d) Resolution of conflict among the parties who must jointly decide.

Hill and Hiller model reproduced to analyze the purchase decision from the viewpoint of buyer and consists of three major constituents such as usage of purchased items, reason for purchase and purchase complexity. The intended use of proposed purchase is considered as vital information to the vendor because it will indicate the technical content involved, the value and essentiality of the item, and the degree of risk involved, the likely timing of purchase and whether the product is likely to be buyer or supplier specified. Hill and Hiller proposed five main categories of use.

1. For incorporation of production output which may be to order or to stock.
2. For utilization during production processes but not incorporated in the product.
3. To provide production facility in manufacture, service or resale.
4. For use in maintenance operation.
5. For use in development and engineering work.

Webster and Wind model believes that industrial buying behaviour is impacted by some variables. These variables are divided into four primary categories such as environmental, organizational, interpersonal and buying centre and individual. The factors affecting these variables include

- Buying situation
- Environmental factors
- Organizational factors
- Interpersonal factors
- Personal factors
- Additional influences

Organizational buying is very similar to individual buyer behavior with some contextual differences. Organizations buy in furtherance of organizational objectives, such as to manufacture and deliver goods and services to members, customers or the community.

Purchases are ingredients, components or supplies in the conversion process, for administrative or operational use or for rental or resale. Organizations serve a marketplace and are driven by the needs of their customers, whatever form they take.

Many large organizational purchases involve consultative selling, that is where the buyer and vendor work together to define the problem, identify a solution and work together throughout a long process of implementation and support. Because of the relationship issues which occur in a long association, trust, integrity, empathy and engagement become important factors to consider in the buying decision.

Organizational buying is heavily influenced by derived demand, that is, demand for an end product or for a product or service sold by the buyer's customers. The demand for components by a manufacturer will be dependent on demand coming from their customers, the retailers and wholesalers, who in turn are reacting to demand from their customers, the consumers. Overall consumer demand may in turn be impacted by economic, social, political and technological factors in the environment.

Organizational buying is often referred to as group buying where a number of individuals or groups undertake different roles in the buying process. Often the buying process will involve highly technical issues which will require the input of technical experts. At the same time, major purchases will involve economic considerations such as financing, return on investment, maintenance costs, life cycle consideration and so on.

A problem with working in a B2B environment for many vendors is the difficulty of establishing the members of the different groups and the level of their formal and informal involvement. A further problem lies in the manner in which the problem or solution specifications are arrived at. If developed too early and with little input from the vendor, they could be excluded if they solved the problem in a way different from that required through the specification. Another problem may exist where one vendor has a special relationship with some of the buying groups and is able to bias the specifications towards their solution.

Buying patterns in habitual purchases and frequent low risk purchases where little evaluation is required follow similar processes as for individuals. These tend to use routine procurement practices with little involvement from the vendors prior to the buy decision.

Complex, large or infrequent and perceived risky decisions are similar to personal buy decisions but as we can see, usually involve many more participants and are usually much more formal in process. Organizational decisions are also capable of being of very large scale and can involve purchases in the many millions of dollars, take many months if not years to transact and can make or break careers and fortunes. Perceived risk can be very high and encompass many actors.

These complex transactions are often in situations where the specification or the problem and/or the solution is problematic. In environments where problems are dynamic and interact with a developing and changing society and economy and where solutions evolve with knowledge and technology, the specifications themselves evolve. Often the buyer needs the active support of the vendor to understand the problem or to understand the state of possible solutions.

Solutions themselves may adapt to the problem definition as it is uncovered. Often it takes the active support of the vendor to uncover the requirements, especially where the vendor has much greater knowledge of the problem environment. Thus, it is not unusual for a deep relationship to develop between buyer and vendor as the project evolves. Trust, integrity, empathy and openness often become key characteristics of the final decision process.

A good portion of organizational buying is controlled or constrained by the economic situation. Components, ingredients and supplies must fit with the conversion process and with the economic objectives of the final outcome. Some decisions are constrained by mandated decision rules which limit the scope of the decision making power of the actors, especially prevalent in government procurement.

Organizational buying is not entirely predictable or entirely rational. Individuals who specify requirements or provide technical input, those who search for information and others who undertake evaluations will still be influenced by their own past experiences, knowledge and training. If a rigorous process of information search and evaluation is not undertaken or if there is time pressure to make a decision, then not all vendors will be considered or fully evaluated.

In a complex one-off buying situation, an organization proceeds through a series of steps to arrive at the buying process itself. Externally or internally some trigger kicks off the process. At this point, some part of the organization defines the issues and seeks permission to do something about it. Some individual or department is then given responsibility to investigate and recommend action. A budget needs to be assigned and the process of establishing the need and investigating possible solutions commenced. This process can be complex where multiple organizational units are involved and where organizational change is involved.

Organizations adopt certain methods for buying products such as checking a sample before the actual purchase. Most organizational purchases involve purchase of products in large lots. So it is not feasible to individually inspect each and every item in the lot. In such situations, a sample is checked assuming that this sample represents the entire lot. Like the consumer markets, organizational markets also possess certain demand characteristics. The organizational demand for products or services may be inelastic, derived, joint or fluctuating in nature. Organizational markets normally purchase the goods or services for producing other goods and services, using these as raw materials. There are also resellers, who purchase the products to sell directly to other customers without any modifications. Apart from producers and resellers, there are also government and institutional customers who buy the goods. Government buys goods for public utility or for use in their departments or for production purposes.

7.5 NOTES

7.6 SUMMARY

Knowledge of the process that organizational buyers follow in making purchasing decisions is fundamental to responsive marketing strategy. As a buying organization moves from the problem-recognition phase, in which a procurement need is defined, to later phases, in which suppliers are screened and ultimately chosen, the marketer can play an active role. In fact, the astute marketer often triggers initial awareness of the problem and helps the organization effectively solve that problem. Incremental decisions made throughout the buying process narrow the field of acceptable suppliers and dramatically influence the ultimate outcome.

The nature of the buying process depends on the organization's level of experience with similar procurement problems. Unraveling the complex forces that encircle the organizational buying process is indeed difficult. The marketer who is sensitive to individual differences is best equipped to develop responsive marketing communications that the organizational buyer will remember.

7.7 KEY WORDS

- Problem recognition
- Product specification
- Supplier search
- Supplier selection
- Risks
- Buyer behavior
- Proposal solicitation
- Supplier performance review
- Industrial buyer process

7.8 SELFASSESSMENT QUESTONS

1. Briefly explain the process of industrial buying.
2. What do you mean by buyer behavior?
3. Explain the concept of buyer behavior.
4. What are the risks involved in buying a product.
5. Discuss the industrial buyer process with a neat diagram.

7.9 REFERENCES

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UNIT - 8 : VALUE ANALYSIS

Structure:

8.0 OBJECTIVES

After studying this unit, you should be able to;

- Outline the formula of value.
- Explain the value analysis.
- Assess the vendor analysis.
- Highlight organization buying activities.
- Discuss purchasing orientations.

8.1 INTRODUCTION

The value of a product will be interpreted in different ways by different customers. Its common characteristic is a high level of performance, capability, emotional appeal, style, etc. relative to its cost. This can also be expressed as maximizing the function of a product relative to its cost:

Value = (Performance + Capability)/Cost = Function/Cost

Value is not a matter of minimizing cost. In some cases the value of a product can be increased by increasing its function (performance or capability) and cost as long as the added function increases more than its added cost. The concept of functional worth can be important. Functional worth is the lowest cost to provide a given function. However, there are less tangible "selling" functions involved in a product to make it of value to a customer.

Lawrence Miles conceived of Value Analysis (VA) in the 1945 based on the application of function analysis to the component parts of a product. Component cost reduction was an effective and popular way to improve "value" when direct labour and material cost determined the success of a product. The value analysis technique supported cost reduction activities by relating the cost of components to their function contributions.

Value analysis defines a "basic function" as anything that makes the product work or sell. A function that is defined as "basic" cannot change. Secondary functions, also called "supporting functions", described the manner in which the basic function(s) were implemented. Secondary functions could be modified or eliminated to reduce product cost.

As VA progressed to larger and more complex products and systems, emphasis shifted to "upstream" product development activities where VA can be more effectively applied to a product before it reaches the production phase. However, as products have become more complex and sophisticated, the technique needed to be adapted to the "systems" approach that is involved in many products today. As a result, value analysis evolved into the "Function Analysis System Technique" (FAST) which is discussed later.

8.1.1 Value Analysis: Meaning, Phases, Merits and Limitations

Value Analysis is one of the major techniques of cost reduction and control. It is a disciplined approach which ensures the necessary functions for the minimum cost without diminishing quality, reliability, performance and appearance.

It is a creative approach to eliminate the unnecessary costs which add neither to quality nor to the appearance of the product. It is a systematic application of techniques to identify the functions of a product or a component and to provide the desired function at the lowest total cost.

These are the days of providing the customer with really best quality products at least cost which is possible through value analysis which proves wrong rightly "Best and Cheap" or "Best is never cheap" or "Cheap is Costly".

Before understanding the meaning of phrase "value analysis" or "value engineering", let us know about value. 'Value' is one of those terms having good many connotations and even contradictory definitions.

'Value' is a word that is very often used by individuals without being clearly understood. Forget about common people. Even different departments of the same organisation have different opinions of the 'value' of the product that the company manufactures.

The designer equates value with reliability; purchase people with price paid for them; production personnel with that of cost from the angle of manufacture; sales people with what customer is willing to pay.

In the field of value investigation, value refers to economic value, which itself can be sub-divided into four types as cost value, exchange value, use value and esteem value.

"Cost Value" is the measure of sum of all costs incurred in producing the product. The 'cost value', therefore is the sum of raw-material cost, labour cost, tool cost and overheads expended to produce the product.

"Exchange Value" is the measure of all the properties, qualities and features of the product which make the product possible of being traded for another product or for money. In a conventional sense, 'exchange value' refers to the price that a purchaser will offer for the product, the price being dependent upon the satisfaction value which derives from the product.

Value derived from the product consists of two components namely (a) value due to reliability of performance of the product and the value which the possession bestows upon the buyer. These are often referred to as "value in value" and "esteem in value".

"Use Value" is the measure of properties, qualities and features which make the product accomplish a use, work or service. Use value, therefore, is the price paid by the buyer or the cost incurred by the manufacturer in order to ensure that the product performs its intended function efficiently.

Use value in the fundamental form of economic value. An item without use value can have neither exchange value nor esteem value. "Esteem Value" is the measure of properties, features, attractiveness graphic packaging and the like which increases sales appeal or which attracts customers and create in them a strong desire to own the product.

"Esteem value", therefore, is the price paid by the buyer or the cost incurred by the manufacturer beyond the use value. It is the perception value.

8.1.2 Definition

Value analysis is an organised approach to identify unnecessary costs associated with any product, material, part, component, system or service by analysis of function and efficiently eliminating them without impairing the quality functional reliability or its capacity to give service.

According to Society of American Value Engineers (SAVE) "Value analysis is the systematic application of recognised techniques which identify the function of a product or services establish a monetary value for the function and provide the necessary function reliability at that lowest overall cost."

Mr. Lorry D. Miles production engineer working at General Electricals of USA defined it as "Value analysis is the study of the relationship of design, function and cost of any material or service with an object of reducing its cost through modification of design or material specifications, manufacture by more efficient process, changes in sources of supply, elimination or incorporation into another item."

Thus, value analysis is a systematic application of established techniques to identify the functions of a product or component and to provide the desired functions at the lowest total cost. It is a creative approach to eliminate unnecessary costs which add neither to quality no to the appearance of the product.

8.1.3 It is a rational and structured process consisting of:

(a) Functional analysis to define the reason for the existence of a product or its components,

(b) Creatively analysis for generating new and better alternatives and

(c) Measurement for evaluating the value of present and future concepts.

The phrase value analysis can be defined as a technique which examines the facts of a function and cost of a product in order to determine whether the cost can be reduced or altogether eliminated, while retaining all the features of performance and quality of a product or both.

Therefore, logically, VA is an organised approach of exposing and eliminating unnecessary costs. The method has logical foundation in its fundamental approach to cost reduction and profit improvement and in this objective approach, the VA techniques has to analyse the functional cost of an item and recommend a change.

Put alternatively, VA is a team approach to think functionally about a component as to "what it does" rather than "what it is". This approach is the real test of understanding problems under study.

8.1.4 Value Analysis and Value Engineering:

'VA' and 'VE' are closely related terms so much so that many people use them interchangeably. Though the philosophy understanding the two is the same the identification of unnecessary costs yet they are different. The difference lies in the time and stage at which the technique is applied.

"Value Analysis" is the application of a set of techniques to an existing product with a view to improve its value. Thus, it is remedial process. "Value Engineering" is the application of exactly the same set of techniques to a new product at the design stage project concept or preliminary design when no hardware exists to ensure that bad features not added. Thus, it is a 'preventive' measure. In that sense, 'VE' is fundamental and VA is collateral because 'prevention is better than cure."

8.1.5 Value Analysis versus Other Conventional Approaches:

Speaking in terms of "cost reduction" value analysis is an effective tool of cost reduction which differs from established conventional approaches such as industrial engineering, production engineering, methods engineering and the like.

The "traditional" or "conventional" approaches differ from this non- conventional or modern technique of VA as under:

1. Traditional approaches concern "post-production" stage but V.A. can be the 'pre-production' as well as "post production stage" technique.

2. Traditional approaches are “methods concerned”. They accept the drawing of the part “as is” and, therefore, set to improve the part through analysis of manufacturing methods, machines, materials, tools, jigs and fixtures and the like.

   On the other hand, ‘VA’ does not accept the designed product and its components “as is” but advocates cost reduction through identification of the function and subsequent redesign of the product so as to make it perform its functions at the lowest possible cost.

   ‘VA’, therefore, challenges the very design specifications, design requirements and the design itself.

3. Traditional methods are mere “cost centered” while VA, in addition to cost improvement, usually seeks to improve quality, reliability, maintainability, safety, performance and alluring features.

4. VA is more potent than traditional cost reduction techniques. Instances can be brought to surface to demonstrate that VA can remove ten to twenty percent of cost after the traditional methods of cost reduction have applied.

Award of warning is essential at this stage, lnspite of VA’s better potential and greater effectiveness, it is not a substitute nor is it intended to replace effective cost reduction techniques which have been in use for many years and have proved effective and valuable in their areas of application. What can be said is that VA can augment or strengthen the process of cost reduction and quality improvement.

8.1.6 Phases of Value Analysis:

1. Phase of Origination:

In the first phase, a value analysis study team is constituted. The project is selected and clearly defined. The team examines in detail the product and its components to understand thoroughly their nature.

2. Phase of Information:

After familiarisation, a functional analysis is carried out to determine the functions and uses of the product and its components. The cost and importance of each function are identified. A value index is calculated on the basis of cost benefit ratio for each function. A list is being prepared in which the items of functions are arranged in decreasing order of value.

3. Phase of Innovation:

This is the creative phase concerned with the generation of new alternatives to replace or removing the existing ones.

4. Phase of Evaluation:

Each and every alternative is analysed and the most promising alternatives are selected. These alternatives are further examined for economic and technical feasibility.

The alternatives finally selected must be capable of performances the desired functions satisfactorily. These must meet the standards of accuracy, reliability, safety, maintenance and repairs, environmental effects and so on.

5. Phase of Choice:

In this phase, report is prepared. This report contains a summary of the study, conclusions and specific proposals. The decision makers choose the alternative. The programs and action places are then developed to implement the chosen alternative.

6. Phase of Implementation:

The chosen alternative is put to the actual use with the help of the programs and action plans so developed in advance.

7. Phase of Review:

The progress of analysis changes in continuously monitored and followed up in order to provide assistance, to clarify any misconceptions and to ensure that the desired results are achieved.

8.1.7 Merits of Value Analysis:

Value analysis is really a very valuable technique of cost reduction and quality improvement. The specific merits of it are:

1. Improvement in Product Design:

It leads to improvements in the product design so that more useful products are given shape. Now in case of ball points, we do not have clogging, there is easy and even flow of ink and rubber pad is surrounding that reduces figures fatigue.

2. High Quality is maintained:

High quality implies higher value. Thus, dry cells were leaking; now they are leak proof; they are pen size with same power. Latest is that they are rechargeable.

3. **Elimination of Wastage:**

Value analysis improves the overall efficiency by eliminating the wastages of various types. It was a problem to correct the mistakes. It was done by pasting a paper. Now, pens are there and liquid paper is developed which dries fast and can write back.

4. Savings in Costs:

The main aim of value analysis is to cut the unwanted costs by retaining all the features of performance or even bettering the performance. Good deal of research and development has taken place. Now milk, oils, purees pulp can be packed in tetra packing presuming the qualities and the tetra pack is degradable unlike plastic packs.

5. Generation of New Ideas and Products:

In case of took brushes, those in 1930's were flat and hard, over 60 to 70 years brushes have come making brushing teeth easy, cosy and dosy as it glides and massages gums.

6. Encourages Team-Spirit and Morale:

Value analysis is a tool which is not handled by one, but groups or teams and an organisation itself is a team of personnel having specification. A product is the product of all team efforts. Therefore, it fosters team spirit and manures employee morale as they are pulling together for greater success.

7. Neglected Areas are brought under Focus:

The organisational areas which need attention and improvement are brought under the spot-light and even the weakest gets a chance of getting stronger and more useful finally join's the main strain.

8. Qualification of Intangibles:

The whole process of value analysis is an exercise of converting the intangibles to tangible for decision making purpose. It is really difficult to make decisions on the issues where the things are (variables) not quantifiable.

However, value analysis does it. The decision makers are provided with qualified data and on the basis of decisions are made. Such decisions are bound to be sound.

9. Wide Spectrum of Application:

The principles and techniques of value analysis can be applied to all areas-man be purchasing, hardware, products, systems, procedures and so on.*10. Building and Improving Company Image:*

The company's status or image or personality is built up or improved to a great extent. Improvement in quality and reduction in cost means competitive product and good name in product market; it is a good pay master as sales and profits higher and labour market it enjoys reputation; it capital market, nobody hesitates to invest as it is a quality company.

8.1.8 Limitations:

Like any other cost reduction technique, value analysis has its own limitations. The most common limitations are that the man-made excuses are the blocks in implementing these plans of value analysis.

The most common excuses given are:

(a) Lack of motivation

(b) Resistive to change

(c) Inertia

(d) Lack of knowledge and patience

(e) Attitude of 'It will not work in India

(f) We are very small or very big

(g) This has been tried earlier and failed

(h) The change is too big

(i) 'Let competitors try before we try'

(j) Difficulty of teams meeting or team meeting for getting consensus.

These limitations are man-made and can be over-come one the company divides to implement. However, they should be educated of the plus and minus points and the main beneficiaries are those that are to be told and they are to be taken into confidence.

8.1.9 The value analysis method

In all problem solving techniques, we are trying to change a condition by means of a solution that is unique and relevant. If we describe in detail what we are trying to accomplish, we tend to describe a solution and miss the opportunity to engage in divergent thinking about other alternatives. When trying to describe problems that affect us, we become locked in to a course of action without realizing it, because of our own bias. Conversely, the more abstractly we can define the function of what we are trying to accomplish, the more opportunities we will have for divergent thinking.

This high level of abstraction can be achieved by describing what is to be accomplished with a verb and a noun. In this discipline, the verb answers the question, “What is to be done?” or, “What is it to do?” The verb defines the required action. The noun answers the question, “What is it being done to?” The noun tells what is acted upon. Identifying the function by a verb-noun is not as simple a matter as it appears.

Identifying the function in the broadest possible terms provides the greatest potential for divergent thinking because it gives the greatest freedom for creatively developing alternatives. A function should be identified as to what is to be accomplished by a solution and not how it is to be accomplished. How the function is identified determines the scope, or range of solutions that can be considered.

That functions designated as “basic” represent the operative function of the item or product and must be maintained and protected. Determining the basic function of single components can be relatively simple. By definition then, functions designated as “basic” will not change, but the way those functions are implemented is open to innovative speculation.

As important as the basic function is to the success of any product, the cost to perform that function is inversely proportional to its importance. This is not an absolute rule, but rather an observation of the consumer products market. Few people purchase consumer products based on performance or the lowest cost of basic functions alone. When purchasing a product it is assumed that the basic function is operative. The customer’s attention is then directed to those visible secondary support functions, or product features, which determine the worth of the product. From a product design point of view, products that are perceived to have high value first address the basic function’s performance and stress the achievement of all of the performance attributes. Once the basic functions are satisfied, the designer’s then address the secondary functions necessary to attract customers. Secondary functions are incorporated in the product as features to support and enhance the basic function and help sell the product. The elimination of secondary functions that are not very important to the customer will reduce product cost and increase value without detracting from the worth of the product.

The cost contribution of the basic function does not, by itself, establish the value of the product. Few products are sold on the basis of their basic function alone. If this were so, the market for “no name” brands would be more popular than it is today. Although the cost contribution of the basic function is relatively small, its loss will cause the loss of the market value of the product.

One objective of value analysis or function analysis, to improve value by reducing the cost-function relationship of a product, is achieved by eliminating or combining as many secondary functions as possible.

8.1.10 Value improvement process

Performing value analysis or producing the FAST model and analysing functions with the value analysis matrix are only the first steps in the process. The real work begins with brainstorming, developing and analysing potential improvements in the product. These subsequent steps are supported by:

- The QFD Concept Selection Matrix is a powerful tool to evaluate various concept and design alternatives based on a set of weighted criteria that ultimately tie back to customer needs.
- Benchmarking competitors and other similar products helps to see new ways functions can be performed and breaks down some of the not-invented-here paradigms.
- Product cost and life cycle cost models support the estimating of cost for the Function-Cost and Value Analysis Matrices and aid in the evaluation of various product concepts.
- Technology evaluation is leads us to new ways that basic functions can be performed in a better or less costly way. Concept development should involve people with knowledge of new technology development and an open mind to identify how this technology might relate to product functions that need to be performed. Methods such as the theory of inventive problem solving or TRIZ are useful in this regard.
- Design for Manufacturability/Assembly principles provide guidance on how to better design components and assemblies that are more manufacturable and, as a result, are lower in cost.

Value Analysis or Function Analysis provide the methods to identify the problem and to begin to define the functions that need to be performed. As we proceed in developing a FAST model, implicit in this process is developing a concept of operation for the product which is represented by all of the lower order functions in a FAST diagram.

Concept alternatives will be developed through brainstorming, benchmarking other products performing similar functions, and surveying and applying new technology. Since multiple concepts need to be evaluated, we want to use a higher level of abstraction for the FAST model to provide us with the greatest flexibility and a minimum level of effort. Trade studies and technical analysis will be performed to evaluate various product concepts. A concept selection matrix is a good tool to summarize a variety of different data and support making a decision about the preferred concept.

All of these steps may be iterative as a preferred concept evolves and gets more fully developed. In addition, there should be a thorough evaluation of whether all functions are needed or if there is a different way of accomplishing a function as the concept is developed to a lower level of abstraction. When a Function Cost or Value Analysis Matrix is prepared, functions that are out of balance with their worth are identified, further challenging the team to explore different approaches.

8.2 VENDORANALYSIS

Vendors play a major role in a firm's performance. Firms use vendor analysis to select the right vendors for their organization. In this lesson, learn what vendor analysis is and how it is used.

A vendor is a firm or an individual that has a product or service for sale. Firms depend on a vendor's ability to meet their needs in order to efficiently perform the functions of their business. Therefore, it is important for a firm to choose vendors who are able to meet their requirements. Firms use a process known as vendor analysis to assess the ability of existing or prospective vendors.

Vendor analysis identifies the strengths and weaknesses of each vendor, then compares them to find the vendor that best matches the needs of their company. A vendor analysis is conducted whenever a firm needs to find a new vendor or review the performance of its existing vendors.

8.2.1 Definition

Vendor analysis is theassessment of strengths and weaknesses of current and prospective suppliers in terms of their capacity, sales revenue, reputation, stocks, markdowns, markups, gross margins, quality, reliability, service, pricing policies, payment terms etc.

Vendor Analysis can be defined as the assessment of weaknesses and strengths of prospective and current suppliers with respect to their – availability of capable staff, business model, capacity, sales revenue, stocks, reputation, mark-ups, mark-downs, gross margins, quality, service, reliability, pricing policies, payment terms, etc.

This process is undertaken generally when a company is choosing a new vendor, consolidating the existing suppliers, or assessing the capabilities of the existing suppliers. It can also be done when a company decides to reach out to third party for some problem existing in their business. Let us consider an example – Raymonds was seeking an IT solution provider to perform all the IT related jobs for them. Accenture is now doing that for them.

Raymonds would have analyzed all the quotations they received and the vendors from they received on the earlier mentioned parameters. After performing the vendor analysis only they would have finalized Accenture.

There are companies which deal with a number of vendors. They perform vendor analysis from time to time basis in order to understand which vendor is most beneficial to in them with respect to the cost of doing business with them and their contribution in company's profit. Businesses are always looking to cut costs, increase profits and efficiency of operations. In such a scenario vendor analysis is very important for all the stated goals.

8.2.2 Process of vendor analysis.

1. Assess your Needs and Identify Priorities and Deal-breakers

In order to understand which vendor is the right one for you, it is necessary to understand your firm's immediate needs for a vendor. For instance, a firm may open a new store in a different region and may look for a vendor that offers products indigenous to that area. Many companies review things such as a vendor's reputation, financial strength, sales, capacity, prices, services, payment terms, qualities, or reliability.

It is important for a firm to identify what is important to them and what their deal-breakers are. Finding vendor that are reliable, have competitive pricing, and quality products may be important vendor characteristics for a firm. A bad reputation or not offering certain services may be deal-breakers.

2. Set Goals and Guidelines

Firms conducting a vendor analysis, should set SMART goals (specific, measurable, attainable, relevant, and timely) for what they want to accomplish. Setting a goal of decreasing inventory carrying cost by 20% over the next four months is an example of a SMART goal.

The next step in this process is to set up guidelines that are easily understood. For instance, a vendor's quality may be rated on a scale of 1 to 5, with 5 being the worse. The number 1 may signify exemplary quality, 2 may signify the product is a quality product but made out of cheaper materials, and so on, with each number signifying a worse quality then the number before.

3. Create a List and Narrow the Selection

Create a comprehensive list of all existing and potential vendors. You may be wondering why existing vendors would need to be added to this list. Existing vendors may be able to fulfill your requirements; however, they may not be your best option. So, it is always good to evaluate and compare vendors new and old.

Now that you have a large list of vendors to choose from it is time to eliminate most of them. Researching a vendor is a great way to narrow your selection. You can talk to the vendor's customer regarding their experiences, visit the website, and visit the premises. You may also submit a questionnaire for to fill out and return.

8.3 PURCHASING ORIENTATION

In the past, purchasing department occupied a low position in the management hierarchy, in spite of often managing more than half the company costs. Recent competitive pressures have led many companies to upgrade their purchasing department and elevate administrators to vice presidential rank.

Today purchasing departments are staffed with MBAs who aspire to be CEOs-like Thomas Stall Kamp, Chrysler former executive vice president of procurement and supply, who cut costs and streamlined the automaker manufacturing processes.

These new, more strategically oriented purchasing departments have a mission to seek the best value from fewer and better suppliers. Some multinationals have been elevated them to strategic supply departments with responsibility for global sourcing and partnering. At Caterpillar, for example, purchasing, inventory control, production scheduling and traffic have been combined into one department. Lockheed Martin is another firm that has improved its business buying practices.

8.3.1 Buying Orientation:

The purchaser focus is short term and tactical. Buyers are rewarded in their ability to obtain the lowest price from suppliers for the given level of quality and availability. Buyers use two tactics namely commoditization, where they imply that the product is a commodity and care only about price; and multi-sourcing where they use several sources and make them compete for share of the company purchases.

8.3.2 Procurement Orientation:

Here buyers simultaneously seek quality improvements and cost reduction. Buyers develop collaborative relationships with major suppliers and seek savings through better management of acquisition, conversion, and disposal costs. They encourage early supplier involvement in materials handling, inventory levels, just-in-time management, and even product design. They negotiate long-term contracts with major suppliers to ensure the timely flow of material. They work closely with their manufacturing group on materials requirement planning (MRP) to make supplies arrive on time.

8.3.3 Supply Chain Management Orientation:

Here purchasing role is further broadened to become a more strategic, value-adding operation. Purchasing executives at the firm work with marketing and other company executives to build a seamless supply chain management system from the purchase of raw materials to the-time arrival of finished goods to the end users.

8.3.4 Types of Purchasing Processes:

Marketers need to understand how business purchasing departments work. These departments purchase many types of products, and the purchasing process will vary depending on the types of products involved. Four products related purchasing processes are distinguished below:

1. Routine product: These products have low value and cost to the customer and involve little risk (e.g. office supplies). Customers will seek the lowest price and emphasize routine ordering. Suppliers will offer to standardize and consolidate orders.

2. Leverage products: These products have high value and cost to the customer but involve little risk of supply (e.g. engine pistons) because many companies make them. The supplier knows that the customer will compare market offerings and costs, and it needs to show that its offering minimizes the customer total cost.

3. Strategic products: These products have high value and cost to the customer and also involve high risk (e.g. mainframe computers). The customer will want a well-known and trusted supplier and be willing to pay more than the average price. The supplier should seek strategic alliances that take the form of early supplier involvement, co-development programs, and co-investment.

4. Bottleneck products: These products have low value and cost to the customer but they involve some risk (e.g. spare parts). The customer will want a supplier who can guarantee a steady supply of reliable products. The supplier should propose standard parts and offer a tracking system, delivery on demand, and a help desk.

The conclusion is that the upgrading of purchasing means business marketers must upgrade their sales personnel to match the higher caliber of the business buyers. Formally, we can distinguish three company purchasing orientations.

8.4 PRACTICES OF BUSINESS ACTIVITIES

8.4.1 Introduction

Industrial markets exist to offer goods and services to the consumer market. Virtually all products bought and consumed by final consumers emanate directly or indirectly from the industrial market. In classification of market, one of the classifications is purpose base classification, which consists of consumer market, institutional market and industrial market. Industrial market exists to make goods and services available to producers, intermediaries and government. Institutional or government market exists to render services to other markets and collect taxes in return, while consumer market receives the goods and services from industrial market and service from government in exchange with money and taxes respectively.

According to Haas cited in Nwokoye, N. G. (2004) industrial marketing refers to "marketing activities that are intended to acquire and sell goods or services to business or other organizations to be used directly or indirectly in their own operations. These businesses or organizations may be public or private, and domestic or multinational".

Industrial marketing comprises all activities directed at providing, businesses or organizations with inputs required for production or business operation. The aim of consumer market is to buy for final consumption while industrial market seeks to buy to aid business operations and production.

In some ways industrial and consumer markets share similarities. These are found in areas such as people, exchange means and want satisfying product. Both industrial and consumer markets involve people who assume buying roles and make purchase decision to satisfy identified needs. The two markets also engage in exchange process and in centre of the exchange process is the product.

8.4.2 Some of the practices of business customer's are:

1. They deal with very few numbers of suppliers when compared with consumer market.
2. Business or industrial markets are more geographic concentrated than consumer markets. Availability of natural resources, raw materials, labours, managerial and technical expertise and capital may warrant geographical concentration. Industrial buyers are geographically concentrated.
3. Many industrial products have inelastic demand. This implies that demand for many industrial products is not affected by changes in price mostly in the short run. Demand for some industrial products is price insensitive.
4. Business or industrial product faces derived demand. The demand for industrial products is by demand for another industrial or consumer product. For instance, the rate of demand for steel by an automobile company is necessitated by demand for cars.
5. Industrial products have joint demand: the demand for industrial products goes with the demand for additional one or more products. Without these additional products the industrial product will not be useful or effective. For instance, the demand for vehicle requires demand for diesel, engine oil, gear oil. etc.
6. Industrial purchase requires well-trained experts or professional and knowledgeable buyers.
7. Business market involves formalized buying process. Business normally asks for detailed product specification, purchase order, bidding or bargain, supplier sourcing

and formal approval. This is unlike consumer buying which does not undergo this process.

8. Direct Distribution: Most industrial products are distributed directly to the buyer/user especially where the order size is large and special delivery arrangement is made.

9. Complex Decision: Purchase of industrial products involves huge amount of money, complex and technical considerations, economic consideration, etc, thus, making buying decision complex.

10. Buyer-seller reciprocity: This is a situation where industrial marketer and his customer agree to purchase each other's product based on agreed terms.

11. Dependency of Marketer and customer: Industrial marketing brings long-term business relationship between the seller and the buyer.

12. More Decision Participants: More people tend to involve in making buy-decision than in consumer marketing. Those involves in buying decision are well trained, professional and knowledgeable individuals who pool ideas together so as to get the right product, at the right price, from the right source, at the right time and quantity.

13. Industrial products are easily identifiable.

14. It involves more technically complex products.

15. Requires after sales services.

16. There is a greater tendency for rationality in industrial purchasing.

8.4.3 Industrial Buying On the Internet

Advancement in information and communication technology has brought tremendous change to business-to-business (industrial) marketing process. Before the advent of modern world (information and communication technologies), all businesses were transacted on face-to-face interactions. But today, technology has made it possible for transaction to take place without the buyer knowing the face of the seller. One of such technologies is the internet. Thus, on-line purchasing also called, e-procurement has advanced rapidly. There are associated advantages of on-line procurement.

- It has given buyers more access to new supplies and suppliers.
- It has reduced administrative, operation and purchasing costs.
- It facilitates order processing and delivery.
- It creates greater opportunity for information accessibility.
- It builds sound customer relationship.

- It reduces paper work associated with traditional ordering and re-ordering procedures and also reduces order lead-time.

However, e-purchasing or e-procurement poses a security threat to organizations.

8.5 ORGANIZATIONAL BUYINGACTIVITIES

Organizational buying activities center on the level of experience and information that firms have in purchasing certain products and services. In making a routine purchase, buyers have little need for information because of their past experience with the purchasing situation. When a purchasing situation is entirely new, information needs may be extensive due to the firm's lack of experience with the product, service, or suppliers. In the purchase of a new computer system, for example, buyers will be very concerned with identifying computer characteristics (e.g., programs and peripheral equipment) that will satisfy their needs, services provided to maintain the system, and the supplier's capability to provide those services.

Buying activity also consists of various phases of decision making. Depending on the type of buying situation, whether it is routine or new, these phases will vary in their degree of importance. Effective industrial marketing strategy, then, requires that marketers focus their attention on the type of buying situation a firm is facing, where it is in its decision-making process (which phase), and what criteria various influencers will emphasize in the purchasing decision.

8.6 NOTES

8.7 SUMMARY

Value analysis and its more robust cousin, Function Analysis System Technique, are important analysis tools. These methodologies lead to improved product designs and lower costs by:

- ♦ Providing a method of communication within a product development team and achieving team consensus
- ♦ Facilitating flexibility in thinking and exploring multiple concepts
- ♦ Focusing on essential functions to fulfill product requirements
- ♦ Organizational buying involves more buyers-more decision makers or contributors to portions of the decisions.
- ♦ Committees (the buying center) are involved, with professionals in each discipline (stakeholders) making decisions that are driven by their particular needs.
- ♦ Different types of decisions are often occurring simultaneously in the process, spread throughout the buying organization.

8.8 KEY WORDS

♦ Value analysis	♦ Vendor analysis	♦ Purchasing orientations
♦ Organization buying activities	♦ Industrial buying on net	♦ leverage product
♦ Bottleneck products	♦ Routine products	♦ Strategic products

8.9 SELFASSESSMENT QUESTIONS

1. Define value analysis.
2. Define Vendor analysis.
3. Explain the purchasing orientations of business customers.
4. Discuss the purchasing practices of business customers.
5. Outline the organization buying activities

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MODULE - III
STRATEGY FORMULATION IN INDUSTRIAL MARKET

UNIT - 9: STRATEGIC PLANNING

Structure:

9.0 OBJECTIVES

After studying this unit, you will be able to;

- Analyze strategic planning significance in the organization
- Evaluate the development of strategic plan
- Describe the strategic planning with examples
- Suggest how companies are useful by forming strategic planning

9.1 INTRODUCTION

Strategic planning is an organization's process of defining its strategy, or direction, and making decisions on allocating its resources to pursue this strategy. It may also extend to control mechanisms for guiding the implementation of the strategy.

Strategic planning involves clearly defining the organization's mission and an assessment of its current state and competitive landscape. Strategic planning also requires a well-thought out plan for how to properly allocate time, human capital and financial resources. By following a strategic planning process, organizations can improve business outcomes and avoid taking on unanticipated risk due to lack of foresight.

Depending on the scope of an organization's plans, a strategic planning process can look forward one, five or 10 years, or even more in some cases. Findings are often gathered in a formal strategic planning document.

Strategic planning is an organization's process of defining its strategy, or direction, and making decisions on allocating its resources to pursue this strategy. It may also extend to control mechanisms for guiding the implementation of the strategy. Strategic planning became prominent in corporations during the 1960s and remains an important aspect of strategic management. It is executed by strategic planners or strategists, who involve many parties and research sources in their analysis of the organization and its relationship to the environment in which it competes.

Strategy has many definitions, but generally involves setting goals, determining actions to achieve the goals, and mobilizing resources to execute the actions. A strategy describes how the ends (goals) will be achieved by the means (resources). The senior leadership of an organization is generally tasked with determining strategy. Strategy can be planned (intended) or can be observed as a pattern of activity (emergent) as the organization adapts to its environment or competes.

Strategy includes processes of formulation and implementation; strategic planning helps coordinate both. However, strategic planning is analytical in nature (i.e., it involves "finding the dots"); strategy formation itself involves synthesis (i.e., "connecting the dots") via strategic thinking. As such, strategic planning occurs around the strategy formation

Overview

Strategic planning is a process and thus has inputs, activities, outputs and outcomes. This process, like all processes, has constraints. It may be formal or informal and is typically iterative, with feedback loops throughout the process. Some elements of the process may be continuous and others may be executed as discrete projects with a definitive start and end during a period. Strategic planning provides inputs for strategic thinking, which guides the actual strategy formation. The end result is the organization's strategy, including a diagnosis of the environment and competitive situation, a guiding policy on what the organization intends to accomplish, and key initiatives or action plans for achieving the guiding policy.

Michael Porter wrote in 1980 that formulation of competitive strategy includes consideration of four key elements:

- Company strengths and weaknesses;
- Personal values of the key implementers (i.e., management and the board);
- Industry opportunities and threats; and
- Broader societal expectations.

The first two elements relate to factors internal to the company (i.e., the internal environment), while the latter two relate to factors external to the company (i.e., the external environment). These elements are considered throughout the strategic planning process.

Inputs

Data is gathered from a variety of sources, such as interviews with key executives, review of publicly available documents on the competition or market, primary research (e.g., visiting or observing competitor places of business or comparing prices), industry studies, etc. This may be part of a competitive intelligence program. Inputs are gathered to help support an understanding of the competitive environment and its opportunities and risks. Other inputs include an understanding of the values of key stakeholders, such as the board, shareholders, and senior management. These values may be captured in an organization's vision and mission statements.

Activities

The essence of formulating competitive strategy is relating a company to its environment.

Michael Porter

Strategic planning activities include meetings and other communication among the organization's leaders and personnel to develop a common understanding regarding the competitive environment and what the organization's response to that environment (its strategy) should be. A variety of strategic planning tools (described in the section below) may be completed as part of strategic planning activities.

The organization's leaders may have a series of questions they want answered in formulating the strategy and gathering inputs, such as:

What is the organization's business or interest?

What is considered "value" to the customer or constituency?

Which products and services should be included or excluded from the portfolio of offerings?

What is the geographic scope of the organization?

What differentiates the organization from its competitors in the eyes of customers and other stakeholders?

Which skills and resources should be developed within the organization?

Outputs

The output of strategic planning includes documentation and communication describing the organization's strategy and how it should be implemented, sometimes referred to as the strategic plan. The strategy may include a diagnosis of the competitive situation, a guiding policy for achieving the organization's goals, and specific action plans to be implemented. A strategic plan may cover multiple years and be updated periodically.

The organization may use a variety of methods of measuring and monitoring progress towards the objectives and measures established, such as a balanced scorecard or strategy map. Companies may also plan their financial statements (i.e., balance sheets, income statements, and cash flows) for several years when developing their strategic plan, as part of the goal setting activity. The term operational budget is often used to describe the expected financial performance of an organization for the upcoming year. Capital budgets very often form the backbone of a strategic plan, especially as it increasingly relates to Information and Communications Technology (ICT).

Outcomes

Whilst the planning process produces outputs, as described above, strategy implementation or execution of the strategic plan produces Outcomes. These outcomes will invariably differ from the strategic goals. How close they are to the strategic goals and vision will determine the success or failure of the strategic plan. There will also arise unintended outcomes, which need to be attended to and understood for strategy development and execution to be a true learning process. One of the immediate goals to be achieved by the action plan includes ensuring that the organization conforms to the legal requirements. A business organization that operates within the legal requirements operates with minimum problems; this directly increases the company's share-market. Climbing the corporate ladder sees to it that the organization increases both its income and expenses. The other short-term objective to be met by the strategic action plan entails increased customer loyalty. Customers are usually attracted to business organizations that offered good services and respected the client needs. Each departmental head will be responsible for their teams. They will monitor the activities and operations of the conducted for each strategic action. Different organizational teams will take responsibility for the various marketing strategies in the organization. The successful strategists will be rewarded, an incentive for them to work harder to attain the organization's long-term goals

9.2 DEFINITION OF THE STRATEGIC PLANNING PROCESS

Strategic planning is a process undertaken by an organization to develop a plan for achievement of its overall long-term organizational goals.

Model

There is no one model of strategic planning. However, the strategic planning process should include a situational analysis. This consists of looking at the current external and internal environment the organization finds itself in, formulating organizational objectives and strategies based upon the environmental assessment, and developing procedures to implement and evaluate the strategic plan. Strategic plans for business organizations often cover a three-to-five year period, but if the business or its environment is highly dynamic, a shorter period may be advisable.

Strategic Planning Steps

Here are the main steps for strategic planning.

9.2.1. Analysis of the current state

Here, you analyze your organization's external and internal environment. You may conduct a SWOT analysis, which is an examination of your organization's strengths, weaknesses, opportunities, and threats. You will also carefully examine the specific external environmental factors, such as your rivals, the power of your suppliers, the power your buyers or customers have, whether there is a viable threat that major clients or customers can effectively substitute your product or service, and whether there are any barriers to entry into a new market.

9.2.2 Defining the future state

Here, you will develop an organizational vision and a mission statement that describes the future of your organization - where it wants to be, its essential values, and what it wants do. After you have defined the organization's vision and mission, you can begin to formulate a detailed strategy to achieve them.

9.2.3 Determination of objectives and strategies

Now that you have defined the organi zation's vision and mission, you can develop a set of objectives that will lead you to the overall strategic goal or vision. For an example, an objective may be to increase market share year-over-year by at least five percent. Think of achieved objectives as building blocks in constructing your goal or vision.

9.2.4 Implementation and evaluation

The next step is to implement and evaluate the plan. Implementation in large organizations, such as governmental agencies or large corporations, will be done by a different set of organizational members than the members that created the plan. Different parts of the plan are typically distributed to various parts of the organization. You will also need to constantly monitor and assess the implementation of the plan to determine if the plan is achieving the objectives leading to the strategic goal. If not, then

Ever used a road map to get somewhere? Well, a strategy is a road map for a business. In this lesson, you'll learn about the process of strategy formulation. You'll also have a chance to take a short quiz after the lesson.

!!!What Is Strategy Formulation?

A strategy is a broad plan developed by an organization to take it from where it is to where it wants to be. A well-designed strategy will help an organization reach its maximum level of effectiveness in reaching its goals while constantly allowing it to monitor its environment to adapt the strategy as necessary. Strategy formulation is the process of developing the strategy.

9.3 THE PROCESS

Strategy formulation requires a series of steps performed in sequential order. The steps must be taken in order because they build upon one another. However, there are two processes that are continually performed throughout the strategy formulation: environmental scanning and continuous implementation.

Environmental scanning is simply the process of paying attention to the external environment for factors that may affect your organization's performance, which will need to be addressed in the strategy formulation process. For example, you will pay attention to what your competition is doing and make adjustments to your strategic plan as necessary throughout the process. **Continuous implementation** is simply implementing parts of the strategy that must take place in order for the next step of the strategy formulation process to be undertaken. The rest of the strategy formulation must be taken in order.

The Process: Steps

The first step is values assessment. Every organization has values, and the strategic plan should align with the organization's values. A value assessment should look into the personal values of the organization's members, organizational values, the organization's operating philosophy, culture and stakeholders.

The second step is vision and mission formulation. Once you have a firm handle on an organization's values, it's time to establish its mission and vision, which is the foundation upon which your strategy will be built.

An effective vision requires a core ideology and an envisioned future. A core ideology is the force that binds the organization together. It consists of core values and core purposes. The **core** purpose is the organization's *raison d'être*, or reason for being. It's why the organization even exists **-** what it's here for. The envisioned future is your conception of where the organization will be at a specific point in time.

The mission statement states the purpose of the organization in express and unequivocal terms. The mission statement helps to determine the allocation of resources, guides your organizational culture, establishes the boundaries of its activities and helps to facilitate accountability, control, time and performance by providing criteria for mission achievement.

The Process: Strategy

The next step is strategy design, which involves four elements. First, you must identify the major lines of your organization's business or activities, called LOBs.

Then, you must establish critical success indicators (CSIs**)**, which are just a way to measure progress towards the organization's mission. Indicators should include a target deadline. Indicators can include such things as the return on investment, profit margins, and customer loyalty and employee retention.

Next, you need to identify where you will focus your efforts, known **as strategic thrusts**. Examples of strategic thrusts include focusing on existing products and services, development of joint ventures and strategic alliances, diversification or liquidation.

Strategic Planning

Business or Organizations who are in their infancy or who are in their maturity need a very essential tool to assure survival. That tool is none other than Research and Development or R & D. Research and Development was extensively used by the pharmaceutical industry and those involved in scientific projects because it was considered an essential, a necessity. Today, however, small, medium-sized and large business and organizations have to employ research and development. It has become a necessity as well to business or organizations that desire to survive in the modern marketplace.

Research and Development is Essential

The roots of research and development go all the way back to ancient times. When kings and kingdoms waged war against each other, they would employ certain techniques of information gathering. The sole purpose of which was to gain an upper hand during the actual war or battle. This information was used to aid in the formulation of offensive and defensive strategies.

The same principles hold true today. Business or organizations need to gather information as part of its research and development, with the same purpose. That is of gaining an upper hand in the business battle. The modern day marketplace is a conglomeration of every conceivable product or service, almost. An in order to gain an advantage over the others excellently planned and analyzed research and development will do the job.

The method and the kind of research and development may not be the uniform in all business or organizations. But the goal is similar; to use data, information, behavior and the like, gathered in the research and development for the ultimate good and existence of the business or organization.

Connecting with End-Users

The purpose of business or organizations is to create and keep customers. This statement has been the driving force behind the efforts of retailers, manufacturers and service providers. But creating and keeping customers is no easy task. It is hard work, but it is hard work that results in a good pay off. To create and keep customers, business or organizations need an excellent research and development effort.

The primary goal of such effort is to begin with identifying the customer and his needs. If you begin with a product or an idea and start to find ways to sell it, you got the whole equation wrong. Research and development should and must connect business or organizations to the End-Users, the customer. And to do that one has to ask the right questions. Who is our customer? What are his needs? What are his wants? Who are currently providing it?

These questions allow business and organizations to channel research and development to the right direction. Asking the right questions will develop ones sensitivity (to what the customer needs and wants), and the right question will develop ones sensibility as well (to what products or services will satisfy them).

The research and development effort begins with identifying the customer. In a world where products and services have almost become like fashion “here today, gone tomorrow; the quicker the business or organization identifies its customers, the better its chance of providing a product or service on time.

Examples abound: mobile phones have always had a feature called SMS, and it was not utilized by the west, however, it was in Asia that customers discovered it can we a new way to communicate, Text as they call it. Phone manufacturers, who were able to quickly identify the end-user, came up with the phone and equipment and thus have a well-entrenched position in the industry. Customers sometimes might be difficult to identify but they are out there waiting.

9.4 DEVIATIONS DURING RESEARCH AND DEVELOPMENT

The modern marketplace is chaotic and so is the modern day customer. Today they want one product; tomorrow they do not even dare to look at it. They change their tastes frequently; today they may like earth colors, and tomorrow all they want is black. Today they want compact cars, tomorrow they still want small cars but with big engines. It is the normal behavior of the modern marketplace and the modern day customer. Deviations and variations are frequent occurrences in the modern marketplace.

It is the business or organizations research and development that will identify such deviations in customer and customer behavior way ahead of the competition that will make a tremendous effect to the business or organizations operations. A case in point is the fast food industry that was primarily conceptualized due to the changing lifestyle: the fast paced life does not allow people time to cook and eat at home frequently. Later on however, researchers found a very marginal deviation, they noticed that children and teens had purchasing power “money from their parents, and they could decide when and where to eat. Marketers then were able to come up with food chains and menus that cater to their specific needs.

A deviation will need a correction. Research and development might be looking the wrong way, and deviations and variations in lifestyle, market behavior and taste will be warning signals to business or organization to make such timely correction. There are no magic formulas in research and development, but the one logical thing to do is that if you find a deviation, and then make the necessary correction.

Unpredictable Scenarios

Deviations may be small unusual movements in the marketplace, scenarios are major movements in the marketplace. Such movements if not easily identified will spell tragedy on business or organizations. It is well-planned and well-coordinated research and development that will forewarn us of such events, unpredictable scenarios. They can become predictable through the research and development program of the business or organization.

We live in a world of balance and this is probably where research and development should start watching. There is day but there is also night; there is success but there is also failure, there is much but there is also less, there is a storm but there is also calm, the list can actually go on. And one unpredictable scenario is what many term as the trend-countertrend scenario.

The driving force of modern business and our lives is telecommunications: mobile phones, computers, and gadgets and fancy equipment that allow us to communicate and to be reached. These things have helped us tremendously by making the world one big global village. So, what is unpredictable about it? It is the counter trend that it generates.

Strategic planning aided by a well-planned and well-coordinated research and development should take note of these things. Let us take a peek at some counter-trends, these are the opposites: people can be easily reached today but it also produces so much stress and they want to go to places where they can not be reached, the answer? One counter trend: resorts and vacation places that cannot be reached. They have no phones, no computers, nothing.

Another counter trend: people have been working like mad to earn so much, but they become restless, overburdened and depressed, and they want to do something else. They want jobs overseas that may not be as rewarding financially but allows them to have a new environment and to rest. The truth is: there are so many job openings for westerners in Asia today than it was 10 years ago. Research and development indeed plays a vital role in strategic planning; it feeds the planners with the right stuff.

9.5 NOTES

9.6 SUMMARY

Business or Organizations who are in their infancy or who are in their maturity need a very essential tool to assure survival. That tool is none other than Research and Development or R & D. Research and Development was extensively used by the pharmaceutical industry and those involved in scientific projects because it was considered an essential, a necessity. Today, however, small, medium-sized and large business and organizations have to employ research and development. It has become a necessity as well to business or organizations that desire to survive in the modern marketplace.

9.7 KEY WORDS

Strategic planning, end users

9.8 SELFASSESMENTQUESTIONS

1. How strategic management plays an important role in the organization
2. Describe the development of strategic plan
3. Explain the strategic planning process

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UNIT-10 : ANALYZING INDUSTRIAL PRODUCT

Structure:

10.0 OBJECTIVES

After studying this unit, you should be able to;

- Explain product life cycle
- Analyze industrial product
- Evaluate the concept and process of new product development
- Explain new product development with live examples

10.1 PURPOSE AND IMPORTANCE OF INDUSTRIALANALYSIS

Marketing Environment Analysis cannot be completed without Industry Analysis.

An analysis of the mega environment alone will not enable the firm to have a total grasp of its environment, as such an analysis does not reveal details about its proximate environment, which includes the industry in which it operates and its competitors therein.

After all, the mega environment will be by and large common to all industries. It is the structural realities of the specific industry, the nature and intensity of competition therein, and the relative abilities of the players that are of special relevance to the firm in formulating its competitive / marketing strategy. It is not in the mega environment but in a specific industry that a firm operates as a player. And, it is here that the firm€™s efforts at scoring over competition are concentrated. So, a close scrutiny of the industry concerned becomes essential for completing the environment analysis.

Industry analysis supports strategy formulation by revealing industry attractiveness and Firm competitive position.

Industry analysis serves as a groundwork / prelude to strategy formulation. It helps the firm to assess industry attractiveness as well as its own strengths relative to the other players in the industry i.e. its own competitive position within the industry. The findings on these two fronts take the firm closer to strategy formulation.

In fact, industry attractiveness and firms competitive position within the industry are the two central concepts in forgoing competitive strategy. For knowing both of them, the firm needs to analyze the industry and competition. With this analysis, the firm gets to know details such as industry growth, industry profitability, industry potential and number of players in the industry, the manner in which the players are positioned within the industry, their market shares, their installed capacities and their relative strengths within the industry. In addition, it also gets an idea of the strength of the other competitive forces that shape the competition in the industry and hence industry profitability / attractiveness. Similarly, the firm gets to know its competitive position within the industry.

Why Analyze Industry and Competition?

- Analyzing industry and competition completes the process of marketing environment analysis.
- Supports strategy formulation; serves as a prelude to strategy formulation.
- Helps a firm know the two key factors in forging strategy: industry attractiveness and its competitive position within the industry.
- Helps the industry identify and build its competitive advantage.

Industry Analysis help Create Differential Advantage, which is Central to Strategy:

In simple terms, developing successful strategy means designing products, services and marketing programs that will enable a firm to attract the customers and score over competition. And it means that products, service and marketing programs should carry attributes, which are important to customers and which provide a differential advantage over competitors. It is not sufficient, though it is necessary, if the attributes are important to customers, for, competitors too will be providing attributes that are important t customer.

The firms offering must be not only important to customers, but also mean a differential advantage over competitors. Delivering a differential advantage is truly the name of the game in competitive strategy. The firm has to offer attributes of value to customers and which bring in a differential advantage over competition. And, analyzing industry and competition provides the firm with the knowledge required for achieving such a differential advantage. With industry analysis, the firm constantly compares its products, prices, channels and promotion with its competitors. And, from this comparison, the firm learns where and how it can secure a differential advantage.

Both industry attractiveness and the firm competitive position must be good for firm to prosper. A firm in a very attractive industry may not earn attractive profits if its competitive position within the industry is poor. In the same way, a firm with an excellent competitive position may still be quite unprofitable, and its efforts to enhance its position will be of little help, if the industry in which it operates is unattractive.

The fact is that, both industry attractiveness and the firm competitive position are dynamic entities; industries become more or less attractive over time; and a firm competitive position too keeps changing as it reflects the unending battle among competitors. Fortunately, both industry attractiveness and firm competitive position, especially the latter, can be shaped by a firm to a considerable extent, through its strategy.

10.2 PRODUCT LIFE CYCLE

Definition: Product life cycle (PLC) is the cycle through which every product goes through from introduction to withdrawal or eventual demise.

Description: These stages are:

Introduction: When the product is brought into the market. In this stage, there's heavy marketing activity, product promotion and the product is put into limited outlets in a few channels for distribution. Sales take off slowly in this stage. The need is to create awareness, notprofits.

***Growth*:** In this stage, sales take off, the market knows of the product; other companies are attracted, profits begin to come in and market shares stabilize.

Maturity: where sales grow at slowing rates and finally stabilize. In this stage, products get differentiated, price wars and sales promotion become common and a few weaker players exit.

***Decline*:** Here, sales drop, as consumers may have changed, the product is no longer relevant or useful. Price wars continue, several products are withdrawn and cost control becomes the way out for most products in this stage.

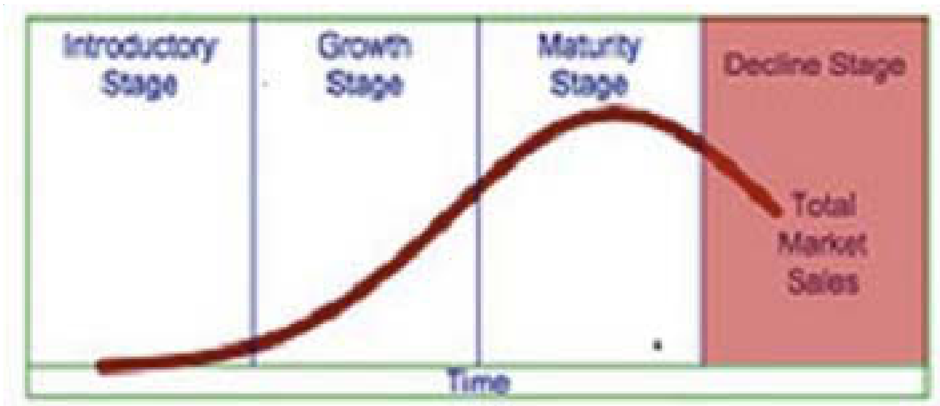
10.3 SIGNIFICANCE OF PLC

PLC analysis, if done properly, can alert a company as to the health of the product in relation to the market it serves. PLC also forces a continuous scan of the market and allows the company to take corrective action faster. But the process is rarely easy.

A decline is a fall or descent and, in the product life cycle, the decline stage represents similar behavior for products. The decline stage in the product life cycle is when a product dissolves as a result of decreased or negative growth.

The introduction and growth stages provided the strength for the success of the product to this point, and with most products the decline stage is a result of lower demand, which ultimately results from new inventions and technology advancements. For the company, profitability will decrease to a level at which it is no longer sensible to produce and distribute the product and production activities will cease.

For many of us as consumers, this activity offers some benefits, since companies that cannot maintain the product will slash the prices to eliminate inventories or discontinue the product altogether, which creates promotional 'sales' and 'clearances' for the consumers.



As competition in the market increases and multiple companies start to dominate the market, it is hard for the struggling companies to maintain acceptable sales and growth. Buyer preferences also change with the advancements of new technologies which in the end may make products obsolete.

Characteristics of the Decline Stage

There are some distinct characteristics of the decline stage:

- A decrease in sales can be seen as competition increases, and preference for the product falls.
- A decrease in sales price leads to lower profits, and, in some cases, losses for the company.

10.4 NEW PRODUCT DEVELOPMENT

Definition: New Product Development (NPD)

The term New Product Development (NPD) is normally used to refer to the complete process of introducing a new product in the market. Here product can be in terms of a tangible product or an intangible service as well.

The steps involved in the new product development include i) idea generation where the company also decides whether to go for cost leadership strategy or differentiation strategy ii) product design and engineering of the product iii) market research and analysis. Normally the new product development falls within the first stage (introduction phase) of the product life cycle.

Market (ex. DVD players into the home movie market), some are new to the company (ex. Game consoles for Sony), some are completely novel and create totally new markets (ex. the airline industry). When viewed against a different criteria, some new product concepts are merely minor modifications of existing products while some are completely innovative to the company.

- Changes to Augmented Product
- Core product revision
- Line extensions
- New product lines
- Repositionings
- Completely new

A new product is the culmination of a process, a series of steps beginning with generation of ideas and proceeding to the commercialization of full scale marketing of the product. It is the general process that conceives, develops and brings to the market the new product.

There are six logical steps in this creative process of new product development namely, Idea Generation, Screening, Business Analysis, Product Development, Test Marketing and Commercialization. This process can be compared to a hurdle race where the new product ideas are to cross all the barriers to go into commercial production.

¨ The following picture makes it amply clear to that effect:

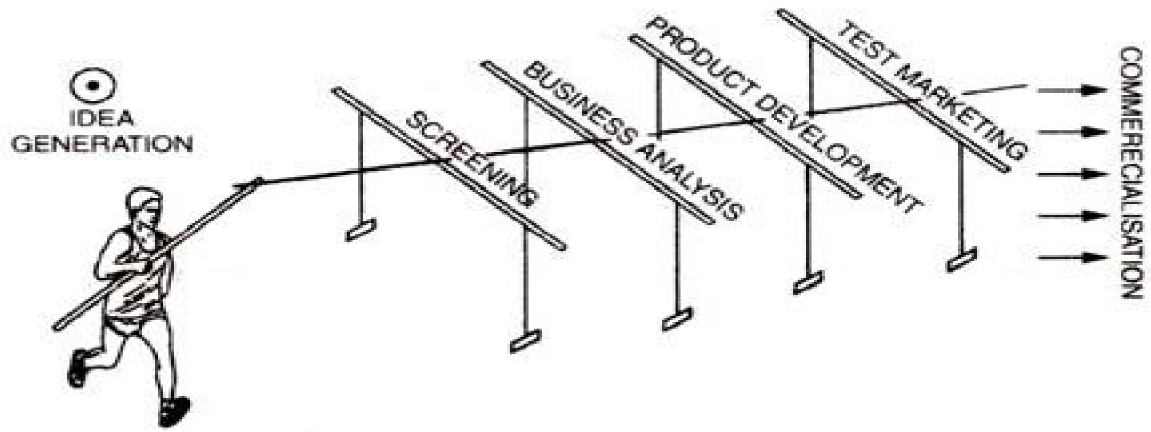


Fig. 1.06. Hurdles in Production Development

Idea Generation:

- The first vital step is to generate ideas, for new products are from new ideas. Product idea generation means fusion of perceived need with the recognition of a technical opportunity. That is, the perceived need may be new or old apparent or latent currently partly fulfilled or unfulfilled.

♦ However, when a technical opportunity is recognized to satisfy this need, a product idea is generated. Though house-wives knew full well that food can be cooked easily and quickly at high pressure, there was no such utensil. This was made possible by pressure cooker.

♦ Though the basic input for the development new products are ideas, all ideas do not become products. The real difficulty is not in gathering these ideas but in identifying the 'good' ones. Unfortunately, 'good' ideas are generally as plentiful as is often believed and they may well have to be actively and painstakingly sought.

♦ Therefore, large number of ideas must be generated in order to ensure finding a few good ones. In fact, greater the number of ideas generated, better the best ones are likely to be. It is so because; the rate of mortality of ideas for new products is exceptionally high even higher than the failure rates for products that are actually introduced. This situation is best explained by Decay/Mortality Curve of new product ideas.

♦ According to one famous study conducted by M/s Booz, Allen and Hamilton Inc., in 1968, of 51 companies, for every 58 ideas, about 12 pass the initial screening. Only 7 of these survive after evaluation and only 3 pass through test marketing. Of these, only two are eventually marketed and in the final analysis only one is said to be commercially successful.

♦ In another study of product development in food, manufacturing industry, it was concluded by the consultancy house M/s Buzzell and Nourse in 1967, out of every 1,000 new product ideas:

Number of Ideas	Percentage	Remarks
810	81.00	Were rejected at Preliminary Screening
135	13.50	Were Rejected on the basis of Product tests
12	1.20	Were discontinued after test - marketing
43	4.30	Were introduced to market on a regular basis
36	3.6	Remained on market after introduction

♦ Since, a company has a little or no control over the idea generation phase, constant stream of ideas both good and managerial are to be channeled into the system.

The Sources of New Ideas:

Idea generation involves using various idea sources and idea generation techniques to identify new ways of satisfying needs and monitoring evolving technologies. Where do new product ideas come from? Actually, they stem from many 'internal and external sources.

a) Internal sources:

These are in-company sources of product idea generation. There are four such possible sources.**These are:**

1. Basic research: Almost all large companies engage in some kind of basic or fundamental research. Research and development often are divided between the development of product ideas that have already passed the initial screening stages and research into areas of technology that give promise of producing totally new product concepts. For instance, 'Nylon' is the product of laboratory and 'Teflon' the result of basic research for space programme and 'Polythelene' and 'Transistor' are the outcome of Research and Development efforts within a firm.

2. Manufacturing:

People who manufacture products often have ideas about modifications and improvements. They do come out with new product ideas. It is the constant contact with product its performance, cost, quality, structure that makes them to give possible improvements.

3. Sales people: Company sales-representatives can be helpful source of new product ideas. These people are on the competitive firing line. They know what customers want and what they are not getting. They are the first one to learn about competitor's new products. They are in everyday contact with customers, and are thus in a good position to note consumer needs and the extent of satisfaction.

4. To management: Top executives can play an important part in the generation of new product ideas. Their ideas are ought to be good as they know precisely about the company needs and resources. Moreover, they are keen observers of technological trends and of competitive activity. If nothing else, the top company managers should set an example. If they expect the rest of the organization to be generating new product ideas, they should be doing so well.

B) External Sources:

External sources are those sources of product generating ideas that signify outside sources. There can be such six sources. **These are:**

1. Secondary sources of information: There are published lists of new products; list of available licenses that provide clues for new product ventures. Most magazines have a new product section and some business publications are devoted almost entirely to the area of new product news.

2. Competitors: Firms must establish a formal procedure for monitoring the new product activities of their competitors. By the time a competitor has a new product; it is pretty late to be trying to do anything about it. It is equally true that the new product developments are closely guarded secrets and it is often difficult to discover what actually is being developed.

However, most of these development activities are at least partially exposed. Good inferences about competitive product development can be made on the basis of indirect evidence gained from salesmen, suppliers, resellers and even customers. Hiring away competitor's employees, disassembly and analysis of competitor's product are quite common though legally challenged.

3. Customers:

The firms are to pay more and more attention to customers who constitute the focal point of new products. Consumers frequently generate new product ideas, or at least really information regarding problems that new and improved products would help to solve.

Most of the educated house-holds often write directly to the manufacturers with suggestions for product changes. General Food Corporation of America receives 80,000 letters from customers annually may be letters of complaints or compliments they are the source of new ideas.

4. Resellers:

Resellers are component part of firm's marketing system. They too have a stake in the manufacturer's new product development activity. Their needs in building a profitable line naturally are reflected in the products that their suppliers develop. They do contribute ideas of new products.

5. Foreign markets:

No country of the world has a monopoly of new product development. Each country is known for certain product or products say, Germany—Volkswagen Bug car; Italy—shoes; France—wine and perfumes; Japan electronics—particularly sound gadgets; India—soap and incense sticks and tea. These are natural gifts. These can be tapped and improved upon.

6. Inventors:

Inventors and other creators signify yet another key source of technological innovation and product ideas from outside the company. Most of the major companies are constantly approached with new product ideas that can be acquired or licensed for production or distribution. To make sure that the ideas received in this way are appropriately screened and not rejected quickly or lost, the creators are to be identified and trained too. Whatever may be the source, there is need for organized efforts to manage new ideas. When there is no formal management responsible for gathering ideas, many useful ideas are lost forever to the company. There should be someone responsible for this.

- The person can be say, new product manager who should be responsible for three things namely:
- SEARCH—he is to conduct an active search in the environment for good product ideas.
- STIMULATION—he would encourage company employees to develop and send ideas to his office and
- ENHANCEMENT—he would reroute the ideas to logical parties in other parts of the company for feedback and idea enhancement.
- Methods/Techniques for Generating New Product Ideas:
- Product idea generation as an effort should be organised and systematic. Several methods have been developed to generate better ideas with a view to better the sources of new ideas.
- The most commonly used are—Focus Groups—Attribute testing— Focused relationships—Brain storming—Reverse brain storming and Problem inventory analysis:
- **1. Focus groups:**
- The idea of focus group interviews is not new in the area of marketing research which has been in vogue since 1950s. A focus group interview consists of a moderator leading a group of people through an open in-depth discussion.
- This concept of group discussion need not be confused with in-depth interview. This is much different from a group interview in which the moderator simply asks the questions to solicit responses from the participants.
- In the focus group the moderator focuses the discussion of the group on the new product area in a non- directive manner. The focus group is an excellent means for the initial screening of ideas and concepts in addition to new idea generating. Recently, several procedures have been developed whereby quantitative analysis can be used in interpreting the focus group results. This has increased the credibility of this method.
- **2. Attribute listing:**

- This technique consists of listing of existing attributes of a product idea or area; these attributes are then modified until a new combination of attributes emerges that will improve the product idea or area.

♦ Thus, a company manufacturing say ball-point pens may list the product attributes as the ball-point, pen-head, and size, grip and so on. It may have new combinations to have improved ballpoint pen altogether. Generally, nine sets of questions are used in attribute testing to generate new product ideas.

The Indian media and entertainment industry: size and projections

Overall industry size (INR billion) (For Calendar Years)	2008	2009	2010	2011	2012	2013	2014	Growth in 2014 over 2013	2015P	2016P	2017P	2018P	2019P	CAGR (2014-2019P)
TV	241.0	257.0	297.0	329.0	370.1	417.2	474.9	13.8%	543.2	631.2	739.6	854.6	975.5	15.5%
Print	172.0	175.2	192.9	208.8	224.1	243.1	263.4	8.3%	284.5	307.1	331.9	358.0	386.8	8.0%
Films	104.4	89.3	83.3	92.9	112.4	125.3	126.4	0.9%	136.3	155.6	170.7	186.3	204.0	10.0%
Radio	8.4	8.3	10.0	11.5	12.7	14.6	17.2	17.6%	19.6	22.3	27.0	32.7	39.5	18.1%
Music	7.4	7.8	8.6	9.0	10.6	9.6	9.8	2.3%	10.4	12.0	14.2	16.9	18.9	14.0%
OOH	16.1	13.7	16.5	17.8	18.2	19.3	22.0	14.0%	24.4	27.1	29.6	32.2	35.1	9.8%
Animation and VFX	17.5	20.1	23.7	31.0	35.3	39.7	44.9	13.1%	51.0	58.7	68.5	80.6	95.5	16.3%
Gaming	7.0	8.0	10.0	13.0	15.3	19.2	23.5	22.4%	27.5	31.8	35.4	40.0	45.8	14.3%
Digital Advertising	6.0	8.0	10.0	15.4	21.7	30.1	43.5	44.5%	62.5	84.0	115.3	138.2	162.5	30.2%
Total	**580**	**587**	**652**	**728**	**821**	**918**	**1,026**	**11.7%**	**1159**	**1330**	**1532**	**1740**	**1964**	**13.9%**

Source: KPMG in India analysis.

10.5 NOTES

10.6 SUMMARY

Industry analysis serves as a groundwork / prelude to strategy formulation. It helps the firm to assess industry attractiveness as well as its own strengths relative to the other players in the industry i.e. its own competitive position within the industry. The findings on these two fronts take the firm closer to strategy formulation.

10.7 SELFASSESSMENT QUESTIONS

1. What is PLC? Explain its stages?
2. What do you mean by new product development? Give live examples.
3. Explain the steps involved in new product development process.

10.8 REFERENCES

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2. Marketing Strategies- James Colborn.
3. Business Marketing-Karunakaran.

UNIT - 11: PRODUCT DECISION

Structure:

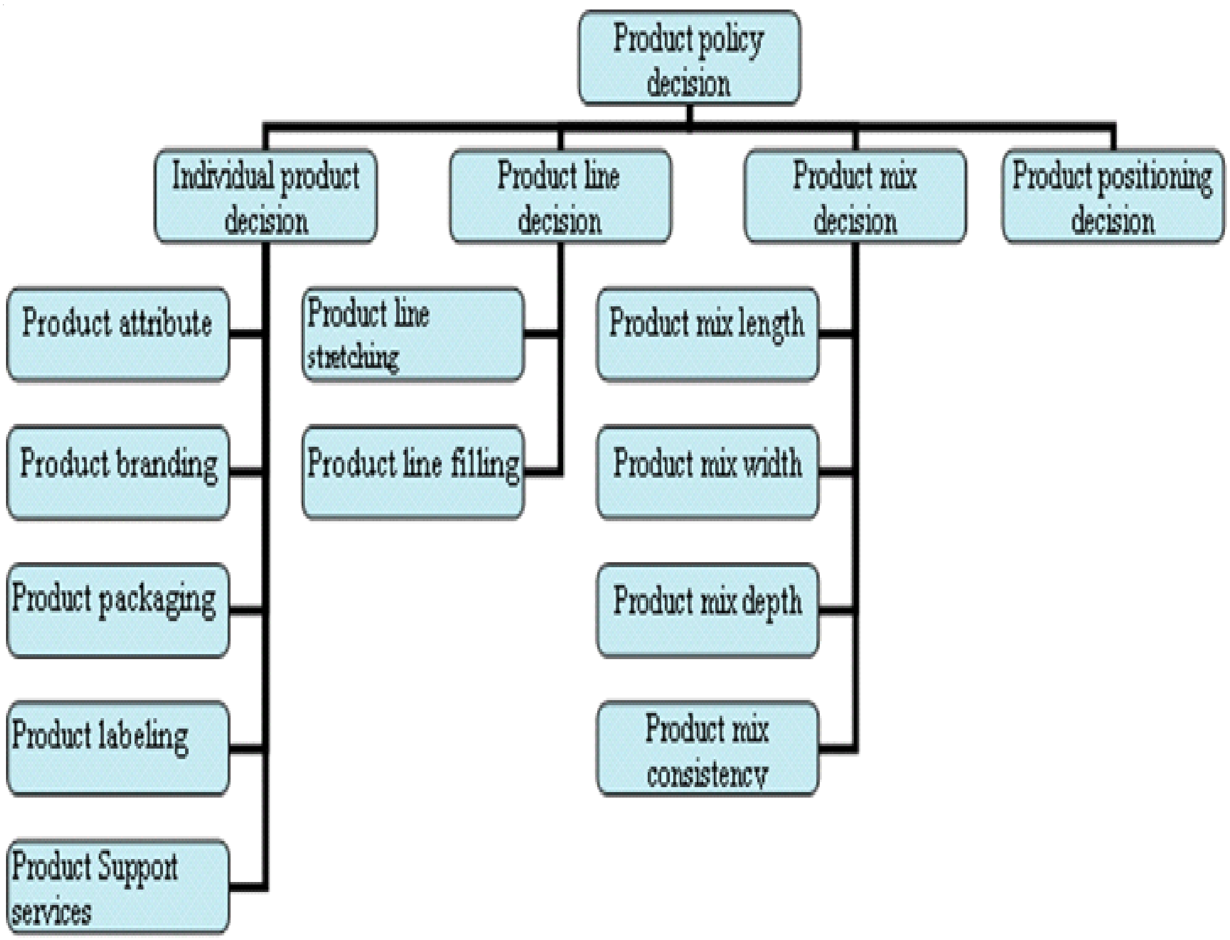
11.0 OBJECTIVES

After studying this unit, you will be able to;

- Explain the product decision
- Describe the pricing objectives
- Identify factors influence on pricing
- Evaluate the method of pricing, pricing strategy and pricing policies

11.1 INTRODUCTION

Product design plays a key role in the success of global marketing. Product design decisions address questions, such as whether to design different products for different national markets or to design a single product for the global market. Four factors influence the product design decisions of international marketers: preferences, cost, laws & regulations, and compatibility. The following chart shows the product policy decision in business enterprises



11.2 TYPES OF PRODUCT POLICY DECISION

The marketer has to keep in mind the product policy decision while introducing a product. As it is a competitive tool in the hands of the marketer. It involves four basic decisions. These are:

11.2.1 Individual product decision:-

a) Product attribute: It refers to the quality, feature, style and design of the product. With the help of the quality manufacturer can give the customers assured quality product. Feature helps in differentiating the product from other products. Style and design helps to bring the attention of the customers towards the product.

b) Product branding: It is very essential to give a product a brand name. Only with the help of brand name the customer can differentiate the product from the other products. Branding facilitates the marketers in promoting the product and making consumer brand conscious.

c) Product packaging: Packaging means the wrapper which contains the product. Like a pack of Cadbury chocolate has a primary golden color wrapper and then a secondary wrapper to cover it. Packaging act as a silent salesman. It is with the help of the packaging the customer come to know about the product quality, quantity, weight, price etc.

d) Product labeling: Labeling gives the consumer information regarding the manufacturer's name, place, date of manufacturing, expiry date, calories, carbohydrates, nutritional value etc.

e) Product support services:- It means the services which are provided to the customer after selling the product to the customer like after sale services, installation etc.

11.2.2 Product line decision: –

It means group of product which are closely related to each other. Like lakme, maybaline etc. in product line decision the marketer has to make decision regarding the product line length, which means the number of product in the product line. There may be short product line, means the marketer can increase the profit by adding new product or there may be long product line. There are two ways of adding the product.

i) Product line stretching: It means when company adds a new product by stretching the product line by upward, downward or both ways.

ii) Product line filling: It means adding a new product within existing range of products.

11.2.3 Product mix decision:-

It means the complete set of product line produced and sold by the company. Like nestle produces, milk powder, maggi, ghee, sugar, tea etc. product mix consists:

i) Product mix width: Refers to how many products company is offering. Like soap, shampoo, powder etc.

ii) Product mix length: Refers to how many no. of items in each product line. Like 5 kind of soap, 7 kind of powder etc.

iii) Product depth: Refers to different items in each product line. Like Hindustan liver ltd. offering different kind of soap eg. Lux, santoor, hamam.

iv) Product consistency Refers to how closely related the various product line in end use.

11.2.4 Product positioning decision

It is the way how the marketer communicate the information regarding the product to the prospective buyer. It can be done on the biases of price or size or usage.

11.3 PRICING

Price is the value that is put to a product or service and is the result of a complex set of calculations, research and understanding and risk taking ability. A pricing strategy takes into account segments, ability to pay, market conditions, competitor actions, trade margins and input costs, amongst others

11.4 IMPORTANCE OF PRICING IN MARKETING STRATEGY

11.4.1 Price is the Pivot of an Economy:

In the economic system, price is the mechanism for allocating resources and reflecting the degrees of both risk and competition. In an economy particularly free market economy and to a less extent in controlled economy, the resources can be allocated and reallocated by the process of price reduction and price increase.

Price policy is a weapon to realize the goals of planned economy where resources can be allocated as per planned priorities.

Price is the prime mover of the wheels of the economy namely, production, consumption, distribution and exchange. As price is a sacrifice of purchasing power, it affects the living standards of the society; it regulates business profits and, hence, allocates the resources for the optimum output and distribution. Thus, it acts as powerful agent of sustained economic development.

11.4.2. Price regulates demand:

The power of price to produce results in the market place is not equaled by any other component in the product-mix.

It is the greatest and the strongest 'P' of the four 'Ps' of the mix. Marketing manager can regulate the product demand through this powerful instrument. Price increases or decreases the demand for the products. To increase the demand, reduce the price and increase the price to reduce the demand.

Price has a special role to play in developing countries where the marginal value of money is high than those of advanced nations. De-marketing strategy can be easily implemented to meet the rising demand for goods and services.

As an instrument, it is a big gun and it should be triggered exclusively by those who are familiar with its possibilities and the dangers involved.

It is so because; the damage done by improper pricing may completely sap the effectiveness of the well-conceived marketing program. It may defame even a good product and fame well a bad product too.

11.4.3. Price is competitive weapon:

Price as a competitive weapon is of paramount importance. Any company whether it is selling high or medium or low priced merchandise will have to decide as to whether its prices will be above or equal to or below its competitors. This is a basic policy issue that affects the entire marketing planning process. Secondly, price does not stand alone as a device for achieving a competitive advantage.

In fact, indirect and non-price competitive techniques often are more desirable because, they are more difficult for the competitors to copy. Better results are the outcome of a fine blend of price and non-price strategies. Thirdly, there is close relationship between the product life-cycle and such pricing for competition.

There are notable differences in the kinds of pricing strategies that should be used in different stages. Since the product life span is directly related to the product's competitiveness, pricing at any point in the life-cycle should reflect prevailing competitive conditions.

11.4.4. Price is the determinant of pr ofitability:

Price of a product or products determines the profitability of a firm, in the final analysis by influencing the sales revenue. In the firm, price is the basis for generating profits. Price reflects corporate objectives and policies and it is an important ingredient of marketing mix. Price is often used to off-set the weaknesses in other elements of the marketing-mix.

Price changes can be made more quickly than any other changes in the product, channel, and personal selling and sales-promotion includes advertising. It is because; price change is easily understood and communicating to the buyer in a precise way. That is why, price changes are used frequently for defensive and offensive strategies. The impact of price rise or fall is reflected instantly in the rise or fall of the product profitability, thinking that other variables are unaffected.

11.4.5. Price is a decision input:

In the areas of marketing management, countless and crucial decisions are to be made. Comparatively marketing decisions are more crucial because, they have bearing on the other branches of business and more difficult as the decision-maker is to shoot the flying game in the changing marketing environment.

Normally, profit or contribution is taken as a base for pay-off conditions. Price can be a better criterion for arriving at cut-off point because; price is the determinant of profit or contribution.

As pointed earlier, price as an indicator has a special role in the decision-making process in developing countries because, consumer response to price changes will be more quick and tangible as people have higher marginal value of money at their disposal. For instance, if it is a decision regarding selecting product improvement possibilities, select that possibility which gives the highest price as compared to the cost.

These five points make product pricing an important and major function of marketing manager. However, until recently, it has been one of the most neglected areas of marketing management.

In fact, we must have a specialist in pricing as we do have in other functions of marketing. This negligence is quite evident from the fact that even the well-known companies in the world price their products on simple concepts of costs market position competition and desired profit. Scientific pricing is much more than this easy exercise.

11.5 PRICING OBJECTIVES

1. Price and Pricing Strategies

Our local farmer needs to come up with a pricing strategy for his certified organic product. You will have a chance to learn all about the pricing strategy choices that he can choose from for his marketing mix. Price is one of the four P's that make up the marketing mix. The other P's of the marketing mix are product, promotion and place.

A consumer must pay a price for a product or service, and price is what is given up in exchange to acquire a good or service. Price is very important to the marketer as well because it is the revenue that's acquired Revenue is the price charged to customers multiplied by the number of units sold.

The biggest challenge facing a marketer is to figure out what price to charge. A higher price can communicate quality and prestige, while a lower price can communicate lower quality and cheapness, and how you balance the two all depends on the type of product. The three types of pricing strategies that the farmer can choose are profit-oriented maximization, sales-oriented pricing, and status quo pricing.

2. Profit-Oriented Pricing Objectives

Profit-maximization pricing means setting prices so that total revenue is as large as possible relative to total costs. This is the prime pricing strategy to use if you are in a monopoly. The farmer is the only major farm in town selling certified organic produce, so maybe this would be an excellent option for him to use.

There are some other ways that the farmer can maximize profits. He can increase customer satisfaction, which can improve revenue, and he also can reduce costs. Some ways for the farmer to reduce costs would be to lay off employees and improve his product efficiency by minimizing loss of crops and implementing more effective mass distribution of his product line.

3. Sales-Oriented Pricing Objectives

Sales-oriented pricing objectives are based on either market share or unit/dollar sales. Market share is a company's product sales as a percentage of total sales for that industry, and it can be shown via revenue or units. For example, our farmer has 70% of the local organic produce market in revenue.

4. Other Pricing Objective

Price forms an important constituent of the marketing mix and is generally governed by the organizations pricing objectives, which is reflective of the marketing, financial, product and strategic goals, along with the consumer price expectations, the stock at hand, the production capacity and the associated price elasticity.

Pricing objectives can be partitioned into 5 major heads:

a) Survival:

Prices are considerably flexible. The company might lower the prices in order to increase sales by taking a hit on profitability or undergoing losses to keep the business going. It is utilized generally when a company is willing to accept short term losses for the sake of long term viability.

b) Profit:

Price influences the profit made by the company as the price should be such that cost of production is covered while the price also determines the number of units of a good or service sold. Herein there are 2 major categories

a. Target Return: The price point is decided based on meeting a certain targeted return which might be time bound

b. Maximize profit: The price objective in order to maximize profit can be for the long term as well for the short term. Short term maximized profit is possible in case of lack of competition wherein the company charges a very high price since it's the sole company. Whereas in order to maximize long term profit he needs to price in order to avoid new entrants in the industry so that it remains the sole provider.

c) Sales:

Maximizing sales is equivalent to generating as much revenue as possible, irrespective of the profit margins. This might be opted by companies which are in a financial conundrum and need quick cash to pay off their debts. It might be achieved by getting rid of the inventory to have more liquidity. Because of its short term vision and less focus on profitability it is generally to meet short term objectives.

d) Market share:

Some firms set prices in order to capture a large share of the sales in their industry which is not reflective of higher profits. Many companies believe it is imperative to have a major market share for their survival in the industry. It has been widely witnessed in cell phone industry wherein lava, micromax, Intel, and many players fight for a majority market share in the low cost cell phone market in India

e) Status Quo: There are times when the company just wants to maintain the status quo and prices its product similar to its competitors. Companies following this keep a close eye on the prices of the competitors. It has generally been observed in the airline industry wherein the prices among competitors of low cost airlines are highly comparable separated by a few rupees.

11.6 FACTORS AFFECTING PRICING DECISIONS

There are number of factors affecting the pricing decisions and price is not determined simply, there are many factors affecting pricing decisions. The reason is that the price is a very sensitive issue for the customers in their purchasing behavior. Following are the two main factors affecting pricing decisions.

1– Internal Factors

2- External Factors

- **Internal Factors**:

Internal factors are those factors that are related to the internal environment of the business. This means that the issues that prevail within the business organization and upon which the organization has control are included in this category. Internal factors further include the following.

- Marketing Objectives & Marketing Mix Strategies
- Costs
- Organizational Considerations

Each of these is discussed one by one.

Internal Factors Affecting Pricing Decisions

01- Marketing Objectives & Marketing Mix Strategies:

The objectives of the business serve as a basis for the development of proper marketing mix strategy that also includes in the price determination process. Those businesses that have kept clear objectives feel convenience in setting an effective price for their products or services, because their prices are built on the ground of stated objectives. Following are some of important objectives that are covered by most businesses.

- **Survival**:

In this objective the main purpose of the business is survival in the market. The profit maximization purpose becomes secondary importance for such business, because its survival is at stake due to unfavorable market conditions like tough competition, changes in tastes of customers etc. In this case the business tries to keep its price low, so that a sufficient proportion of its product or service should be sold.

- **Profit Maximization**:

Another important objective is the profit maximization that is employed by many businesses. Such businesses count the costs and demand of their products or services and set different prices. From these price combinations, a business chooses the price that can give maximum profit, return on investment or cash flow. This objective is beneficial for the short run and it neglects the long term future of the business. Some businesses try to increase their market share for the purpose of getting highest profit, because their management believed that higher market share lead to lower cost and hence higher profits. Businesses adopting such strategy also keep their prices low.

- **Product Quality Leadership**:

A business can set its basic objective as the product quality leadership in the market. For this purpose, such business keeps its price higher in order to cover the higher performance of its product along with the costs incurred on research and development.

Price can be used to accomplish other objectives for a business. Example include lowering of price to avoid increasing competition, keep prices competitive to make market stable and avoid government intervention, to increase demand by lowering prices etc. In short the decisions taken in respect of price affect other marketing mix variable decisions and so all of these decisions should be consistent with one another to make a marketing program effective. The business should also keep its product as differentiated and set relatively high price for the uniqueness of its product. In this way price is based on many non-pricing factors.

02- Costs:

Cost is the fundamental element in setting prices for a product or service. The simple rule is that the business charges such price that should not only cover all of the costs incurred in manufacturing, distribution and promotion of the product or service, but also provide a fair return on the invested money. If a business has low costs, then it can increase its sales and profit by lowering the price of its product or service.

Kinds of Costs:

Generally there are two major types of costs which are as follow.

1. a) Fixed Cost
2. b) Variable Cost

- **Fixed Cost**:

The fixed cost is such cost that remains fixed and does not change with the changing level of production or sales. The total fixed cost remains same but fixed cost per unit may change. The example includes rent paid for the building, interest paid on loan, salaries to employee staff etc.

- **Variable Cost:**

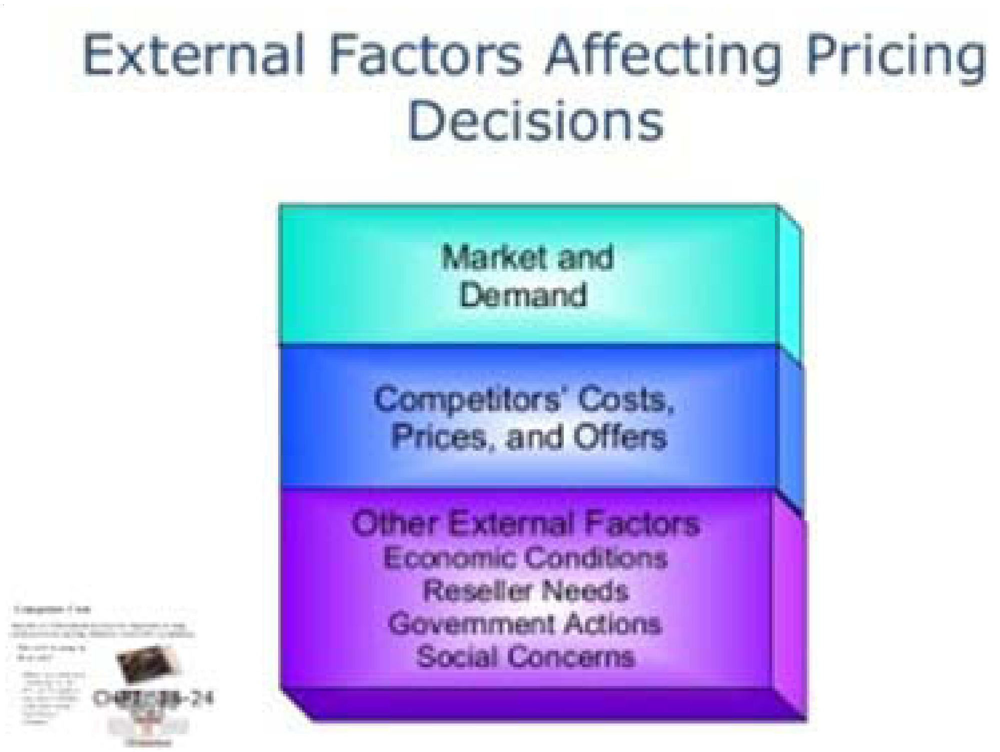
The variable cost is that kind of cost which changes with the change in the level of production and sales. Although the total variable cost change but the unit variable cost remains the same. For example, each car produced includes the variable cost of tires, metal sheets, Misc items etc that change with the increase or decrease in the quantity of production and sales.

The management of the business should ascertain different level of costs with respect to different levels of production and sales so that the lowest cost can be attained for the determination of effective prices for the manufactured products or services.

03- Organizational Considerations:

This factor includes the fact that who should be given the responsibility to set the price within the organization. There many ways to deal with such an issue. In smaller businesses, top management is responsible for setting the price of the product. On the other hand, in large organizations product line managers or divisional manager has the authority to set price for the product or service. In case of industrial markets, salespersons handle the pricing of product by negotiating with the customers within the pre-specified range of prices. In certain price sensitive industries (Oil Companies, Aerospace etc) have a separate pricing department that can either directly determine the best price or facilitates the pricing process of the business. In some firms, top management like the proposed prices of the lower level employees like salespersons etc.

- **External Factors:**



External Factors Affecting Pricing Decisions

External Factors include factors that are related to the external environment of the business. The business has less control over these variables of the external environment. The following are included in this category.

1) The Market and Demand

2) Costs, Prices and Offering of Competitors

- **The Market and Demand:**

We have already discussed that the lower limits of price are determined by the costs incurred. On the other hand the upper limits are determined by the demand and market elements. Price is balanced by the benefits of owning the relative product or service by consumer and industrial customers. For this purpose the price and demand relationship for a product is essential to be understood before setting its price.

- **Pricing in different Markets:**

Different market conditions require different sets of pricing strategies. Generally there are following four types of markets.

1) Pure Competition

2) Monopolistic Competition

3) Oligopolistic Competition

4) Monopoly

5) Consumer perception about value and price

6) Price Demand Relationship

01.Pure Competition:

In case of pure competition in the market, there are many buyers and sellers in the markets dealing with uniform commodities like wheat etc. There is one ongoing price in the whole market and no single buyer or seller can affect this price. Because the customers can easily obtain their required quantity at the ongoing price of the market, so no seller can charge higher prices. Similarly, no seller can charge a lower price because he can sell all his offered quantity to a lot of customers on the market. In case of the rise of the price or profit in the market, new sellers are attracted to enter in the market. In pure competition, pricing, sales promotion, new product development and marketing research are not supported. In other words the sellers on the market do involve in preparation of marketing strategies.

02. Monopolistic Competition:

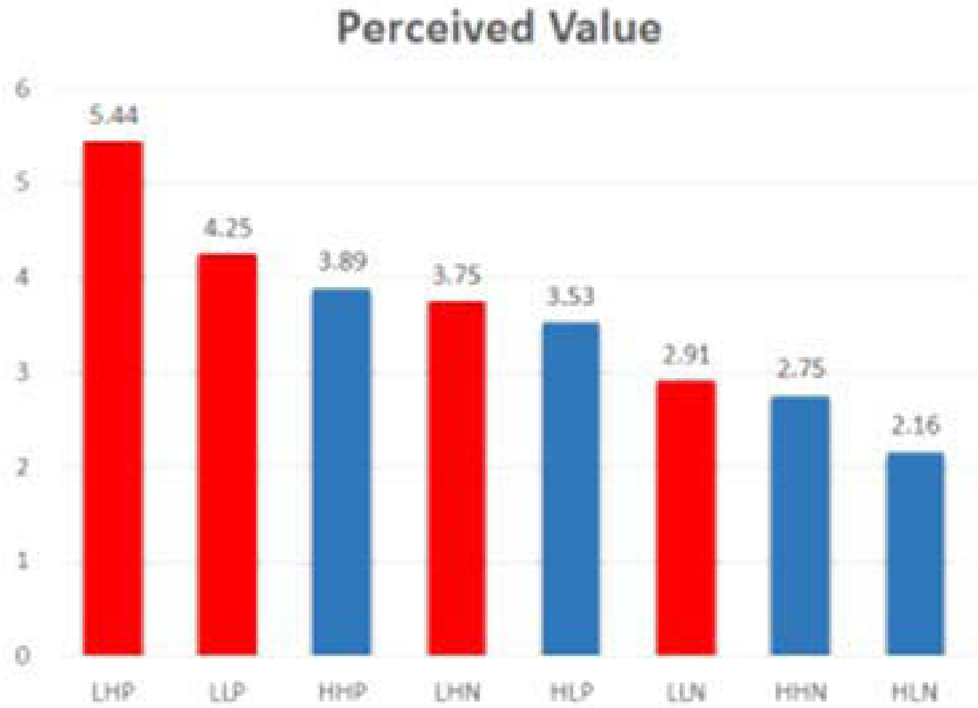
In case of monopolistic competition there are many sellers and buyers who offer their products not at a single price but at a range of prices. The difference in the price range is due to the differentiated product or service offering by the sellers. Customers can feel the difference between the products and hence pay different price for them. These differences can be in shape of features, quality or style etc. So in this kind of market businesses spend more time and money on differentiating their product or services in the shape of sales promotion, advertising etc. A single business is not affected by the marketing strategies of its competitors because there are many competitors in the market.

03. Oligopolistic Competition:

Another factors affecting pricing decisions is oligopolistic. In oligopolistic market, there are few sellers and buyers which are conscious about the pricing and other marketing strategies of competitors. The offered products are either uniform or differentiated. It is difficult for new seller to enter in the market. A certain change in the price of single firm affects its own soil in a negative way even if a seller lowers its price; its competitors also decrease their price. This means that the benefits are only for a short while.

04. Monopoly:

Another market condition is monopoly in which there is only a single seller who can offer its products or services at different rates. As the seller is single and the buyers are much more, therefore the seller charges a relatively higher price because there is no fear of competition. In case of regulated monopoly, the seller can charge only a fair price, but in case of unregulated monopoly the seller has freedom to charge extra for its offering. But mostly the monopoly firm keeps its price low for a number of reasons like quick penetration in tl



Consumer Perception about Value & Price

05- Consumer Perception about Value & Price:

The bottom reality in the pricing decision is that the customers are the final authority who determines the price of a product or service. It is obvious that the consumers pay the price for the exchange of the benefits that they avail by using the relative product or service. So businesses should focus on the pricing that is consumer oriented in which they try to determine that how much would be the consumer willing to pay for how much benefit of a certain product or service.

06. Price Demand Relationship:

Businesses should also consider the important relationship between the price of a product or service and its demand. Generally price and demand is inversely related which means that the increase in the price would lead to the decrease in the demand for that product and vice versa. The reason behind this inverse relationship is that the customers have limited resources for the fulfillment of their demands.

In some case the price and demand show the direct relationship which means that the increase in the price would lead to the increase in the demand of that product in the market. But this only happens with the prestigious products where increased price means increased quality.

The business management should also consider the elasticity of the demand of their offering product while setting its price.

Costs, Prices & Offering of Competitors :

One of external factors affecting pricing decisions of the business is the costs, price and offering of the competitors as compared to its own cost, price & offering. This means that the management of the business should take into account the change in the price and offering of the competitors and take steps accordingly.

There are also some other external factors affecting pricing decisions and are important to be considered in determining a price for a product or service, like economic conditions of the country, government rules and regulations etc.

11.7 METHODS OF PRICING

There are different pricing methods or strategies which are used by the marketer to attract the customer.

1) Cost based pricing: this type of pricing strategies uses break even concept which means the point where the total cost = total revenue. Profit will be zero at break even point. At level where the total revenue > total cost there is profit and where total revenue< total cost there is loss.

2) Demand based pricing: it is of two types;

a) Skimming pricing: it means skim the market initially with high price and high profit, later settle down for the lower price. It means skim the cream initially from the market.

b) Penetration pricing: it seeks to achieve high sale with low price. It is generally used when there are non luxury goods.

3) Competition oriented pricing: in a competitive market the companies generally opt for this pricing strategy. It has three types.

a) Premium pricing: it means price above the competitor's price.

b) Discount pricing: it means price below the competitor's price.

c) Parity pricing: it means price equals to the competitor's price.

4) Value pricing: this method is used when the objective is not to recover the cost of the product but to judge the value of the product in the eyes of the customer. Like homeshop 18.

5) Product line pricing: in this case the company need not fix the price for each product rather they fix the price for the entire product line which results in optimal sales through optimal profit.

6) Sealed bid or tender pricing: this is suitable for those companies where institutional customers call the tenders from the companies. The best and lowest price tender is accepted.

7) Affordable or social welfare pricing: the pricing is done in such a way that all the segments of the market afford to buy and consume the product as per their need. Like government subsidy help each segment of the consumer to buy the product at an affordable pricing.

8) Differentiated pricing: in this case different price is charged by the company from the different segment. Like charging low price from the whole sellers and high price from the retailers.

9) Psychological pricing: many sellers use this technique of selling the product. Like 99 store.

10) Target pricing: here the price is fixed at full cost + mark up.

11) Loss leader: sometime firm sell multiple products, charge relatively low price on some popular product with the hope that customer who will buy this product will also buy the other product of the firm.

12) Cyclical pricing: in depression firm reduce the price of the product while in boom increases the price.

13) Suggested pricing: in this case the manufacturer or whole seller suggests the retailer to charge this price from the customers.

11.8 PRICING STRATEGY

Pricing strategy refers to method companies use to price their products or services. Almost all companies, large or small, base the price of their products and services on production, labor and advertising expenses and then add on a certain percentage so they can make a profit.

Pricing strategy in marketing is the pursuit of identifying the optimum price for a product. This strategy is combined with the other marketing principles known as the four P's (product, place, price, and promotion), market demand, product characteristics, competition, and economic patterns

Pricing is one of the four elements of the marketing mix, along with product, place and promotion. Pricing strategy is important for companies who wish to achieve success by finding the price point where they can maximize sales and profits. Companies may use a variety of pricing strategies, depending on their own unique marketing goals and objectives.

Premium Pricing

Premium pricing strategy establishes a price higher than the competitors. It's a strategy that can be effectively used when there is something unique about the product or when the product is first to market and the business has a distinct competitive advantage. Premium pricing can be a good strategy for companies entering the market with a new market and hoping to maximize revenue during the early stages of the product life cycle.

Penetration Pricing

A penetration pricing strategy is designed to capture market share by entering the market with a low price relative to the competition to attract buyers. The idea is that the business will be able to raise awareness and get people to try the product. Even though penetration pricing may initially create a loss for the company, the hope is that it will help to generate word-of-mouth and create awareness amid a crowded market category.

Economy Pricing

Economy pricing is a familiar pricing strategy for organizations that include Wal-Mart, whose brand is based on this strategy. Aldi, a food store, is another example of economy pricing strategy. Companies take a very basic, low-cost approach to marketing—nothing fancy, just the bare minimum to keep prices low and attract a specific segment of the market that is very price sensitive.

Price Skimming

Businesses that have a significant competitive advantage can enter the market with a price skimming strategy designed to gain maximum revenue advantage before other competitors begin offering similar products or product alternatives.

Psychological Pricing

Psychological pricing strategy is commonly used by marketers in the prices they establish for their products. For instance, $99 is psychologically "less" in the minds of consumers than $100. It's a minor distinction that can make a big difference.

11.10 PRICING POLICIES

Definition: Price is the value that is put to a product or service and is the result of a complex set of calculations, research and understanding and risk taking ability. A pricing strategy takes into account segments, ability to pay, market conditions, competitor actions, trade margins and input costs, amongst others.

HBR first published this article in November 1950 as a practical guide to the problems involved in pricing new products. Particularly in the early stages of competition, it is necessary to estimate demand, anticipate the effect of various possible combinations of prices, and choose the most suitable promotion policy. Then as the product's market status matures, policy revisions become necessary. Joel Dean outlines the possible price strategies for each stage of a product's market evolution and the various grounds for making a choice. To update his original statement, Mr. Dean has written a retrospective comment, which appears at the end of this article. He amplifies his earlier article with insights from intervening years and in light of such developments as inflation.

How to price a new product is a top management puzzle that is too often solved by cost theology and hunch. This article suggests a pricing policy geared to the dynamic nature of a new product's competitive status. Today's high rate of innovation makes the economic evolution of a new product a strategic guide to practical pricing.

New products have a protected distinctiveness which is doomed to progressive degeneration from competitive inroads. The invention of a new marketable specialty is usually followed by a period of patent protection when markets are still hesitant and unexplored and when product design is fluid. Then comes a period of rapid expansion of sales as market acceptance is gained.

Next the product becomes a target for competitive encroachment. New competitors enter the field, and innovations narrow the gap of distinctiveness between the product and its substitutes. The seller's zone of pricing discretion narrows as his or her distinctive "specialty" fades into a pedestrian "commodity" which is so little differentiated from other products that the seller has limited independence in pricing, even if rivals are few.

Throughout the cycle, continual changes occur in promotional and price elasticity and in costs of production and distribution. These changes call for adjustments in price policy.

Appropriate pricing over the cycle depends on the development of three different aspects of maturity, which usually move in almost parallel time paths:

1. Technical maturity, indicated by declining rate of product development, increasing standardization among brands, and increasing stability of manufacturing processes and knowledge about them.

2. Market maturity, indicated by consumer acceptance of the basic service idea, by widespread belief that the products of most manufacturers will perform satisfactorily, and by enough familiarity and sophistication to permit consumers to compare brands competently.

3. Competitive maturity, indicated by increasing stability of market shares and price structures.

Of course, interaction among these components tends to make them move together. That is, intrusion by new competitors helps to develop the market, but entrance is most tempting when the new product appears to be establishing market acceptance.

The rate at which the cycle of degeneration progresses varies widely among products. What are the factors that set its pace? An overriding determinant is technical—the extent to which the economic environment must be reorganized to use the innovation effectively. The scale of plant investment and technical research called forth by the telephone, electric power, the automobile, or air transport makes for a long gestation period, as compared with even such major innovations as cellophane or frozen foods.

Development comes fastest when the new gadget fills a new vacuum made to order for it. Electric stoves, as one example, rose to 50% market saturation in the fast-growing Pacific Northwest, where electric power had become the lowest-cost energy.

Products still in early developmental stages also provide rich opportunities for product differentiation, which with heavy research costs holds off competitive degeneration.

But aside from technical factors, the rate of degeneration is controlled by economic forces that can be subsumed under rate of market acceptance and ease of competitive entry.

Market acceptance means the extent to which buyers consider the product a serious alternative to other ways of performing the same service. Market acceptance is a frictional factor. The effect of cultural lags may endure for some time after quality and costs make products technically useful. The slow catch-on of the garbage-disposal unit is an example.

On the other hand, the attitude of acceptance may exist long before any workable model can be developed; then the final appearance of the product will produce an explosive growth curve in sales. The antihistamine cold tablet, a spectacular example, reflected the national faith in chemistry's ability to vanquish the common cold. And, of course, low unit price may speed market acceptance of an innovation; ball-point pens and all-steel houses started at about the same time, but look at the difference in their sales curves.

Ease of competitive entry is a major determinant of the speed of degeneration of a specialty. An illustration is found in the washing machine business before the war, where with little basic patent protection the Maytag position was quickly eroded by small manufacturers who performed essentially an assembly operation. The ball-point pen cascaded from a $12 novelty to a 49-cent "price football," partly because entry barriers of patents and techniques were ineffective. Frozen orange juice, which started as a protected specialty of Minute Maid, sped through its competitive cycle, with competing brands crowding into the market.

At the outset innovators can control the rate of competitive deterioration to an important degree by nonprice as well as by price strategies. Through successful research in product improvement innovators can protect their specialty position both by extending the life of their basic patents and by keeping ahead of competitors in product development. The record of IBM punch-card equipment is one illustration. Ease of entry is also affected by a policy of stay-out pricing (so low as to make the prospects look uninviting), which under some circumstances may slow down the process of competitive encroachment.

Steps in Pioneer Pricing

Pricing problems start when a company finds a product that is a radical departure from existing ways of performing a service and that is temporarily protected from competition by patents, secrets of production, control at the point of a scarce resource, or by other barriers. The seller here has a wide range of pricing discretion resulting from extreme product differentiation.

A good example of pricing latitude conferred by protected superiority of product was provided by the McGraw Electric Company's "Toastmaster," which, both initially and over a period of years, was able to command a very substantial price premium over competitive toasters. Apparently this advantage resulted from

(1) a good product that was distinctive and superior and

(2) substantial and skillful sales promotion.

Similarly, Sunbeam priced its electric iron $2 above comparable models of major firms with considerable success. And Sunbeam courageously priced its new metal coffeemaker at $32, much above competitive makes of glass coffeemakers, but it was highly successful.

To get a picture of how a manufacturer should go about setting a price in the pioneer stage, let me describe the main steps of the process (of course the classification is arbitrary and the steps are interrelated)

(1) estimate of demand.

(2) decision on market targets.

(3) design of promotional strategy. and

(4) choice of distribution channels.

Estimate of Demand

The problem at the pioneer stage differs from that in a relatively stable monopoly because the product is beyond the experience of buyers and because the perishability of its distinctiveness must be reckoned with. How can demand for new products be explored? How can we find out how much people will pay for a product that has never before been seen or used? There are several levels of refinement to this analysis.

The initial problem of estimating demand for a new product can be broken into a series of subproblems.

(1) whether the product will go at all (assuming price is in a competitive range)

(2) what range of price will make the product economically attractive to buyers

(3) what sales volumes can be expected at various points in this price range.and

(4) what reaction will price produce in manufacturers and sellers of displaced substitutes.

The first step is an exploration of the *preferences and educability of consumers,* always, of course, in the light of the technical feasibility of the new product. How many potential buyers are there? Is the product a practical device for meeting their needs? How can it be improved to meet their needs better? What proportion of the potential buyers would prefer, or could be induced to prefer, this product to already existing products (prices being equal)?

Sometimes it is feasible to start with the assumption that all vulnerable substitutes will be fully displaced. For example, to get some idea of the maximum limits of demand for a new type of reflecting-sign material, a company started with estimates of the aggregate number and area of auto license plates, highway markers, railroad operational signs, and name signs for streets and homes. Next, the proportion of each category needing night-light reflection was guessed. For example, it was assumed that only rural and suburban homes could benefit by this kind of name sign, and the estimate of need in this category was made accordingly.

It is not uncommon and possibly not unrealistic for a manufacturer to make the blithe assumption at this stage that the product price will be "within a competitive range" without having much idea of what that range is. For example, in developing a new type of camera equipment, one of the electrical companies judged its acceptability to professional photographers by technical performance without making any inquiry into its economic value. When the equipment was later placed in an economic setting, the indications were that sales would be negligible.

The second step is marking out this *competitive range of price*. Vicarious pricing experience can be secured by interviewing selected distributors who have enough comparative knowledge of customers' alternatives and preferences to judge what price range would make the new product "a good value." Direct discussions with representative experienced industrial users have produced reliable estimates of the "practical" range of prices. Manufacturers of electrical equipment often explore the economic as well as the technical feasibility of a new product by sending engineers with blueprints and models to see customers, such as technical and operating executives.

In guessing the price range of a radically new consumers' product of small unit value, the concept of barter equivalent can be a useful research guide.

For example, a manufacturer of paper specialties tested a dramatic new product in the following fashion: A wide variety of consumer products totally unlike the new product were purchased and spread out on a big table. Consumers selected the products they would swap for the new product. By finding out whether the product would trade evenly for a dish pan, a towel, or a hairpin, the executives got a rough idea of what range of prices might strike the typical consumer as reasonable in the light of the values received for his or her money in totally different kinds of expenditures.

But asking prospective consumers how much they think they would be willing to pay for a new product, even by such indirect or disguised methods, may often fail to give a reliable indication of the demand schedule. Most times people just do not know what they would pay. It depends partly on their income and on future alternatives. Early in the postwar period a manufacturer of television sets tried this method and got highly erratic and obviously unreliable results because the distortion of war shortages kept prospects from fully visualizing the multiple ways of spending their money.

Another deficiency, which may, however, be less serious than it appears, is that responses are biased by the consumer's confused notion that he or she is bargaining for a good price. Not until techniques of depth interviewing are more refined than they are now can this crude and direct method of exploring a new product's demand schedule hold much promise of being accurate.

One appliance manufacturer tried out new products on a sample of employees by selling to them at deep discounts, with the stipulation that they could if they wished return the products at the end of the experiment period and get a refund of their low purchase price. Demand for foreign orange juice was tested by placing it in several markets at three different prices, ranging around the price of fresh fruit; the result showed rather low price elasticity.

While inquiries of this sort are often much too short-run to give any real indication of consumer tastes, the relevant point here is that even such rough probing often yields broad impressions of price elasticity, particularly in relation to product variations such as styling, placing of controls, and use of automatic features. It may show, for example, that \$5 of cost put into streamlining or chromium stripping can add \$50 to the price.

The third step, a more definite inquiry into the *probable sales from several possible prices,* starts with an investigation of the prices of substitutes. Usually the buyer has a choice of existing ways of having the same service performed; an analysis of the costs of these choices serves as a guide in setting the price for a new way.

Comparisons are easy and significant for industrial customers who have a costing system to tell them the exact value, say, of a forklift truck in terms of warehouse labor saved. Indeed, chemical companies setting up a research project to displace an existing material often know from the start the top price that can be charged for the new substitute in terms of cost of the present material.

But in most cases the comparison is obfuscated by the presence of quality differences that may be important bases for price premiums. This is most true of household appliances, where the alternative is an unknown amount of labor of a mysterious value. In pricing a cargo parachute the choices are.

(1) Free fall in a padded box from a plane flown close to the ground.

(2) Landing the plane

(3) Back shipment by land from the next air terminal or

(4) Land shipment all the way.

These options differ widely in their service value and are not very useful pricing guides.

Thus it is particularly hard to know how much good will be done by making the new product cheaper than the old by various amounts, or how much the market will be restricted by making the new product more expensive. The answers usually come from experiment or research.

The fourth step in estimating demand is to consider the *possibility of retaliation by manufacturers of displaced substitutes* in the form of price cutting. This development may not occur at all if the new product displaces only a small market segment. If old industries do fight it out, however, their incremental costs provide a floor to the resulting price competition and should be brought into price plans.

For example, a manufacturer of black-and-white sensitized paper studied the possibility that lowering its price would displace blueprint paper substantially. Not only did the manufacturer investigate the prices of blueprint paper, but it also felt it necessary to estimate the out-of-pocket cost of making blueprint paper because of the probability that manufacturers already in the market would fight back by reducing prices toward the level of their incremental costs.

Decision on Market Targets

When the company has developed some idea of the range of demand and the range of prices that are feasible for the new product, it is in a position to make some basic strategic decisions on market targets and promotional plans. To decide on market objectives requires answers to several questions: What ultimate market share is wanted for the new product? How does it fit into the present product line? What about production methods? What are the possible distribution channels?

These are questions of joint costs in production and distribution, of plant expansion outlays, and of potential competition. If entry is easy, the company may not be eager to disrupt its present production and selling operations to capture and hold a large slice of the new market. But if the prospective profits shape up to a substantial new income source, it will be worthwhile to make the capital expenditures on plant needed to reap the full harvest.

A basic factor in answering all these questions is the expected behavior of production and distribution costs. The relevant data here are all the production outlays that will be made after the decision day—the capital expenditures as well as the variable costs. A go-ahead decision will hardly be made without some assurance that these costs can be recovered before the product becomes a football in the market. Many different projections of costs will be made, depending on the alternative scales of output, rate of market expansion, threats of potential competition, and measures to meet that competition that are under consideration. But these factors and the decision that is made on promotional strategy are interdependent. The fact is that this is a circular problem that in theory can only be solved by simultaneous equations.

Fortunately, it is possible to make some approximations that can break the circle: scale economies become significantly different only with broad changes in the size of plant and the type of production methods. This narrows the range of cost projections to workable proportions. The effects of using different distribution channels can be guessed fairly well without meshing the choices in with all the production and selling possibilities. The most vulnerable point of the circle is probably the decision on promotional strategy. The choices here are broad and produce a variety of results. The next step in the pricing process is therefore a plan for promotion.

Design of Promotional Strategy

Initial promotion outlays are an investment in the product that cannot be recovered until some kind of market has been established. The innovator shoulders the burden of creating a market—educating consumers to the existence and uses of the product. Later imitators will never have to do this job; so if the innovator does not want to be simply a benefactor to future competitors, he or she must make pricing plans to recover initial outlays before his or her pricing discretion evaporates.

The innovator's basic strategic problem is to find the right mixture of price and promotion to maximize long-run profits. He or she can choose a relatively high price in pioneering stages, together with extravagant advertising and dealer discounts, and plan to recover promotion costs early; or he or she can use low prices and lean margins from the very outset in order to discourage potential competition when the barriers of patents, distribution channels, or production techniques become inadequate. This question is discussed further later on.

Choice of Distribution Channels

Estimation of the costs of moving the new product through the channels of distribution to the final consumer must enter into the pricing procedure, since these costs govern the factory price that will result in a specified consumer price and since it is the consumer price that matters for volume. Distributive margins are partly pure promotional costs and partly physical distribution costs. Margins must at least cover the distributors' costs of warehousing, handling, and order taking. These costs are similar to factory production costs in being related to physical capacity and its utilization, i.e., fluctuations in production or sales volume.

Hence these set a floor to trade-channel discounts. But distributors usually also contribute promotional effort—in point-of-sale pushing, local advertising, and display—when it is made worth their while.

These pure promotional costs are more optional. Unlike physical handling costs they have no necessary functional relation to sales volume. An added layer of margin in trade discounts to produce this localized sales effort (with retail price fixed) is an optional way for manufacturers to spend their prospecting money in putting over a new product.

In establishing promotional costs, manufacturers must decide on the extent to which the selling effort will be delegated to members of the distribution chain. Indeed, some distribution channels, such as house-to-house selling and retail store selling supplemented by home demonstrators, represent a substantial delegation of the manufacturers' promotional efforts, and these usually involve much higher distribution-channel costs than do conventional methods.

Rich distributor margins are an appropriate use of promotion funds only when the producer thinks a high price plus promotion is a better expansion policy in the specialty than low price by itself. Thus there is an intimate interaction between the pricing of a new product and the costs and the problems of floating it down the distribution channels to the final consumer.

Policies for Pioneer Pricing

The strategic decision in pricing a new product is the choice between (1) a policy of high initial prices that skim the cream of demand and (2) a policy of low prices from the outset serving as an active agent for market penetration. Although the actual range of choice is much wider than this, a sharp dichotomy clarifies the issues for consideration.

Skimming Price

For products that represent a drastic departure from accepted ways of performing a service, a policy of relatively high prices coupled with heavy promotional expenditures in the early stages of market development (and lower prices at later stages) has proved successful for many products. There are several reasons for the success of this policy:

1. Demand is likely to be more inelastic with respect to price in the early stages than it is when the product is full grown. This is particularly true for consumers' goods. A novel product, such as the electric blanket when it first came out, was not accepted early on as a part of the expenditure pattern. Consumers remained ignorant about its value compared with the value of conventional alternatives. Moreover, at least in the early stages, the product had so few close rivals that cross-elasticity of demand was low.

Promotional elasticity is, on the other hand, quite high, particularly for products with high unit prices such as television sets. Since it is difficult for customers to value the service of the product in a way to price it intelligently, they are by default principally interested in how well it will work.

2. Launching a new product with a high price is an efficient device for breaking the market up into segments that differ in price elasticity of demand. The initial high price serves to skim the cream of the market that is relatively insensitive to price. Subsequent price reductions tap successively more elastic sectors of the market. This pricing strategy is exemplified by the systematic succession of editions of a book, starting with a very expensive limited personal edition and ending up with a much lower-priced paperback.

3. This policy is safer, or at least appears so. Facing an unknown elasticity of demand, a high initial price serves as a "refusal" price during the stage of exploration. It is difficult to predict how much costs can be reduced as the market expands and as the design of the product is improved by increasing production efficiency with new techniques. When an electrical company introduced a new lamp bulb at a comparatively high initial price, it made the announcement that the price would be reduced as the company found ways of cutting its costs.

4. Many companies are not in a position to finance the product flotation out of distant future revenues. High cash outlays in the early stages result from heavy costs of production and distributor organizing, in addition to the promotional investment in the pioneer product. High prices are a reasonable financing technique for shouldering these burdens in the light of the many uncertainties about the future.

Penetration Price

The alternative policy is to use low prices as the principal instrument for penetrating mass markets early. This policy is the reverse of the skimming policy in which the price is lowered only as short-run competition forces it.

The passive skimming policy has the virtue of safeguarding some profits at every stage of market penetration. But it prevents quick sales to the many buyers who are at the lower end of the income scale or the lower end of the preference scale and who therefore are unwilling to pay any substantial premium for product or reputation superiority. The active approach in probing possibilities for market expansion by early penetration pricing requires research, forecasting, and courage.

A decision to price for market expansion can be reached at various stages in a product's life cycle: before birth, at birth, in childhood, in adulthood, or in senescence. The chances for large-volume sales should at least be explored in the early stages of product development research, even before the pilot stage, perhaps with a more definitive exploration when the product goes into production and the price and distribution plans are decided upon. And the question of pricing to expand the market, if not answered earlier, will probably arise once more after the product has established an elite market.

Quite a few products have been rescued from premature senescence by being priced low enough to tap new markets. The reissues of important books as lower-priced paperbacks illustrate this point particularly well. These have produced not only commercial but intellectual renascence as well to many authors. The patterns of sales growth of a product that had reached stability in a high-price market have undergone sharp changes when it was suddenly priced low enough to tap new markets.

A contrasting illustration of passive policy is the pricing experience of the airlines. Although safety considerations and differences in equipment and service cloud the picture, it is pretty clear that the bargain-rate coach fares of scheduled airlines were adopted in reaction to the cut rates of nonscheduled airlines. This competitive response has apparently established a new pattern of traffic growth for the scheduled airlines.

An example of penetration pricing at the initial stage of the product's market life—again from the book field—occurred when Simon & Schuster adopted the policy of bringing out new titles in a low-priced, paper-bound edition simultaneously with the conventional higher-priced, cloth-bound edition.

What conditions warrant aggressive pricing for market penetration? This question cannot be answered categorically, but it may be helpful to generalize that the following conditions indicate the desirability of an early low-price policy:

- A high price-elasticity of demand in the short run, i.e., a high degree of responsiveness of sales to reductions in price.

- Substantial savings in production costs as the result of greater volume—not a necessary condition, however, since if elasticity of demand is high enough, pricing for market expansion may be profitable without realizing production economies.
- Product characteristics such that it will not seem bizarre when it is first fitted into the consumers' expenditure pattern.
- A strong threat of potential competition.

This threat of potential competition is a highly persuasive reason for penetration pricing. One of the major objectives of most low-pricing policies in the pioneering stages of market development is to raise entry barriers to prospective competitors. This is appropriate when entrants must make large-scale investments to reach minimum costs and they cannot slip into an established market by selling at substantial discounts.

In many industries, however, the important potential competitor is a large, multiple-product firm operating as well in other fields than that represented by the product in question. For a firm, the most important consideration for entry is not existing margins but the prospect of large and growing volume of sales. Present margins over costs are not the dominant consideration because such firms are normally confident that they can get their costs down as low as competitors' costs if the volume of production is large.

Therefor, when toral industry sales are not expected to amount to much, a high - margin policy can be follwed because entry is improbale in view of the expection of low volume and because it does not matter too much to potential competitors if the new product is introduced.

The fact remains that for products whose market potential appears big, a policy of stayout pricing from the outset makes much more sense. When a leading soap manufacturer developed an additive that whitened clothes and enhanced the brilliance of colors, the company chose to take its gains in a larger share of the market rather than in a temporary price premium. Such a decision was sound, since the company's competitors could be expected to match or better the product improvement fairly promptly. Under these circumstances, the price premium would have been short-lived, whereas the gains in market share were more likely to be retained.

Of course, any decision to start out with lower prices must take into account the fact that if the new product calls for capital recovery over a long period, the risk may be great that later entrants will be able to exploit new production techniques which can undercut the pioneer's original cost structure. In such cases, the low-price pattern should be adopted with a view to long-run rather than to short-run profits, with recognition that it usually takes time to attain the volume potentialities of the market.

It is sound to calculate profits in dollar terms rather than in percentage margins, and to think in terms of percentage return on the investment required to produce and sell the expanded volume rather than in terms of percentage markup. Profit calculation should also recognize the contributions that market-development pricing can make to the sale of other products and to the long-run future of the company. Often a decision to use development pricing will turn on these considerations of long-term impacts upon the firm's total operation strategy rather than on the profits directly attributable to the individual product.

An example of market-expansion pricing is found in the experience of a producer of asbestos shingles, which had a limited sale in the high-price house market. The company wanted to broaden the market in order to compete effectively with other roofing products for the inexpensive home. It tried to find the price of asphalt shingles that would make the annual cost per unit of roof over a period of years as low as the cheaper roofing that was currently commanding the mass market. Indications were that the price would have to be at least this low before volume sales would come.

Next, the company explored the relationship between production costs and volume, far beyond the range of its own volume experience. Variable costs and overhead costs were estimated separately, and the possibilities of a different organization of production were explored. Calculating in terms of anticipated dollars of profit rather than in terms of percentage margin, the company reduced the price of asbestos shingles and brought the annual cost down close to the cost of the cheapest asphalt roof. This reduction produced a greatly expanded volume and secured a substantial share of the mass market.

Pricing in Maturity

To determine what pricing policies are appropriate for later stages in the cycle of market and competitive maturity, the manufacturer must be able to tell when a product is approaching maturity. Some of the symptoms of degeneration of competitive status toward the commodity level are:

- ***Weakening in brand preference.*** This may be evidenced by a higher cross-elasticity of demand among leading products, the leading brand not being able to continue demanding as much price premium as initially without losing position.
- ***Narrowing physical variation among products as the best designs are developed and standardized.*** This has been dramatically demonstrated in automobiles and is still in process in television receivers.

- ***The entry in force of private-label competitors.*** This is exemplified by the mail-order houses' sale of own-label refrigerators and paint sprayers.
- ***Market saturation.*** The ratio of replacement sales to new equipment sales serves as an indicator of the competitive degeneration of durable goods, but in general it must be kept in mind that both market size and degree of saturation are hard to define (e.g., saturation of the radio market, which was initially thought to be one radio per home and later had to be expanded to one radio per room).
- ***The stabilization of production methods.*** A dramatic innovation that slashes costs (e.g., prefabricated houses) may disrupt what appears to be a well-stabilized oligopoly market.

The first step for the manufacturer whose specialty is about to slip into the commodity category is to reduce real prices promptly as soon as symptoms of deterioration appear. This step is essential if the manufacturer is to forestall the entry of private-label competitors. Examples of failure to make such a reduction are abundant.

By and large, private-label competition has speeded up the inevitable evolution of high specialities into commodities and has tended to force margins down by making price reductions more open and more universal than they would otherwise be. From one standpoint, the rapid growth of the private-label share in the market is a symptom of unwise pricing on the part of the national-brand sector of the industry.

This does not mean that manufacturers should declare open price war in the industry. When they move into mature competitive stages they enter oligopoly relationships where price slashing is peculiarly dangerous and unpopular. But, with active competition in prices precluded, competitive efforts may move in other directions, particularly toward product improvement and market segmentation.

Product improvement at this stage, where most of the important developments have been put into all brands, practically amounts to market segmentation. For it means adding refinements and quality extras that put the brand in the elite category, with an appeal only to the top-income brackets. This is a common tactic in food marketing, and in the tire industry it was the response of the General Tire Company to the competitive conditions of the 1930s.

As the product matures and as its distinctiveness narrows, a choice must sometimes be made by the company concerning the rung of the competitive price ladder it should occupy—roughly, the choice between a low and a not-so-low relative price.

A price at the low end of the array of the industry's real prices is usually associated with a product mixture showing a lean element of services and reputation (the product being physically similar to competitive brands, however) and a company having a lower gross margin than the other industry members (although not necessarily a lower net margin). The choice of such a low-price policy may be dictated by technical or market inferiorities of the product, or it may be adopted because the company has faith in the long-run price elasticity of demand and the ability of low prices to penetrate an important segment of the market not tapped by higher prices. The classic example is Henry Ford's pricing decision in the 1920s.

In Summary

In pricing products of perishable distinctiveness, a company must study the cycle of competitive degeneration in order to determine its major causes, its probable speed, and the chances of slowing it down. Pricing in the pioneering stage of the cycle involves difficult problems of projecting potential demand and of guessing the relation of price to sales.

The first step in this process is to explore consumer preferences and to establish the feasibility of the product, in order to get a rough idea of whether demand will warrant further exploration. The second step is to mark out a range of prices that will make the product economically attractive to buyers. The third step is to estimate the probable sales that will result from alternative prices.

If these initial explorations are encouraging, the next move is to make decisions on promotional strategy and distribution channels. The policy of relatively high prices in the pioneering stage has much to commend it, particularly when sales seem to be comparatively unresponsive to price but quite responsive to educational promotion.

On the other hand, the policy of relatively low prices in the pioneering stage, in anticipation of the cost savings resulting from an expanding market, has been strikingly successful under the right conditions. Low prices look to long-run rather than short-run profits and discourage potential competitors.

Pricing in the mature stages of a product's life cycle requires a technique for recognizing when a product is approaching maturity. Pricing problems in this stage border closely on those of oligopoly.

Retrospective Commentary

Twenty-five years have brought important changes and have taught us much, but the basics of pricing pioneer products are the same, only clearer. New product pricing, if the product is truly novel, is in essence monopoly pricing—modified only because the monopoly power of the new product is

(1) Restricted because buyers have alternatives,

(2) Ephemeral because it is subject to inevitable erosion as competitors equal or better it, and

(3) Controllable because actions of the seller can affect the amount and the durability of the new product's market power.

In pricing, the buyers' viewpoint should be controlling. For example, buyer's-rate-of-return pricing of new capital equipment looks at your price through the eyes of the customer. It recognizes that the upper limit is the price that will produce the minimum acceptable rate of return on the investment of a sufficiently large number of prospects. This return has a broad range for two reasons. First, the added profits obtainable from the use of your equipment will differ among customers and among applications for the same customer. Second, prospective customers also differ in the minimum rate of return that will induce them to invest in your product.

This capital-budgeting approach opens a new kind of demand analysis, which involves inquiry into: (1) the costs of buyers from displaceable alternative ways of doing the job, (2) the cost-saving and profit-producing capability of your equipment, and (3) the capital management policies of your customers, particularly their cost of capital and cutoff criteria.

Role of Cost

Cost should play a role in new product pricing quite different from that in traditional cost-plus pricing. To use cost wisely requires answers to some questions of theory: Whose cost? Which cost? What role?

As to whose cost, three persons are important: prospective buyers, existent and potential competitors, and the producer of the new product. For each of the three, cost should play a different role, and the concept of cost should differ accordingly.

The role of prospective *buyers'* costs is to forecast their response to alternative prices by determining what your product will do to the costs of your buyers. Rate-of-return pricing of capital goods illustrates this buyer's-cost approach, which is applicable in principle to all new products.

Cost is usually the crucial estimate in appraising *competitors'* capabilities. Two kinds of competitor costs need to be forecasted. The first is for products already in the marketplace. One purpose is to predict staying power; for this the cost concept is competitors' long-run incremental cost. Another purpose may be to guess the floor of retaliation pricing; for this we need competitors' short-run incremental cost.

The second kind is the cost of a competitive product that is unborn but that could eventually displace yours. Time-spotted prediction of the performance characteristics, the costs, and the probable prices of future new products is both essential and possible. Such a prediction is essential because it determines the economic life expectancy of your product and the shape of its competitiveness cycle.

This prediction is possible, first, because the pace of technical advance in product design is persistent and can usually be determined by statistical study of past progress. It is possible, second, because the rate at which competitors' cost will slide down the cost compression curve that results from cost-saving investments in manufacturing equipment, methods, and worker learning is usually a logarithmic function of cumulative output. Thus this rate can be ascertained and projected.

The *producer's* cost should play several different roles in pricing a new product, depending on the decision involved. The first decision concerns capital control. A new product must be priced before any significant investment is made in research and must be periodically repriced when more money is invested as its development progresses toward market. The concept of cost that is relevant for this decision is the predicted full cost, which should include imputed cost of capital on intangible investment over the whole life cycle of the new product. Its profitability and investment return are meaningless for any shorter period.

A second decision is "birth control." The commercialization decision calls for a similar concept of cost and discounted cash-flow investment analysis, but one that is confined to incremental investment beyond product birth.

Another role of cost is to establish a price floor that is also the threshold for selecting from candidate prices those that will maximize return on a new product investment at different stages of its life. The relevant concept here is future short-run incremental cost.

Segmentation Pricing

Particularly for new products, an important tactic is differential pricing for separated market segments. To enhance profits, we split the market into sectors that differ in price sensitivity, charging higher prices to those who are impervious and lower prices to the more sensitive souls.

One requisite is the ability to identify and seal off groups of prospects who differ in sensitivity of sales to price or differ in the effectiveness of competition (cross-elasticity of demand). Another is that leakage from the low price segment must be small and costs of segregation low enough to make it worthwhile.

One device is time segmentation: a skimming price strategy at the outset followed by penetration pricing as the product matures. Another device is price-shaped modification of a basic product to enhance traits for which one group of customers will pay dearly (e.g., reliability for the military).

A similar device is product-configuration differentials (notably extras: the roof of the Stanley Steamer was an extra when it was a new product). Another is afterlife pricing (e.g., repair parts, expendable components, and auxiliary services). Also, trade channel discounts commonly achieve profitable price discrimination (as with original equipment discounts).

Cost Compression Curve

Cost forecasting for pricing new products should be based on the cost compression curve, which relates real manufacturing cost per unit of value added to the cumulative quantity produced. This cost function (sometimes labeled “learning curve” or “experience curve”) is mainly the consequence of cost cutting investments (largely intangible) to discover and achieve internal substitutions, automation, worker learning, scale economies, and technological advances. Usually these move together as a logarithmic function of accumulated output.

Cost compression curve pricing of technically advanced products (for example, a microprocessor) epitomizes penetration pricing. It condenses the time span of the process of cutting prices *ahead* of forecasted cost savings in order to beat competitors to the bigger market and the resulting manufacturing economies that are opened up because of creative pricing.

This cost compression curve pricing strategy, which took two decades for the Model T’s life span, is condensed into a few months for the integrated circuit. But though the speed and the sources of saving are different, the principle is the same: a steep cost compression curve suggests penetration pricing of a new product. Such pricing is most attractive when the product superiority over rivals is small and ephemeral and when entry and expansion by competitors is easy and probable.

Impacts of Inflation

Continuous high-speed inflation has important impacts on new product pricing. It changes the goal. It renders obsolete accounted earnings per share as the corporation’s overriding goal—replacing it with maximization of the present worth (discounted at the corporation’s cost of capital) of the future stream of real purchasing power dividends (including a terminal dividend or capital gain). Real earnings in terms of cash-flow buying power alone determine the power to pay real dividends.

Inflation raises the buyers’ benchmark costs of the new products’ competitive alternatives. Thus it lifts the buyer benefits obtainable from the new products’ protected distinctiveness (for example, it saves more wage dollars).

It raises the seller’s required return on the investment to create and to launch the new product. Why? Because the cost of equity capital and of debt capital will be made higher to compensate for anticipated inflation. For the same reason, inflation raises the customer’s cutoff point of minimum acceptable return. It also intensifies the rivalry for scarce investment dollars among the seller's new product candidates. Hence it probably tends to increase stillbirths, but may lower subsequent infant mortality. For these reasons, perennial inflation will make an economic attack on the problem of pricing new products even more compelling.

Pricing of new products remains an art. But the experienced judgment required to price and re price the product over its life cycle to fit its changing competitive environment may be improved by considering seven pricing precepts suggested by this analysis.

1. Pricing a new product is an occasion for rethinking the overriding corporate goal. This goal should be to maximize the present worth, discounted at the corporation's cost of capital, of the future stream of real (purchasing-power) dividends, including a terminal dividend or capital gain. The Wall Street traditional objective— maximizing the size or the growth of book earnings per share—is an inferior master goal that is made obsolete by inflation.

2. The unit for making decisions and for measuring return on investment is the entire economic life of the new product. Reported annual profits on a new product have little economic significance. The pricing implications of the new product's changing competitive status as it passes through its life cycle from birth to obsolescence are intricate but compelling.

3. Pricing of a new product should begin long before its birth, and repricing should continue over its life cycle. Prospective prices coupled with forecasted costs should control the decision to invest in its development, the determination to launch it commercially, and the decision to kill it.

4. A new product should be viewed through the eyes of the buyer. Rate of return on customers' investment should be the main consideration in pricing a pioneering capital good: the buyers' savings (and added earnings), expressed as return on their investment in the new product, are the key to both estimating price sensitivity of demand and pricing profitably.

5. Costs can supply useful guidance in new product pricing, but not by the conventional wisdom of cost-plus pricing. Costs of three persons are pertinent: the buyer, the competitor, and the producer. The role of cost differs among the three, as does the concept of cost that is pertinent to that role: different costs for different decisions.

6. A strategy of price skimming can be distinguished from a strategy of penetration pricing. Skimming is appropriate at the outset for some pioneering products, particularly when followed by penetration pricing (for example, the price cascade of a new book). In contrast, a policy of penetration pricing from the outset, in anticipation of the cost compression curve for manufacturing costs, is usually best when this curve falls steeply and projectably, and is

buttressed by economies of scale and of advancing technology, and when demand is price sensitive and invasion is threatened.

7. Penetration and skimming pricing can be used at the same time in different sectors of the market. Creating opportunities to split the market into segments that differ in price sensitivity and in competitiveness, so as to simultaneously charge higher prices in insensitive segments and price low to elastic sectors, can produce extra profits and faster cost-compression for a new product. Devices are legion.

11.11 NOTES

11.12 SUMMARY

Price is the prime mover of the wheels of the economy namely, production, consumption, distribution and exchange. As price is a sacrifice of purchasing power, it affects the living standards of the society; it regulates business profits and, hence, allocates the resources for the optimum output and distribution. Thus, it acts as powerful agent of sustained economic development.

11.13 SELFASSESSMENT QUESTIONS

1. What is pricing? Explain the factors influence on pricing.

2. Describe different method of pricing.

3. Explain objectives of pricing.

4. Explain in detail about pricing strategies.

11.14 REFERENCES

1. Marketing Management- Philip Kotler

2. Marketing Strategies- James Colborn

3. Business Marketing-Karunakaran

UNIT - 12: INDUSTRIALSERVICES

Structure:

12.0 OBJECTIVES

After studying this unit, you will be able to;

- Explain importance of industrial services
- Evaluate the industrial strategies
- Describe buying skills in marketing
- Discuss live cases

12.1 INTRODUCTION OFSERVICE INDUSTRY

In an economy, some business organizations are involved in producing some goods and some of them involved in extending the service to the customer. The goods producing industries include those who involve in the production of agriculture, forestry, mining, construction, and manufacturing. The service offering companies include hotels, personal services, automobiles repair, entertainment zones, health care, legal services, social services, museums, consulting business etc. Services are more abstract and intangible when compared to the goods.

In the service sector there are various divisions which can be classified mainly into (a) Giving service to the consumers directly (b) Giving service to the business organizations.

Example: Telecom companies like BSNL, Airtel, Vodafone offer individual service to the customers and also give service to the corpoartes.

Service industry activities can be understood by its nature like physical, intellectual, aesthetic, and other experiential activities. Physical activities involve car repairs, saloons, facility management, gardening, hotels etc. Intellectual activities involve mental thinking and idea creation like schools, colleges, universities, training institutes, software etc.

In India, the services sector contributes a larger share to the country's GDP, received maximum foreign direct investment, important contribution to the exports and maximum provider of employment. Indian service sector grew at the rate of 8% annually and and has contributed to the 64% of GDP in the year 2015-2016.

Following are some of the major highlights of the Indian service sector performances:

From 2000 to 2016 India has attracted the FDI upt to the tune of US$ 50.79 billion which is 18% of the total share of FDI received in India. Following table reveals the annual growth rate and market size of some of the Indian service industries.

Indian Service Industry	Annual Growth	Market Size
Telecommunication	10.30%	US$ 103.9 billion by 2020
IT & ITeS	23.72%	US$ 146 billion in 2015
Aviation	Domestic passenger - 21.63%	Indian domestic air traffic is expected to cross 100 million passengers by FY2017
Banking	Total Lending & Deposits increased at a CAGR of 20.7% & 19.7%	Asset size will increase to US$ 28.5 trillion by FY25
Education & Training	Distance Education is expected to grow at a CAGR of 34% by 2018	US$ 100 billion in 2015-16
Financial Services	Life insurance industry 22.5%,	Total outstanding credit by commercial banks in 2015 stood at US$ 1.08 trillion, Insurance sector is expected to touch US$ 350-400 billion by 2020
Media & Entertainment	CAGR of 14.3%	US$ 33.7 billion by 2020
Health Care	CAGR of 22.9%	US$ 280 billion by 2020

12.2 INDUSTRIAL STRATEGIES FOR SERVICE INDUSTRIES

Service strategy is an action plan of the organization to plan, develop and implement the various services to the customers. Effective strategy helps the business organization to overcome the challenges in the business cycles, competition, disruptive technology and leadership issues.

Service strategy consists of the following key elements:

a) Creating more value to the customers

b) Developing assets which will offer key advantage while delivering the services

c) Various types of extending the services to the customers

d) Clearly identifying the areas in which the services are provided.

e) Arrangements for delivering the services

f) Management of finance

g) Range of services

h) Managing the demand for the services

i) Calculating Return on Investment

Assessing the Strategic Capabilities of the Organization

Service strategy experts should do the careful analysis of the current position of the organization by making a detailed study on company's distinctive services, profitable services and most different and effective service activities in the value chain.

The key factors which play a vital role in the strategic assessment are:

(1) Strengths and Weaknesses: Need to assess the areas in which we hold an advantage when compared to other players in the industry like number of products, facilities, service points, price, efficiency etc. Also stock should be taken about the areas in which we are weak than our competitors which enables us to bridge the gap.

(2) Business Strategy: The outlook, plan, systems, standards received from the strategy of the organization.

(3) Critical Success Factors: The way in which we will come to know about the successful delivery of the service to the customer in the crucial phases.

(4) Threats and Opportunities: Determining the possible areas in which the competitors outperform us and also doing the research and arriving at the key areas which will give us a lot of advantage in the market.

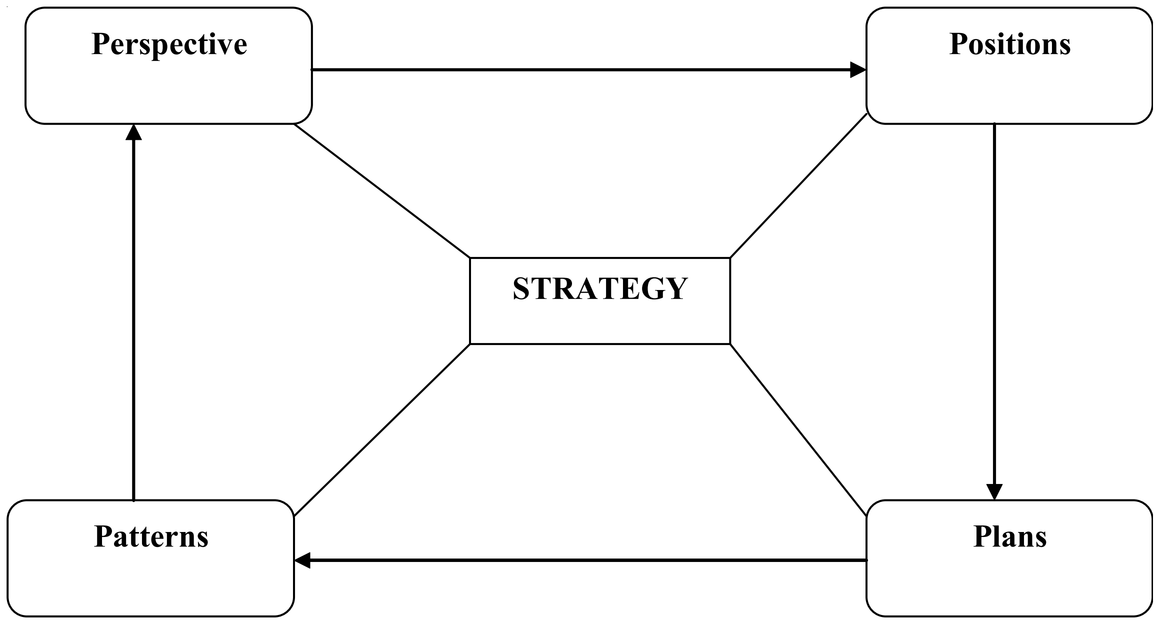
How to Create More Value for the Customers in the Service Industry:

Service oriented organizations offers more value for the customers in two ways by providing **Utility** and **Warranty.**

Utility is the perception of the customer about the service quality, its features, quality, cost and the service benefits which can meet their needs. **Warranty** represents the level of certainty about the service availability in a continuous manner to meet the demand in the market without violating any safety norms.

The Four Ps of Strategy

Below mentioned four Ps are the different forms of service strategies which are very basic to any service provider.



Perspective sets the vision and objectives of providing the service to the customers. Position explains the unique way in which an organization offers the service to its customers. The uniqueness in the service compared to the other players results in creating attractive value in the eyes of the customer. Uniqueness may be in offering world class premium service or low cost service, highly scarce or rare variety of service. Plan determines the exact blue print of the ways in which we achieve the uniqueness in offering the service. Pattern denotes the most fundamental way in which the organization does the things or offers service.

12.3 TYPES OF SERVICE STRATEGIES

Service organization functioning in any of the industry can adopt the different strategies in order to achieve the competitive edge over the others. Generally following are the different varieties of strategies:

(1) Growth Strategy: ensures the organization comes out with new services or enhancing the features to the existing services. **Example**: Hospitals have started extending their services to the homes by taking the blood samples from the patients and delivering the reports through mail or post to the door step. Also modern banking services have undergone a drastic change like online banking, mobile banking, self operated customer kiosks, 24/7 ATMs, extended banking hours etc. New and unique services and features results in more customers availing the service and hence increased revenue and profits.

(2) Service Differentiation Strategy: Many hospitals in Bangalore have started providing additional services to the foreign patients like visa approval, home stay, language assistance, local trip facility etc in addition to the core hospital services which differentiated with other hospitals. **Example:** New food startups in India like Zomato, Foodpanda, hangouts etc have come out with a unique food delivery service by organizing the home cooked from different houses and delivering to the customers. In a highly competitive market service differentiation helps the organization to build the brand image, loyal customers and revenue.

(3) Price-Skimming Strategy: includes charging higher prices for the unique services. When the organization charges higher prices for the service then the customer expectations will also be high. **Example:** When travel advisory websites like tripadvisor.com, makemytrip.com etc charge relatively higher prices for their tour packages which assures satisfaction, safety, highest comfort and time saving to the customers.

(4) Acquisition Strategy: The best strategy to grow after achieving the stability is to acquire the existing similar service providing companies. Acquisition enables getting more employees, customers, capacity to the organization. **Example:** Ola acquired Taxi for Sure in order to enhance its taxi feet size, customer size and take out one of the competitor in the market.

(5) Defending the Service Business from Competitors: In the market it is easy that many players will copy the content and form of service provided by the organization. Hence appropriate research and development should be done in order to create the enhanced demand with the economies of scale concept, adopting newer technology, and every tiny effort to build the reputation of the organization. **Example**: When private players were allowed in the Indian Insurance Industry, it was predicted that Life Insurance Corporation (LIC) will go down without having the necessary competencies to outperform the private players. But after so many years LIC is still managing to have the highest market share in India by providing the reliable, trusted and good settlement history of their policies.

(6) Automation: Traditionally services used to be only performed manually by human being which is outdated in the present context. There are various technological interventions which can enhance the customer satisfaction, increase the efficiency and build a quick, reliable service delivery image to the organization. **Example:** Automatic car washes, automated banking services, real time data transfer, NEFT payment, instant response systems, sensors have changed the perceptions of the customer and the organization in the way the service was delivered earlier and in the present day situation.

(7) Reducing the costs: One of the key question asked in the service organization is how to reduce the cost of giving the service? Well the answer lies in clear understanding of the nature of the service delivered. If the service is delivered using more people then we can reduce the cost of hiring the people by recruiting less qualified people. If qualified human beings are necessary because of their expertise skill and competencies then the option of outsourcing and hiring the consultants is one of the ways to reduce the cost of service delivery.

(8) Value Engineering: Services should be broken into various parts or components which should be clearly indicated the standard procedure for each of these various parts of a service. **Example:** Every time you walk into a MacDonald, in your mind you have the quality of the service provided. One important aspect is the quality of the service and also consistency in delivering this service time and again to the customers.

(9) Development of New Services: Organization should continuously strive to differentiate their services by offering more value enhanced delivery. Every time a new service or a new feature is introduced it should bring in innovative and more improved method of service experience to the valued customer. **Example**: Taxi Aggregator Ola after successful launch of its taxi booking service through its app across India moved to different class of services like Ola Prime, Ola Share, Ola Corporate, Ola Money, Ola Select, Ola Credit and Ola Shuttle to differentiate the services to the various customers.

12.4 NOTES

12.5 SUMMARY

The service industries (More formally termed: 'tertiary sector of industry' by economists) involve the provision of services to businesses as well as final consumers. Such, therefore, include accounting, tradesmanship (like mechanic or plumber services), computer services, restaurants, tourism, etc.

12.6 SELFASSESSMENT QUESTIONS

1. Describe industrial services with examples.

2. Explain the industrial strategies followed in the organization

12.7 REFERENCES

1. Marketing Management- Philip Kotler

2. Marketing Strategies- James Colborn

3. Business Marketing-Karunakaran

MODULE - IV
DISTRIBUTION CHENNEL FOR INDUSTRIAL GOODS

UNIT - 13 : DISTRIBUTION CHANNELS

Structure:

13.0 OBJECTIVES

After studying this unit, you will be able to;

- Define the distribution channels.
- Know the nature of industrial distribution channel.
- Explain the types of distribution system.
- Discuss the levels of Marketing Channels.
- Discuss the participants in business marketing channels

13.1 INTRODUCTION

When a company or a manufacturer produces goods or services, it has the immediate responsibility to distribute and sell them to the industrial and institutional customers. The industrial customers generally constitute of wholesalers, retailers, manufacturers, educational institutions, governments, hospitals, public utilities, and other formal organizations.

There are various intermediaries who are involved in a distribution and selling process helping the manufacturers to make their goods reach the end users. Thus, a network or channel that helps to flow the goods from the producer to the consumer through a set of interdependent organizations (intermediaries) is called distribution channel or trade channel or marketing channel. Channels are the tools used by management to move the goods from the place of production to the place of consumption. In the progression, the title of goods gets transferred from sellers to buyers.

Industrial distribution is unique as there are several different methods of channeling the products and services to industrial consumers. The type of product, the selling price of the product and technical knowledge required to sell the product all play a considerable role in selecting the proper sales or distribution channel.

Unlike consumer organizations, the decisions taken by the industrial organizations on distribution channels is of great significance as the decisions involved are of long-term nature that cannot be changed frequently. The industrial organizations carry on certain important functions till the products reach the consumers – like utilizing the services of transportation companies for distribution, the services of warehouses for safe storage of goods, inventory control, order processing and selection of marketing channels. This necessitate taking important decisions like devising effective communication tools, planning promotional activities, managing finances etc that help in serving the consumers better.

13.2 MEANING

A distribution channel is the chain of businesses or intermediaries through which a good or service passes until it reaches the end consumer. A distribution channel can include wholesalers, retailers, distributors and even the internet. Channels are broken into direct and indirect forms, with a "direct" channel allowing the consumer to buy the good from the manufacturer and an "indirect" channel allowing the consumer to buy the good from a wholesaler. Direct channels are considered "shorter" than "indirect" ones.

The path through which goods and services travel from the vendor to the consumer or payments for those products travel from the consumer to the vendor. A distribution channel can be as short as a direct transaction from the vendor to the consumer, or may include several interconnected intermediaries along the way such as wholesalers, distributors, agents and retailers. Each intermediary receives the item at one pricing point and movies it to the next higher pricing point until it reaches the final buyer. Coffee does not reach the consumer before first going through a channel involving the farmer, exporter, importer, distributor and the retailer.

13.3 NATURE OF INDUSTRIAL DISTRIBUTION CHANNEL

The nature of industrial distribution channel is quite different from the consumer goods distribution channel. The intermediaries stock the products they are distributing thereby assuming part of the burden of marketing the product and maintaining close contact with customers. There are various factors that affect the distribution of industrial goods.

Geographical Distribution

The industrial distributors are concentrated highly in the industrial markets they serve and certain other places that have large number of industries like large towns and cities.

Size

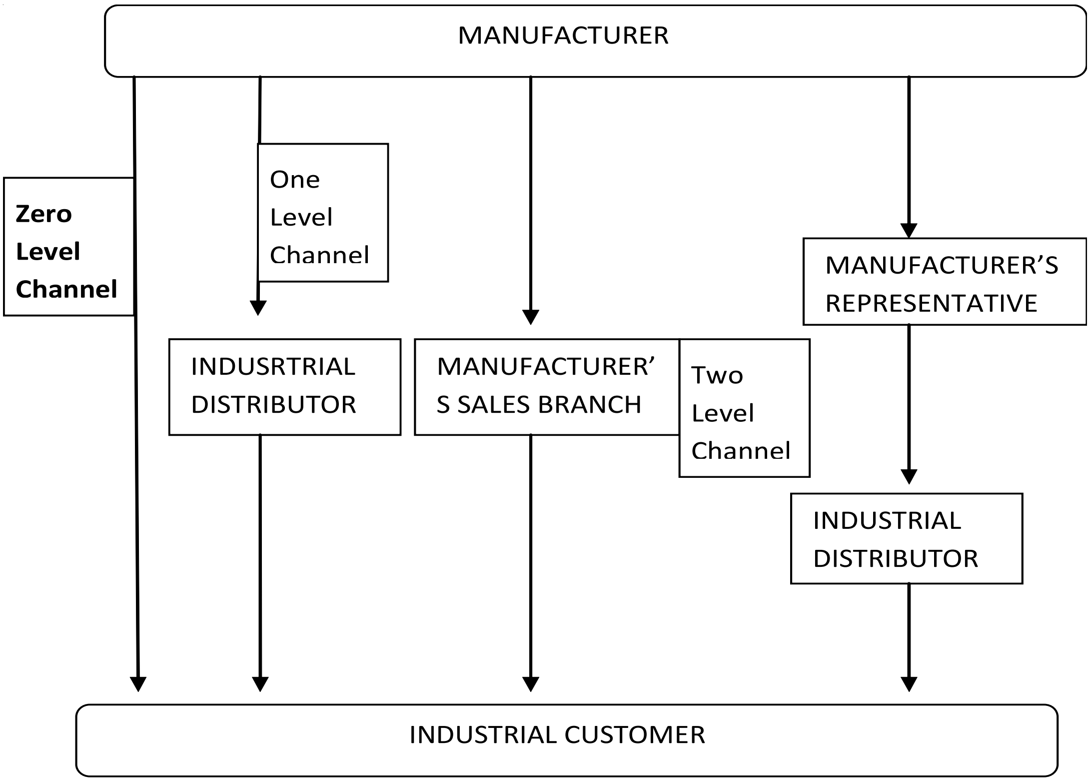
Unlike consumer markets, the industrial markets tend to have fewer channels of distribution. Even the industrial channel is shorter in size as organizational buyers expect immediate product availability, technical expertise and prompt after-sales service. This indirectly calls for investment in training and physical facilities for the industrial organizations.

Intermediary characters

The intermediaries involved in industrial marketing are technically qualified who maintain very close relationship with industrial organizations. Industrial manufacturers tend to depend more heavily on each member of the channel and may do more to support that channel member. Industrial distributors, brokers and agents are some types of intermediaries used by industrial marketers to reach customers.

Mixed channels

A combination of direct and indirect channels is used by some industrial marketers to cater to different market segments or when they have some resource constraints. To cater to large-volume customers, industrial firms generally use their own sales force, and to cover small scale organizations, they use independent distributors. In case of large geographical territories, due to resource constraints they use their agents called as 'manufacturers' representatives'.



Industrial Marketing Channel (with various levels)

Zero level – Manufacturer to Customer

One level – Single intermediary involved

Two level – Two intermediaries are involved in the channel network

The Structure of Industrial Channel

There are different ways in which an industrial channel can be structured. Some of the industrial channel structures are direct while some are indirect.

a. Direct Channel Structures

In direct channel structures, the entire task necessary to create sales and to deliver the products to industrial customers is performed by the manufacturers themselves. The various tasks involved in this process are contacting the potential customers, communicating and negotiating with them, financing and selling, storing the products, transportation and providing related services. This approach is viable to the company only if

- The buying process is lengthy,
- The selling includes extensive technical and commercial negotiations at various levels, including top management,
- The industrial buyer insists on buying directly from the manufacturer, and
- The value of each transaction is large.

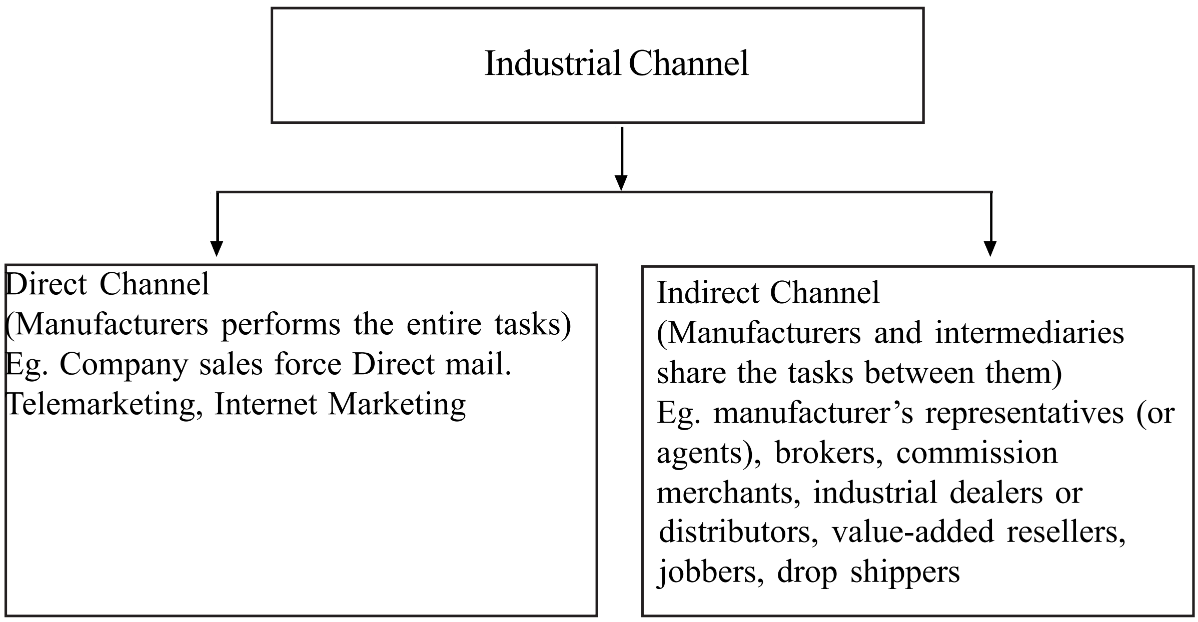
Some of the examples of direct channels are direct sales (through the company sales force) and direct marketing (through direct mail, telemarketing, Internet marketing)

b. Indirect Channel Structures

In indirect channel structures, the various tasks discussed above is shared both by the manufacturer and the intermediaries. An indirect distribution approach is appropriate when

- The industrial buyers are widely dispersed,
- The value of transaction or sales are low,
- The industrial buyers purchase many product items in one transaction, and
- The manufacturer has limited resources.

Some of the examples of indirect channel are manufacturer's representatives (or agents), brokers, commission merchants, industrial dealers or distributors, value-added resellers, jobbers, drop shippers. Indirect distribution is used in industrial chemicals, construction machinery, iron and steel products, etc.,

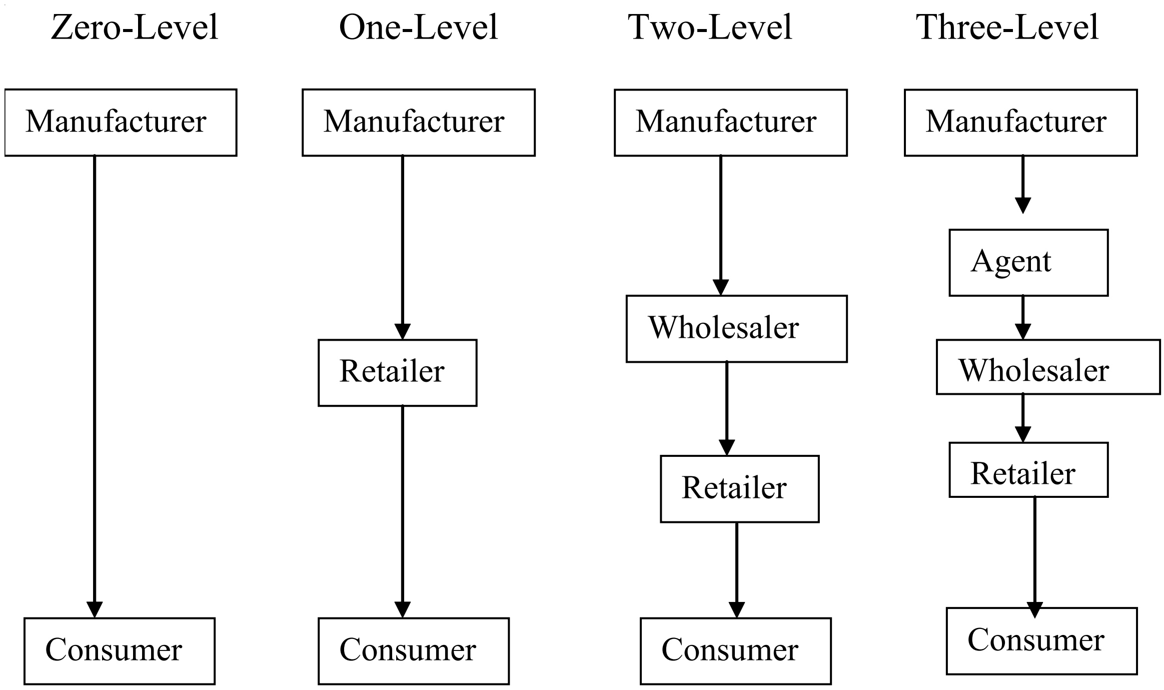


The Industrial Channel Structure

13.4 CHANNEL STRUCTURE

Channel structure is distinguished on the basis of the number of intermediaries. There are different levels in a channel structure. The common levels are zero-level, one-level, two-level, and three-level. Each level presents both opportunities and challenges for the marketer. Exhibit 1.5 gives a picture of the different levels

13.5 TYPICAL CHANNEL STRUCTURE FOR CONSUMER GOODS



Zero-level

Structure is one of the simplest forms of the channel structure. Here organizations like Avon, Eureka Forbes use direct selling mode to take the products from their production houses to the consumers directly. A lot of money has to be spent in order to make this channel structure effective, as there is no third party to take your product to the consumer. Even a bakery can come as a firm, which bakes cakes and sells it directly to the consumers. Marketers who use the mailing services, toll-free numbers are also using this service.

One-level

Structure is one in which we have one intermediary acting as a link between the manufacturer and the consumer. Here the retailers procure goods directly from the manufacturer and supply it to the consumers. Retailers like Viveks, Wal-Mart deal directly with the manufacturer. In some cases in order to retain profitable and reputed retailers the manufacturers act as wholesalers. One of the advantages for the intermediaries is the customization and the discounts they receive.

Two-level

Channel has two people interceding before the product reaches the consumer. Here there would be a wholesaler and a retailer who takes the efforts for a speedy delivery and this is one of the most commonly used structures for consumer goods. In the case of Metro, most of the small retail and Kirana stores buy all the merchandise from Metro and in urn sell them to the consumer. One of the advantages of the four-level structure is the benefit of using the wholesaler in the distribution of services.

Three-level

Channel happens predominantly when the firms plans to go global. When a manufacturer enters another country, it always holds well when he uses the help of agents to operate in that environment. The agents are people who know the legal procedures and who can negotiate with the host country in case of a problem. Most of the airline firms that operate in different countries take the help of agents to penetrate the market

13.6. DESIGNING DISTRIBUTION CHANNELS

Channel design refers to those decisions that involve in the development of new marketing channels or modifying the existent ones. The channel design decision can be broken down into six steps namely:

1. Recognizing the need for channel design decision
2. Setting and coordinating distribution objectives
3. Specify the distribution tasks
4. Develop alternative channel structures
5. Evaluate relevant variables
6. Choose the best channel structure

1. Recognizing the need for a channel design decision

First and foremost task for the organization is to recognize the need for a channel design. An organization would go in for a new channel design for the following reasons namely

- When a new product or product line is developed, mainly when the existing channels are not suitable for the new line
- When the existing product is targeted to a different target market. This is common when an organization is used to catering the B2B, plans to enter the consumer market
- When there is a change in the marketing mix elements, when an organization reduces its prices on certain offering the channel worked out will be based on the price points, they may look in for discounters

- When facing major environmental changes namely in economic or technological or in legal spheres.
- Finally when the organization opens up new geographic marketing areas

The list by no means is comprehensive, but gives a picture about some of the most common conditions when channel design decisions are worked out.

2. Setting and Coordinating Distribution Objectives

Once a need for a design is recognized the next task for the channel manager is to work out to develop the channel structure, either form the scratch or by modifying the existing one. It is necessary for the channel manager to carefully evaluate the firm's distribution objectives. In order for the distribution objectives to be effective and well coordinated the channel manager need to perform three tasks namely

- Become familiar with the objectives and strategies in other marketing mix areas and other relevant objectives and strategies of the firm. In most cases the person or the group that sets the objectives of the other marketing mix elements will also set the objectives for distribution as well.
- Set the objectives and state them explicitly. A good objective is one, which is clear, and explicit, and has a greater role in achieving the firm's overall objectives. Some examples of good distribution objectives are as follows.
- Apple Computers set a distribution objective to reach more consumers with what it refers to as the 'Apple experience'. So, Apple reinvigorated and reestablished relationships with large retail chains, which it had neglected in recent years.
- In the same way Coca-Cola seeks to broaden its penetration in schools and college markets, as a result of which it has entered into contact with many schools and colleges, whereby these institutions would sell only Coca-Cola products on their campuses.

3. Specifying the Distribution Tasks

Once the objectives are formulated, a number of functions need to be performed in order for the distribution objectives to be met. The manager therefore has to specify the nature of the tasks that needs to be carried out in order to meet the objectives. The tasks need to be precisely stated so that it meets the specified distribution objectives. For e.g. a manufacturer of a consumer product, say a high quality cricket bats aimed at serious amateur cricket players would need to specify distribution tasks such as gathering info on target markets shopping patterns, promote product availability to the target, maintain inventory, and timely availability, compile info about the product features, provide hands on experience using the product, process and fill customers orders, transport the product, arrange for credit provisions, provide warranty, provide repair and service, establish product return to make the offering readily available. Sometimes these functions may appear to be production oriented rather than distribution tasks, but when we talking about meeting customers, they are indeed distribution tasks.

4. Developing Possible Alternative Channel Structures

Once the tasks have been specified by the channel manager he should find out alternate ways of allocating these tasks. In most cases the channel manager chooses from more than one channel to reach the consumer effectively. Britannia would sell their biscuits thorough wholesale food distributor, departmental stores, convenience stores and even in pharmacies. Whatever may be the channel structure, the allocation alternatives should be in terms of (a) the number of levels in the channel (b) the intensity at various levels, and (c) the types of intermediaries?

The number of levels can be from two level up to five levels. The channel manager can think of going for a direct way of meeting the customers to using two intermediaries as an appropriate way. Intensity refers to the number of intermediaries at each level.

Generally the intensities can be classified into three categories namely intensive, selective and exclusive. Intensive saturation means as many outlets as possible are used at each level of the channel. Selective means that not all possible intermediaries at a particular level are used. Exclusive refers to a very selective pattern of distribution.

A firm like Parle may use intensive distribution channel structure, while Rolex may use high degree of selectivity. The types of intermediaries, third component has to be carefully dealt. The firms should not overlook new types of intermediaries that have emerged in recent years particularly the auction firms such as baazee, bid or buy as possible sales outlet for their products.

13.7 CASE STUDY

Master of the Online Supermall

Amazon.com could well go down in history as a love child born of the heady fling that the stock market had with dotcoms in the late 1990s. But the company, founded by Jeff Bezos in July 1995 when the internet was still an untested business medium, is a survivor-par-excellence. It floundered a bit in the swirl of the dotcom bust, but unlike thousands that were swept away, Amazon.com reinvented itself and emerged stronger.

The 40-year old Bezos, a computer science grad from Princeton University, is the pioneer of Internet Retailing. His compelling vision introduced a new paradigm for retail, the click-and-buy model; buy goods from a website instead of a physical store, from wherever there is an internet connection: home, office or cyber-café. A model that gave convenience to buyers, and mind-boggling market reach to sellers.

Named after the mighty Amazon river and its numerous tributaries that surge through dense rain forests, Amazon.com was started with an initial investment of a few thousand dollars. In less than three weeks after the website went live, Bezos and his wife Mackenzie were pulling in sales of over $20,000 a week. And soon after going public in 1997, the company had a market capitalization higher than that of its brick-and-mortar rivals. In 1999, Bezos was chosen as Time Magazine's 'Person of the Year'. But things changed soon after and the dotcom bust saw Amazon.com lose almost 90 percent of its market cap in 2000.

Bezos didn't give up on his vision. He set about transforming Amazon.com from a website selling books into something much bigger: the world's largest online retailing platform. A series of tie-ups with companies like Toys R Us and Target helped give the website the feel of an online supermall where a customer could buy almost anything.

Marketing initiatives followed – from free shipping to highly discounted prices to very customized offerings (based on customer profile) to wide distribution through sites which can divert traffic to Amazon.com for a small commission. But the biggest move was Bezos' decision to make the site 'more global'.

The moves have paid off. The company announced its first full year profit in 2003. It has been making money now for three straight quarters and revenues have exceeded a billion dollars for the last six quarters. If proof was needed that there is money to be made in online retailing, this is it. And Bezos has proved that the right idea, coupled with perseverance, pays in the end. (Excerpt from Business Today, May 2004)

Questions

1. How does Amazon.com bring utility or create value for its customers?

2. Explain the marketing framework of Amazon.com? 3. What do you learn about marketing from the Amazon story?

13.8 NOTES

13.9. SUMMARY

In all, the concept of industrial marketing may be referred as marketing of goods and services to business organizations: manufacturing companies, service organizations, institutions and middlemen in private and public sector organizations, and Government undertakings. The differences between industrial and consumer marketing exist in certain characteristics such as market, product, buyer behavior, channel, promotional, and price. The demand for industrial products is derived from the ultimate demand for consumer goods and services. It is, therefore, called as derived demand. Joint demand occurs when one industrial product is required, if other product also exists. Cross-elasticity of demand is the reaction of the sales of one product to a price change in another product.

13.10 KEY WORDS

Distribution channels, intermediaries, marketing channels

13.11 SELFASSESSMENT QUESTIONS

1. Explain the main differences between consumer and industrial marketing.
2. Illustrate with example why industrial demand is called derived demand.
3. Discuss the nature of industrial distribution channel?
4. Explain the industrial marketing channels with various levels?

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UNIT- 14 : CHANNELAND CHANNEL CONFLICT

Structure:

14.0 OBJECTIVES

After studying this unit, you will be able to;

- Expalin the participants in business market.
- Explain the market channel design.
- Highlight the functions of market channels.
- Discuss the causes for conflict and also how to manage the conflict.

14.1 INTRODUCTION

To develop an effective marketing plan, an industrial marketer needs to understand industrial markets. The industrial market is composed of commercial enterprises, governmental organizations, and institutions whose purchasing decisions vary with the type of industrial good or service under consideration. Effective marketing programs thus depend upon a understanding of how marketing strategy should differ with the type of organization being targeted and the products being sold. The industrial market is characterized by wonderful diversity both in customers served and products sold. Component parts, spare parts, accessory equipment, and services are example of the types of products purchased by the variety of customers in the industrial market. Industrial distributors or dealers who in turn sell to other industrial customers, commercial businesses, government, and institutions buy a variety of products that, in one way or another, are important to the functioning of their business endeavors. Knowing how this immense array of industrial customers‘purchase and use products and what criteria are important in their purchasing decision is an important aspect of industrial marketing strategy. For the purpose, industrial sellers understand the types of industrial buyers.

14.2 MEANING

Marketing Channels - Sets of interdependent organizations involved in the process of making a product or service available for use or consumption.

Distribution Channels -Distribution channels move products and services from businesses to consumers and to other businesses. Also known as marketing channels, channels of distribution consist of a set of interdependent organizations—such as wholesalers, retailers, and sales agents—involved in making a product or service available for use or consumption. Distribution channels are just one component of the overall concept of distribution networks, which are the real, tangible systems of interconnected sources and destinations through which products pass on their way to final consumers.

14.3 MULTIPLE CHANNELS OFDISTRIBUTION

For many products and services, their manufacturers or providers use multiple channels of distribution. A personal computer, for example, might be bought directly from the manufacturer, either over the telephone, direct mail, or the Internet, or through several kinds of retailers, including independent computer stores, franchised computer stores, and department stores. In addition, large and small businesses may make their purchases through other outlets.

Channel structures range from two to five levels. The simplest is a two-level structure in which goods and services move directly from the manufacturer or provider to the consumer. Two-level structures occur in some industries where consumers are able to order products directly from the manufacturer and the manufacturer fulfills those orders through its own physical distribution system.

In a three-level channel structure retailers serve as intermediaries between consumers and manufacturers. Retailers order products directly from the manufacturer, then sell those products directly to the consumer. A fourth level is added when manufacturers sell to wholesalers rather than to retailers. In a four-level structure, retailers order goods from wholesalers rather than manufacturers.

Finally, a manufacturer's agent can serve as an intermediary between the manufacturer and its wholesalers, creating a five-level channel structure consisting of the manufacturer, agent, wholesale, retail, and consumer levels. A five-level channel structure might also consist of the manufacturer, wholesale, jobber, retail, and consumer levels, whereby jobbers service smaller retailers not covered by the large wholesalers in the industry.

Why are they used?

- Because producers lack resources to carry out direct marketing.
- Because direct marketing is not feasible.
- Because rate of return on manufacturing increases rate of return on retailing.
- Because they reduce the amount of work that must be done.

14.4 CHANNEL FUNCTIONS & FLOWS

Info-Promotion-Negotiation-Ordering-Financing-Risk taking- Physical possession-Payment-Title

All of the functions have 3 things in common:

1. They use up scarce resources.

2. Can be performed better through specialization.

3. They are shift able among channel members.

14.4.1 Channel Levels

Each intermediary that performs work in bringing the product & its title closer is a channel level.

- Zero-channel level (direct-marketing channel) consists of a manufacturer selling directly to the final customer (i.e. door-to-door sales, mail order. Telemarketing, TV selling)
- One level channel contains one selling intermediary (i.e. retailer)
- Two level...(wholesalers, retailers)
- Three level...(wholesalers, jobbers, retailers)
- The longer the channel, the more difficult it is to exercise control.

14.5 CHANNELS DESIGN DECISIONS

Designing a channel system calls for analyzing customer needs, establishing channel objectives, & identifying & evaluating the major channel alternatives.

Analyzing Customers' desired service output levels Channels produce 5 service output levels:

1. **Lot size:** number of units that the marketing channel permits a typical customer to purchase on a purchase occasion

2. **Waiting time:** Average time that customers of that channel wait for receipt of the goods.

3. **Spatial convenience:** Degree to which the marketing channel makes it easy for customers to purchase the product.

4. **Product variety:** assortment breadth.

5. **Service backup:** add-on services provided by the channel (installation, repairs, credit).

14.5.1 Establishing the Channel Objectives & Constraints

The channel objectives should be stated in terms of targeted services output level. Under competitive conditions, channel institutions should arrange their functional tasks so as to minimize total channel costs with respect to tasks desired levels of service output.

Effective channel planning requires manufactures to determine which market segment to serve and the best channels to use in each case. Each producer develops its channel objectives in the face of constrains stemming from products, intermediaries, competitors, company policy, environment and the level of service output desired be target customers.

Product characteristics:- Perishable products require more direct marketing because of the dangers associated with delays and repeated handling. Bulky products require channels that minimize the shipping distance.

Custom-built machinery and specialized business forms are sold directly by company sales representatives because middlemen lack the requisite knowledge. Products requiring installation and/or maintenance services are usually sold and maintained by the company or exclusively branches dealers.

Competitive characteristics:- Channel design is influenced by the competitor's channels. The produces may want to compete in or near the same outlets carrying the competitor's products. In some other industries, producers may want to avoid the channels used by competitors.

- Channels objectives vary with product characteristics.
- Channel design must take into account the strengths & weaknesses of different types of intermediaries.
- Channel design is also influenced by the competitors' channels.
- Channel design must also adapt to the larger environment.
- Legal regulations & restrictions also affect channel design.

14.6 CHANNEL CONFLICT

In an effort to increase product sales, marketers are often attracted by the notion that sales can grow if the marketer expands distribution by adding additional resellers. Such decisions must be handled carefully, however, so that existing dealers do not feel threatened by the new distributors who they may feel are encroaching on their customers and siphoning potential business.

For marketers, channel strategy designed to expand product distribution may in fact do the opposite if existing members feel there is a conflict in the decisions made by the marketer. If existing members sense a conflict and feel the marketer is not sensitive to their needs they may choose to stop handling the marketer's products.

14.6.1. Types of Conflict & Competition

- **Vertical** channel conflict exists when there is conflict between different levels within the same channel.

- **Horizontal** channel conflict exists when there is conflict between members at the same level within the channel.
- **Multichannel** conflict exists when the manufacturer has established two or more channels that compete with each other in selling to the same market.

14.6.2. Causes of Channel Conflict

- Goal incompatibility
- Unclear roles & rights
- Differences in perception
- Intermediaries' great dependence on the manufacturer

14.7. MANAGING CHANNEL CONFLICT

- Some channel conflict can be constructive. It can lead to more dynamic adaptation to a changing environment. But too much is dysfunctional.
- Perhaps the most important mechanism is the adoption of super ordinate goals. Working closely together might help them eliminate or neutralize the threat.
- Exchange of persons between two or more channel levels is useful.
- Cooptation is an effort by one organization to win support of the leaders of another organization by including them in advisory councils, boards of directors, etc.
- Encouraging joint membership in & between trade associations.

14.8. THE ROLE OF MARKETING CHANNELS

Why would a producer delegate some of the selling job to intermediaries? Delegation means relinquishing some control over how and to whom the products are sold. Producers do gain several advantages by using intermediaries. Many producers lack the financial resources to carry out direct marketing. Producers who do establish their own channels can often earn a greater return by increasing investment in their main business. In some cases direct marketing simply is not feasible. Intermediaries normally achieve superior efficiency in making goods widely available and accessible to target markets. Through their contacts, experiences, specialisation, and scale of operations, intermediaries usually offer the firm more than it can achieve on its own

Channel Functions and Flows

A marketing channel performs the work of moving goods from producers to consumers. It overcomes the time, place, and possession gaps that separate goods and services from those who need and want them. Members of the marketing channel perform a number of key functions. Some functions constitute a forward flow of activity from the company to the customer. Other functions constitute a backward flow from customers to the company. Still others occur in both directions. A manufacturer selling a physical product and services might require three channels:

- A sales channel
- A delivery channel
- A service channel

The question is not whether various channel functions need to be performed but rather, who is to perform them. All channel functions have three things in common:

- They use up scarce resources
- They can often be performed better though specialization
- They can be shifted among channel members

TYPES OF INTERMEDIARIES

Marketing intermediaries are the individuals and the organizations that perform various functions to connect the producers with the end users. These middlemen are classified into three:

1. Merchant middlemen, who take title to the goods and services and resell them.

2. Agent middlemen, who do not take title to the goods and services but help in identifying potential customers and even help in negotiation.

3. Facilitators, to facilitate the flow of goods and services from the producer to the consumer, without taking a title to them. Eg. Transport companies

Merchant Middlemen

Merchant middlemen are those who take title to the goods and channelize the goods from previous step to the next step with a view to making profit. They buy and sell goods in their own risk and the price for their effort is profit. They act as an intermediaries between producers and consumers. These merchant middlemen are broadly classified into wholesalers and retailers.

Wholesalers:

Wholesaler is a trader who deals in large quantity. He purchases goods from the producers in bulk quantity and sell it to the retailers in small quantity. According to American Management Association, " wholesalers sells to retailers or other merchants and/or individual, institutional and commercial users but they do not sell in significant amounts to ultimate consumers."

Functions of wholesalers

1. Assembling and buying: It means bringing together stocks of different manufactures producing same line of goods, and making purchases in case of seasonal goods.
2. Warehousing: The warehousing function of the wholesalers relieves both the producers and the retailers from the problem of storage.
3. Transporting: In the process of assembling and warehousing, the wholesaler do undertake transportation of goods form producers to their warehouse and back to retailers
4. Financing: They grant credit on liberal terms to retailers and taking early delivery of stock from the manufacturers to reduce their financial burden.
5. Risk bearing: Wholesaler bear the risk of loss of change in price, deterioration of quality, pilferage, theft. Fire etc.
6. Grading, Packing and packaging: By grading they sort out the stocks in terms of different size, quality shape and so on.
7. Dispersing and selling: Dispersing the goods already stored with them to the retailers.
8. Market information: Finally providing the market information to the manufactures

Services of wholesalers:

A. Services to Manufacturers:

1. The wholesaler helps the manufacture to get the benefit of economies of large scale production.
2. Wholesalers helps the manufactures to save his time and trouble by collecting orders from large number of retailers on behalf of the manufactures.
3. The wholesaler provides market information to the manufactures which will helps him to make modifications in his product.
4. The wholesaler buys in large quantities and keeps the goods in his warehouses. This relieves the manufacturer the risk of storage and obsolescence.
5. The wholesales helps to maintain a steady prices for the product by buying the product when the prices are low and selling when the prices are high.

B. Services to Retailers:

1. He gives valuable advices to the retailers on his business related matters.

2. He helps the retailer to get the goods very easily and quickly.

3. He render financial assistance to the retailer by granting credit facilities.

4. The wholesalers bears the risk associated with storage and distribution of goods to a certain extend.

5. The wholesaler helps the retailers to keep price steady.

Retailers:

The term 'retail' implies sale for final consumption. A retailer is the last link between final user and the wholesaler or the manufacturer. According to Professor William Standton, "retailing includes all activities directly related to the sale of goods and services to the ultimate consumers for personal or non business use." In other words retailer is one whose business is to sell consumers a wide variety of goods which are assembled at his premises as per the needs of final consumers. In India, Most of the Indian retail outlets are owner managed and have few or no sales assistant. Most important issues of these outlets are those of inventory management and funds management.

14.9 FACTORS INFLUENCING CHOICE OF DISTRIBUTION CHANNEL:

It is very important to select a channel for the distribution of goods and services to the ultimate consumers in an effective way. The marketer has to select the most suitable channel. While selecting the channel of distribution, the marketer has to consider the following factors:

1. **Nature of Product** The selected channel must cope up perish ability of the product. If a commodity is perishable, the producer prefer to employs few middlemen. For durable and standardized goods, longer and diversified channel may be necessary. If the unit value is low , intensive distribution is suggested. If the product is highly technical, manufacture is forced to sell directly, if it is not highly technical, intensive distribution can be selected. Seasonal products are marketed through wholesalers.

2. **Nature of market** If the market is a consumer market, then retailer is essential. If it is an industrial market, we can avoid retailer. If consumers are widely scattered large number of middlemen are required. When consumers purchase frequently, more buyer seller contacts are needed and middlemen are suggested.

3. **Competitors' Channel:** The distribution channel used by the competitors will influence the channel selection. There is nothing wrong in copying the channel strategy of the competitor if it is a right one.

4. **The financial ability of channel members:** Before selecting the channel, the manufacture has to think about the financial soundness of the channel members. In most of the case financial assistance are required to the channel members in the form of liberal credit facilities and direct financing.

5. **The Company's financial position:** A company with a strong financial background can develop its own channel structure. Then there is no need to depend other channel intermediaries to market their product.

6. **Cost of Channel:** The cost of each channel may be estimated on the basis of unit sale. The best type of channel which gives a low unit cost of marketing may be selected.

7. **Economic factors:** The economic conditions prevailing in he country have bearing on channel selection decision. During the period of boom, it is better to depend channels directly. During the periods of deflation direct relation with the consumers are desirable.

8. **The legal restrictions:** Before giving the final shape to channels of distribution, we have to consider the existing legal provisions of the various Acts. For eg. MRTP Act prevent channel arrangements that tend to lessen competition, create monopoly and those are objectionable to the very public interest.

9. **Marketing policy of the company:** The marketing policy of the company have a greater and deeper bearing on the channel choice. The marketing policies relating to channels of distribution are advertising, sales promotion, delivery, after sale service and pricing. A company has a heavy budget on advertising and sales promotion, the channel selected is bound to be direct as it requires a few layers of people to push the product.

14.10. CASE STUDY

Keiretsu and Supply Chain Management (SCM)

Supply chain management (SCM) aims at managing supply and demand optimizing resources, reducing cost and providing efficient customer service. 'Keiretsu' is a Japanese word that refers to powerful business group. It depicts how businesses share each other's resources. Keiretsu is a relationship among suppliers, partners and customers who do business with each other. It is basically a vertically related group with sound manufacturing and a large network of suppliers and subcontractors.

Under the Keiretsu arrangement, major suppliers and subcontractors do business with only one of the producers. Keiretsu shares many of the goals of the SCM as the latter is based on the management of relationships both between corporate functions and across companies. SCM offers an opportunity for firms to enjoy many of the benefits of Keiretsu, such as stability and efficiency. In Japan, large companies act as the centre of Keiretsu.

In Japan, there are six main business groups: Mitsui, Mitsubishi, Sumitomo, Fuyo, Sanwa and Dai-Ichi Kangyo. Toyota is a member of Mitsui group and has such as extensive network of suppliers and subcontractors that it has become a core company of its own Keiretsu. This ensures that there is no overlap between similar companies. Major suppliers do business with only one of the producers.

A major Japanese manufacturer also uses a single source for its material requirement. This makes the supplier more responsive. As global competition continues to grow, firms need to re-examine their channel alternatives and assess which forms of channel relationships will fit best with their long term objectives.

14.11 NOTES.

14.12 SUMMARY

In this unit, we have learnt various channels of distribution, channel functions, diffrent leveels of channels, and channel design structure. We have also learnt how to establish the channels and the role of markenting channels. We also discuss types of conflict and competition, the causes of channel conflict and how to manage channel conflict.

14.13 KEY WORDS

Participants, channel design, channel conflict

14.14 SELFASSESSMENT QUESTIONS

1. Who are major participants in business marketing
2. Explain the marketing channel design process?
3. What are the causes for channel conflict?
4. How channel conflict can manage in an organization?
5. What are factors influencing for channel conflict?

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UNIT - 15 : CHANNELS OF DISTRIBUTION – FUNCTIONS

Structure:

15.0. OBJECTIVES

After studying this unit ,you will be able to;

- Define the distribution channels.
- Highlight the functions of channels of distribution.
- Know how to select a Marketing Channel members
- Explain the process of Channel Design Process.

15.1. INTRODUCTION

It is very important that a distribution channel is properly aligned to satisfy the needs of channel members and also for the success of any industrial marketing strategy. A good industrial channel creates the communication and physical supply linkages with existing and potential customers. Channel designing is a dynamic process that consists of either developing the new channels or modifying the existing ones.

15.2. MEANING

A channel of distribution may be referred to by other names, and terms vary from industry to industry. But whether channel, trade channel, or some other variant of the term is used, the functions performed remain the same. The term channel of distribution has its origins in the French word for canal, suggesting a path that goods take as they flow from producers to consumers. In this sense, a channel of distribution is defined by the organizations or individuals along the route from producer to consumer. Because the beginning and ending points of the route must be included, both producer and consumer are always members of a channel of distribution. However, there may be intermediate stops along the way. Several marketing institutions have developed to facilitate the flow of the physical product or the transfer of ownership (title) to the product from the producer to the consumer. Organizations that serve as marketing intermediaries (middlemen) specializing in distribution rather than production are external to the producing organization. When these intermediaries join with a manufacturer in a loose coalition aimed at exploiting joint opportunities, a channel of distribution is formed.

15.3. CHANNEL DESIGN PROCESS:

Designing an appropriate industrial channel and managing it is a tough and continuing task. A well designed channel structure helps to achieve the desired marketing objectives. A channel structure consists of types and number of middlemen, terms and conditions of channel members, number of channels. The various steps that are involved in channel design are given in the following figure.

Channel Design Process

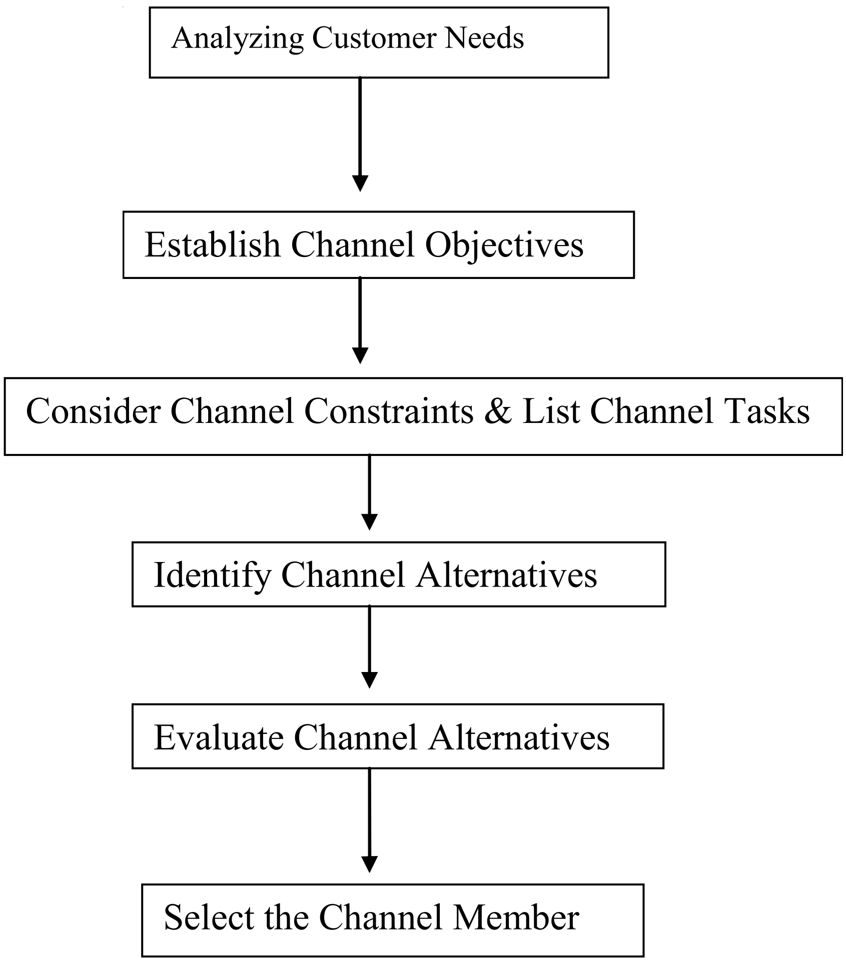

Fig: Steps involved in channel design process

Let us understand each of the stages of design process in detail:

a. Analyzing the needs of the customer:

When a marketer designs a marketing channel, he must understand the service output levels desired by the target customers. Different customers have different levels of service requirements. A high potential customer needs to be offered effective and professional service backup, ensured availability of varied products compared to the low potential customer. The marketing channel designer has to know at this stage itself that providing superior service output means increased channel costs and higher prices for customers.

b. Establishing channel objectives:

Channel objectives are a part of and result from the company's marketing objectives that need to be stated in terms of targeted service output levels. Profit considerations and asset utilization must be reflected in channel objectives and the resultant design. It should be the endeavour of the channel members to minimize the total channel costs and still provide with the desired level of service outputs. Channel objectives keep varying depending on the characteristics of the products. For example, while a customized non-standard product requires company sales force to sell directly, products like HVAC (Heating, Ventilation and Air-conditioning) are either sold by the company or its franchised dealers.

c. Considering channel constraints:

The industrial marketer develops his channel objectives keeping into consideration various constraints like the company, competition, the environment, product characteristics and the level of service output desired by the target customers.

Company: If a company has financial limitation as constraint, then it may restrict its direct distribution approach through company sales force to few high potential customers.

Competition: If a competitor has been very successful through direct service then it may force all other firms also to adopt the same strategy of direct selling.

Environment: Economic conditions, legal regulations are the environmental factors that affect channel design. During recession, producers use economical ways to sell the products to avoid additional costs. Similarly, the law looks down upon those channel arrangements that tries to build a monopoly market or minimize competition.

Product characteristics: As already mentioned, complex and non-standard products require direct distribution without any intermediaries. Eg. If an industrial marketer is providing customized machinery to his customer, then he deals directly with him rather than involving any intermediary to understand the customer needs better.

Customer: The industrial marketers depends on intermediaries to offer services to customers who are either giving less business or are located at far-off places.

d. Listing channel tasks:

The industrial marketers have to creatively structure the necessary tasks or functions to meet customer requirements and company goals. They have to first make a list of various tasks to be performed, identify the critical tasks, take objective and realistic decisions on which tasks can be effectively performed by the company and which cannot be performed due to certain constraints. For instance, a company manufacturing pump sets depend on distributors to sell them to customers who are located at distant locations but they would use their own sales force to serve those customers who are of high potential.

The careful analysis of customer needs, establishing objectives, considering constraints and listing the channel tasks form the backbone of channel design process. Once these aspects are delineated individually, the next step of identifying and evaluating channel alternatives starts.

e. Identifying channel alternatives:

There are four issues that are involved in identifying the channel alternatives. They are: the types of business intermediaries, the number of intermediaries, the number of channels and the terms and responsibilities of each channel members.

The types of business intermediaries: There are different types of intermediaries that the industrial marketers should identify. They have to consider various factors like the tasks to be performed, product and market conditions before selecting either manufacturer's representatives or agents, industrial distributors, brokers, commission merchants or value-added resellers. The marketers should search for innovative or combination of marketing channels.

Number of intermediaries: The manufacturers have to settle on the number of intermediaries they wish to use in their channel structure. They may either go for intensive, selective or exclusive distribution.

Intensive distribution: In this strategy, standard products that are purchased more frequently and have less unit value like raw materials and other convenience goods are distributed intensively i.e. products are stocked in numerous outlets so as to make them available to varied customers on demand.

Selective distribution: The industrial marketer selects few intermediaries to distribute the products to the target customer. This gives the marketer to develop a good working relation with the selected intermediaries, have better control, incur less costs and finally expect a better than average selling effort .Exclusive distribution: This strategy helps to enhance the product image and is more prevalent in consumer markets where some intermediaries exclusively deal and distribute the products of one manufacturer. They are not allowed to handle the competitor's products. The manufacturer expects aggressive selling by the intermediaries and tries to have control over their pricing policies, promotion strategy, credit terms and other services.

Number of channels: Industrial marketers need to serve various market segments. This necessitates them to use more than one channel for distributing and marketing their products. This multi-channel approach helps them not only to increase their market share but also reduce their costs. However, the industrial marketers need to take care of possible channel conflicts like proper demarcation of territory to channel members to sell and serve the customers in their respective areas.

Terms and r esponsibilities of Channel Members: There are various terms and conditions which the industrial marketer must make clear to the participating channel members like the responsibilities and tasks, conditions of sale and territorial rights that would enable both of them to enhance their performance.

Responsibilities and tasks: In order to avoid any future disagreements, there should be clarity in the roles of both the industrial marketers and the channel partners. Each should comply with the commitments about their individual responsibilities and tasks to be performed.

Conditions of sale: It should be clearly mentioned well in advance about the discounts offered by the manufacturers to the distributors, the commission to be paid to the agents or brokers. Other terms relating to warranty period, replacement of defective parts also should be appropriately stated.

Territorial rights: The territory between the distributors should be well demarcated so as to avoid any future confusion that may lead to legal issues.

f. Evaluating alternate channels:

There are several channel alternatives available to the industrial markets. They have to determine the best among the alternatives by evaluating them based on the following criteria:

- ♦ The economic performance of the channel.
- ♦ The degree of control exercised on them.
- ♦ The degree of adaptability of channels to the market situations.

Economic Performance:-

Different channel alternatives generate different levels of sales and incur different levels of costs. An industrial marketer has to pose a question whether sales generation would be more by direct selling through company sales force or through the channel members. Many of the industrial marketers believe that sales will be more from company sales force as they exclusively concentrate on company's product, they are given proper training to sell the product, they show more aggressiveness as their career depends on company's success and finally customers prefer to deal with the company directly. But it may also happen that the intermediary can sell more than the company sales force. The possible reasons for this could be the agency having many sales people with it or its sales force are much motivated with the commission offered by the company or the customers prefer to deal with agents who have extensive contacts.

The marketing manager has to similarly estimate the total costs of selling through different channel members. As shown in the given figure the Selling Cost of having channel members is lower than setting up a company's sales force. But as channel member keeps getting more commission with increased sales, its cost to company keeps rising. There is one level of sales (L B) where the total selling costs for both are same. This level is called as the break even level. The channel member is the most preferred and appropriate choice if the sales volume is below L B as it involves lower selling costs. Otherwise, the company should have its own sales force if sales level crosses L B to reduce the selling costs.

15.4. CHANNEL MANAGEMENT DECISIONS:

After a company completes the task of choosing a channel alternative, it has to start the process of selecting the intermediaries, motivate them, control any channel conflicts and evaluate the performance of channel members.

Selecting the Intermediaries:

Selecting the intermediaries is not part of channel design as some intermediaries leave the channel while others are terminated by the manufacturer. Selecting the best intermediary is a continuous process that is sometimes a more difficult task as producers have to work hard to get qualified middlemen. It involves finding out the distinct characteristics possessed by the intermediaries. Such evaluation is generally based on the experience possessed by the intermediaries, their number of years in the line of business, exposure in other fields, their past history, growth and profit records, their reputation, future growth potential, type of clientele possessed, etc., Thus, a channel that effectively satisfies the needs of a customer better than the competitors should find a place in the manufacturer's priority list.

Motivating the Channel Members:

After selecting the middlemen, the industrial marketer needs to continuously motivate them to do their job better to achieve long-term success. Though the terms and conditions that made them join the channel is a motivating factor, it must be further supplemented by training and encouragement. Understanding the needs and wants of the middlemen is the first step of motivation process. Depending on the motivational technique used by the manufacturer, there would be varying levels of support from the middlemen. Manufacturers generally try to maintain relationship with their distributors by motivating through cooperation, partnership, discounts/commission, and distributor councils.

Cooperation: Most of the manufacturers use the carrot and stick approach to gain cooperation from middlemen. Positive motivators like higher margins, special prices, allowances etc, along with threats like reduction in margins, slow delivery, terminating the contracts etc, are used to increase business. The manufacturer has to do a SWOT analysis of the distributors before implementing this approach.

Partnership: Manufacturers enter into an agreement or partnership with their intermediaries that list the objectives, policies and terms of jobs to be performed by both the parties in order to avoid any future conflicts. A good example of partnership is Vendor Managed Inventory System (VMI) where effective communication happens between the vendor and channel members through the assistance of electronic data interchange (EDI). The EDI helps the company to fill up the stock automatically at the channel member once it reaches the minimum reorder level. All relevant invoices, acknowledgements are electronically processed and sent to the distributors. The system also helps to check the slow moving products at the distributor‘s end, generates a purchase return order based on which the products are returned back to the company. This digital revolution helped in reducing costs and improving customer service both by the manufacturer and distributor thus nurturing their partnership.

Offering discounts/commissions: Another motivating factor for intermediaries is the offering of discounts/commissions by the manufacturers. The compensation is offered taking into account the expenses incurred and the services provided by the intermediaries.

15.5. FUNCTIONS OF CHANNELS OF DISTRIBUTION:

Perhaps the most neglected, most misunderstood, and most maligned segment of the economy is the distribution segment. Retailers are seen by some as the principal cause of high consumer prices, simply because retailers are the marketers with whom consumers most frequently come into contact. Retailers collect money from consumers, so even though much of that money is passed to other distributors or manufacturers, retailers often bear the brunt of customer’s complaints. Wholesalers are also seen as causing high prices, perhaps because much of what they do is done outside the view of consumers. In either case, many suggest “cutting out the middleman” as a means of lowering the prices of consumer goods. For thousands of years, the activities of those who perform the distribution function have been misunderstood, and this viewpoint persists today.

Students of marketing should understand that an efficient distribution system must somehow be financed. Most of the time, .eliminating the middleman. will not reduce prices, because the dollars that go to intermediaries to compensate them for the performance of tasks that must be accomplished regardless of whether or not an intermediary is present. In other words, a company can eliminate intermediaries, but it cannot eliminate the functions they perform.

15.5.1 How Intermediaries Fit into Distribution Channels

In the previous section we outlined a conventional channel of distribution consisting of a manufacturer, a wholesaler, a retailer, and the ultimate consumer. Not all channels include all of these marketing institutions. In some cases, a unit of product may pass directly from manufacturer to consumer. In others it may be handled by not just one but two or more wholesalers. To show why these many variations exist, we will examine the role of intermediaries in marketing channels.

Consider this conventional channel of distribution:

Manufacturer → Retailer → Ultimate Consumer

It is possible, as shown here, to have a channel of distribution that does not include a separate wholesaler. A manufacturer can choose to sell directly to retailers, in effect eliminating the wholesaler. However, the marketing functions performed by the wholesaler must then be shifted to one of the other parties in the channel. The retailer or the manufacturer. For instance, with the wholesaler out of the picture, the manufacturer may have to create a sales force to call on the numerous retailers. If the manufacturer assumes some or all of the marketing functions, they are said to have been shifted back ward in the channel. If the retailer assumes them, they are said to have been shifted forward in the channel. For example, the manufacturer may decide to perform the function of breaking bulk by sending comparatively small orders to individual retail customers. On the other hand, the retailer may be willing to accept truckload lots of a product, store large quantities of it, and perform the activity of breaking down these larger quantities into smaller quantities.

In any case, the functions performed by the eliminated wholesaler do not disappear; they are simply shifted to another channel member. The channel member that assumes these functions expects to be compensated in some way. The retailer may expect lower prices and higher margins for the extra work performed. The manufacturer may expect larger purchase orders, more aggressive retail promotion, or more control over the distribution process.

The key to setting the structure of a channel of distribution is to determine how the necessary marketing functions can be carried out most efficiently and effectively. Certain variables, such as price, the complexity of the product, and the number of customers to be served, can serve as guides to the appropriate channel structure. However, the functions to be performed should be the primary consideration in marketing managers

Distribution plans. Let us consider some of the major functions performed by intermediaries: physical distribution, communication, and facilitating functions.

15.5.2 Physical Distribution Functions

Physical distribution functions include breaking bulk, accumulating bulk, creating assortments, reducing transactions, and transporting and storing.

Bulk-breaking function: An activity, performed by marketing intermediaries, consisting of buying products in relatively large quantities and selling in smaller quantities.

Breaking Bulk. With few exceptions, intermediaries perform a bulk-breaking function. The bulk-breaking function consists of buying in relatively large quantities, such as truckloads, and then selling in smaller quantities, passing the lesser amounts of merchandise on to retailers, organizational buyers, wholesalers, and other customers. By accumulating large quantities of goods and then breaking them into smaller amounts suitable for many buyers, intermediaries can reduce the cost of distribution for both manufacturers and consumers. Consumers, do not buy and store great amounts of merchandise, which would increase their storage costs and the risks of spoilage, fire and theft. Manufacturers are spare the necessity of dividing their outputs into the small order sizes retailers or consumers might prefer. Bulk breaking is sometimes termed .resolution of economic discrepancies,. because manufacturers, as a rule, turn out amounts of merchandise that are vast compared with the quantity that an individual buyer might be able to purchase. Breaking bulk resolves this discrepancy.

Bulk-accumulating function : An activity, performed by marketing intermediaries, consisting of buying small quantities of a particular product from many small producers and then selling the assembled larger quantities.

Assembler : A marketing intermediary that performs a bulk-accumulating function.

Accumulating Bulk. In the majority of cases, it is the task of the intermediary to break bulk. However, an intermediary may also create bulk, buying units of the same product from many small producers and offering the larger amount to those who prefer to purchase in large quantities. These intermediaries are performing bulk-accumulating function. An intermediary performing this function is called surprisingly, an assembler. The classic examples of assemblers are in agriculture and fishing businesses. A maker of tomato sauce, such as Maggie, would probably not want to have to deal with many small farms. Assemblers gather large quantities of apples or tuna or other products attractive to large buyers.

Sorting function : An activity, performed by marketing intermediaries, consisting of classifying accumulated products as to grade and size, and then grouping them accordingly.

After accumulating bulk, marketers of agricultural products and raw materials typically perform a **sorting function**, which involves identifying differences in quality and breaking down the product into grade or size categories. For example, eggs are sorted into jumbo grade AA, large grade AA, and so on.

Assorting function: An activity, performed by marketing intermediaries, consisting of combining products purchased from several manufacturers to create assortments.

Creating Assortments: Another function that intermediaries perform is the creation of assortments of merchandise that would otherwise not be available. This **assorting function** resolves the economic discrepancy resulting from the factory operator's natural inclination to produce a large quantity of a single product or a line of similar products and the consumer's desire to select from a wide variety of choices. Wholesalers that purchase many different products from different manufacturers can offer retailers a greater assortment of items than an individual manufacturer is able to provide.

Consider how magazine publishers and retailers use intermediaries to solve a very big assorting problem. There are hundreds of magazine titles available from Indian publishers. No newsstand operator or other retailer carries anything like that number; a series of intermediaries is used to sort these many titles into appropriate groupings for individual stores. National wholesalers, move the hundreds of titles to hundreds of local wholesalers. Their reward for fulfilling this huge task is about 6 percent of the magazines' retail prices, out of which they must pay all expenses involved. The local distributors continue the task of breaking bulk, moving the magazines to countless supermarkets, new stands, and other retail spots. But there is more to the local wholesaler's task than simply breaking bulk and making delivery. The local wholesaler must select, from among the hundreds of available titles the ones that are appropriate for the individual

retailers. operations. Then, this assortment of titles must be assembled in the proper numbers for each retailer. The local wholesaler is paid about 20 percent of the cover prices. Complicated as this sounds, the system is so efficient that, less than 36 hours after a new Business Today is printed, it has arrived at all the retail establishments that carry the business magazine. Although the influence of wholesalers has declined in certain industries, it is obvious why wholesalers remain very important in the magazine distribution business.

Reducing Transactions. There is one underlying reason why intermediaries can economically accumulate bulk and create assortments. The presence of intermediaries in the distribution system actually reduces the number of transactions necessary to accomplish the exchanges that keep the economy moving and consumers satisfied.

15.5.3 Communication and Transaction Functions

Intermediaries perform a communication function, which includes buying, selling, and other activities involving gathering or disseminating information. The ultimate purpose of the communication link between the manufacturer and the retailer or between the wholesaler and the retailer is to transfer ownership. That is, to complete a transaction that results in an exchange of title.

Selling function: Activities, performed by intermediaries, that are associated with communicating

ideas and making a sale and thus effecting the transfer of ownership of a product.

Buying function: Activities, performed by intermediaries, that are associated with making a purchase and thus effecting the transfer of ownership of a product.

Wholesalers and retailers may perform an important promotional function for manufacturers when they provide product information and price quotes. Most frequently, this communication is carried out by a sales force. However, intermediaries also use advertising and such sales promotion tools as retail displays. In other words, intermediaries perform a selling function for the manufacturer, often providing a sales force or other promotional efforts that they can supply more efficiently than the manufacturer can. The wholesaler provides a buying function for retailers, organizational users, and other customers. A wholesaler's contact with numerous manufacturers allows it to evaluate the quality of a wide assortment of goods from competing manufacturers. Thus, retailers and other customers are freed of the burden of evaluating every manufacturer's product assortments. This allows them more time to specialize in the retailing and merchandising of products.

diaries further serve as channels of communication by informing buyers how products are to be sold, used, repaired, or guaranteed. They can even explain new product developments. (In fact, retailers should pass along more of this information to their customers: unfortunately many retail salespeople are not trained to provide information of this sort). Because intermediaries typically deal with a number of manufacturers or other suppliers of goods, they are in a unique position to serve as conduits of information.

Intermediaries, being "in the middle", are well placed not only to pass information from producers to other channel members but also to collect information from channel members or retail shoppers and return it to producers. For example, suppose a retailer receives serious consumer complaints about a product or some product-related matter such as repair service. The retailer should pass this information backward in the channel to the wholesaler, who can bring the matter to the attention of the producer. Should is the key word here. Too often, whether because of apathy or the fear of somehow being blamed for a problem, intermediaries fail to perform this potentially valuable service. Marketers at all levels should encourage communication throughout channels of distribution, because the satisfaction of all channel members and consumers is at stake.

15.5.4 Facilitating Functions

The transportation and storage functions of channel intermediaries are their most obvious contributions to the operation of the marketing system. However, intermediaries perform additional, so-called facilitating functions, which are not quite so apparent to observers of a channel in operation. Because the tasks of a channel intermediary can be so varied, it is nearly impossible to list all the facilitating functions a channel member might perform. However, three major categories of facilitating functions should be mentioned specifically: providing extra services, offering credit, and taking risks.

Service function: Activities, performed by intermediaries that increase the efficiency and effectiveness of the exchange process. Repair services and management services provided by intermediaries are examples.

Extra Services. Channel member, particularly intermediaries, can and do provide a range of extra services that increase the efficiency and effectiveness of the channel; intermediaries thus perform a **service function**. For many products, the availability of a post-sale repair service is an absolute necessity. Office photocopiers, for examples, always seem to need either routine maintenance or minor or major overhauls.

Wholesalers and retailers of such machines usually offer repair services on either a contract or an emergency basis. They also carry necessary supplies like paper. Other products. such as personal computers and cellular phones are not so prone to breakdowns, yet buyers like to know that repair service is available should it ever be needed. Technical support is critical for many Internet and software companies.

Honouring manufacturers guarantees can be another responsibility of intermediaries. Channel intermediaries can also provide a variety of management services. In the food industry, for example, wholesalers offer such services as computerized accounting systems, inventory planning, store site selection, store layout planning and management training programs. The extra services offered are good business for the wholesalers in that (1) they attract customers and (2) they help their food retailer customers to stay in business and to remain successful. The services, if not offered by every competing wholesaler, can also provide a competitive advantage to the food wholesaler willing to invest in them. Wholesalers may offer other services, too. They may provide help in preparing advertisements, and they may offer a line of private brand goods or a

wholesaler-owned label that smaller retailers can use to create an image similar to those of larger chains.

Credit function : Provision of credit to another member of a distribution channel.

Credit Services : Most intermediaries perform a credit function by offering credit service of one kind or another. Although some wholesalers and retailers operate exclusively on a cash-and-carry basis, promising to pass related savings on to the customers, they make up a relatively small proportion of the millions of intermediaries operating in India.

Some credit services provided by channel members may not be immediately obvious. A retailer that accepts Master Card or Visa provides a credit service that in fact, costs the retailer a percent of the sales fee, which it must pay to the credit card company. Many small/ medium retailers offer their own credit plans, which involve a more clear-cut provision of service than accepting outside card.

Wholesalers and other non-retailer channel members may provide credit in a number of ways. Although a supplier may have a credit system so unique that buyer pay particular notice, supplier credit systems are generally so widespread throughout a trade that buyers scarcely see the credit system as a true service Intermediaries in many fields routinely offer 30, 60 or more days to pay for merchandise ordered. Often, the days do not start .counting. until the goods are delivered to the buyer's place of business. In effect, such a service permits the buyer to make some money on a product before having to pay for it.

Risk-taking function : Assumption of the responsibility for losses when the future is uncertain.

Risk Taking. In almost everything they do, channel intermediaries perform a risk-taking **function.** When purchasing a product from a manufacturer or supplier of any type, intermediaries run the risk of getting stuck with an item that has fallen out of favour with the buying public because of a shift in fashion or the death of a fad. It is also possible for a product to spoil while it is in storage or lost through fire or some other disaster. Intermediaries bear these risks in addition to market risk.

MARKETING FUNCTION	PERFORMED FOR SUPPLIERS	PERFORMED FO R CUSTOMERS
Physical distribution functions	Breaking bulk Accumulating bulk Creating assortments Transportation Storage	Sorting products into desired quantities Assorting items into desired variety
Communication functions	Promotion, especially selling and communication of product information, gathering customer information	Delivery(transportation), storage, Buying based on interpretation of customer needs, Dissemination of information
Facilitating functions	Financing customer purchases Providing management services Taking risks	Credit financing Repair services Technical support

15.6. CASE STUDY

NCR, IBM and other manufacturers of office machines make a substantial proportion of their sales directly to their industrial users. At the same time, wholesalers of office equipments are thriving. Are these two market segments different or there exists some operational disadvantages that has led to this strategy? Explain.

15.7. NOTES

15.8. SUMMARY

Channel designing is resorted to by the industrial marketer when he has to develop either a new channel system or modify an existing one. As channel design and management is a difficult and an incessant task, an industrial marketer has to go through certain stages that are involved in designing a superlative channel system. The various steps that are involved in channel design process are analyzing needs of the customer, establishing channel objectives, considering channel constraints, listing channel tasks, identifying channel alternatives, evaluating alternate channels and selecting the intermediaries.

The industrial marketer also has to take appropriate decisions on channel management by selecting the right intermediaries based on the various steps. The intermediaries need to be continuously motivated by means of offering them various benefits and facilities. Any conflicts arising between the intermediaries due to various reasons need to be solved by the industrial marketer. Finally, the entire channel performance has to be evaluated and necessary control measures need to be taken in order to enhance the performance of the entire channel network.

15.9 KEY WORDS

Channel design, business intermediaries, physical distribution & functions of channels of distribution.

15.10 SELFASSESSMENT QUESTIONS

1. What is the need for channel designing and what are the various stages involved in the process?
2. What are the different techniques used to motivate the channel members?
3. Briefly explain the important functions of channels of distribution?

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UNIT - 16 : LOGISTICS MANAGEMENT

Structure:

16.0. OBJECTIVES

After studying this unit,you will be able to;

- Understand the meaning and Definition of logistics.
- Discuss the significance of logistics management.
- Explain the functions of logistics.
- Highlight the impact of international distribution logistics.

16.1 INTRODUCTION

An inefficient and untimely delivery can make the customers to terminate their relationship with the manufacturer and go in search of a new supplier. This means that products must be delivered to the customers as and when required by them, at their place of choice, while maintaining the quality. Hence, there should be proper supply chain management (SCM) systems in any channel network that calls for substantial investment of resources in the entire process. An efficient SCM helps the channel network to reduce average cost per customer, minimize wastage and prevent duplication, cut down on delivery time, and provide better customer service.

Supply chain management deals with all the activities in the channel network that begins with procuring the raw material by the manufacturer till delivering the goods in the hands of the end user. The entire network is well connected with the organizations in the chain dependent on each other who mutually cooperate and work together. This helps in the systematic flow of products, services and information from the manufacturer to the intermediaries and then to the customers.

16.2 MEANING

Logistics is a military term that refers to the management of various activities like transportation, inventory, warehousing right from the stage of processing the raw materials by the manufacturer to convert it into finished goods till they are made available to the customer for use. While logistics management helps to optimize the flow of material within the organization, supply chain management crosses the boundaries of organization extending material flow integration upwards to suppliers and also descending down to customers.

Logistics basically represents two primary product movements – (i). Physical supply, concerned with supply of raw materials, component parts, and other related supplies necessary for the manufacturing process. This comes under the purchase function (Materials Management);

(ii). Physical distribution, concerned with delivering the finished product to customers and the middlemen. This comes under the marketing management that is also called as Marketing Logistics.

16.3 PHYSICAL DISTRIBUTION (MARKETING LOGISTICS)

Marketing logistics is the process of delivering the finished goods to the intermediaries as well as customers. An efficient delivery system helps to reduce the costs, improve customer service, and minimize time that finally helps to gain customer loyalty. A physical distribution system involves various tasks (as given in the table below) that interact with each other and play an important role in the overall performance of the logistics system. A particular logistics activity cannot be performed without evaluating its impact on other areas. For instance, the objective of maximized customer service may develop into a conflict with the objective of minimized distribution cost. Hence, total cost approach has to be considered to manage such inconsistency.

S.No	Tasks	Key aspects
1	Transportation	An important activity that involves movement of goods from the manufacturer to the customer.
2	Warehousing	A place where goods are stored till they are made available in the market place when needed.
3	Inventory Management	Ensures that right mix of products are available at right place/time in sufficient quantity
4	Packaging	Protects the products, maximizes use of warehouse space, maintains product identity
5	Materials handling	Maximizes speed, minimizes cost of order-picking, moving to and from storage, loading and unloading operations
6	Order processing	Communicates requirements to appropriate locations through inventory management. Starts the physical distribution process
7	Production planning	Goods are made available for inventory. Planning of warehouse facility utilization, transportation requirement
8	Customer service	Establishes customer service levels with marketing objectives as well as cost limitations
9	Plant location	Facilities planning (factory and warehouse location) to ensure capacity & reduce transportation costs

16.4 SIGNIFICANCE OFINTERNATIONAL LOGISTICS

Internationally successful companies have identified the importance of logistics as a management function. Public awareness of logistics has increased significantly, and its influence on strategic corporate decisions is strong. However, many companies are still in the process of defining the specific scope of responsibility for their logistics function and gearing their service networks towards the needs of their customers. Reduced delivery times and adherence to defined delivery dates as well as completeness and accuracy of delivery are important criteria for increasing customer satisfaction through logistics services.

At the same time, worldwide mega trends such as internationalization of procurement, production and sales, increasing resource scarcity and energy costs are challenges for logistics managers and lead to new and changing requirements on the network competence of companies. As a result, overriding macroeconomic and social trends have an ongoing effect on the development of logistics. More than ever before, today's logistics mangers are confronted with dynamic trends in corporate development, and dynamic trends are difficult to forecast. Future –oriented strategies must be able to adapt to nascent trends as early as possible, and logistics goals must be geared towards these trends. This is only way to ensure the long-term success of a company. Besides globalization, other major logistics challenges are continuously arising, especially in the form of internationalization, increased security requirements and an increasing demand for ecological sustainability.

16.5 PROBLEMWITH INTERNATIONAL LOGISTICS

The following are the major issues faced by logistic companies when they are involved in international trade. These might appear at every border, and circumstances can change within a very short distance

16.5.1 Difference in Logistics

International logistics are different from national logistics, and it is not just a case of moving the same activities to another location in terms of types of transport used, large variation in the demand for the service, more intermediaries involved, communication become more difficult distance and culture and documentation is more complicated.

16.5.2 Problem with Trade

The administrative difficulties are one type of problem for international logistics are physical barrier, such as border control and customer formalities, technical barriers, such as differing and health and safety standards and fiscal barriers such as different rates of value added tax, excise and customs duties.

16.5.3 Political and Legal System

The type of government and laws in different countries give significantly different conditions. Practices that are accepted on one country may be unacceptable in a neighbor. So the logistics company should take into consideration of the expectation of the country's political and legal system with regard to logistics.

16.5.4 Economic Conditions

Political system directly affects the economy, and there are significant differences in prosperity, disposable income and spending habits. Sometimes there are very rapid changes between borders of the two countries.

16.5.5 Competition

This competition varies between very tense, the market driven competition in some countries, to state run monopolies in others. Logistics in say China is particularly well developed and companies compete for business over a wide area.

16.5.6 Availability of Technology

Many logistics companies use sophisticated technologies for e-commerce, efficient customer response, satellite location, in-cub navigation, real-time routing, total communication, and a whole range of other developments.

Although such technology feasible, it does not mean that everybody uses it. Most of the world does not have access to, does not need, or cannot afford the latest technological development.

16.5.7 Geography

Transport is generally easier in straight lines over flat terrain. Physical barriers that hinder transport include seas, mountain ranges, desserts, jungles, rivers, cities, national parks, and so on.

16.5.8 Financial Issues

There are many financial factors to consider. Some countries do not allow their currency to be taken out of the country, the value of some currencies fluctuates wildly or falls quickly, some banking system are inefficient, sometimes exchanging money is difficult and so on. A different type of problem comes with customs duties and tariffs for material entering the country.

16.5.9 Customs Barriers

Conventionally, customs duty is payable whenever materials enter a country. In practice, there is more than just customs duty, and it can be quite difficult to add all the taxes and duties to calculate the amount payable. For example goods entering the European Union one might have to pay customs duty, countervailing duties, anti dumping duties etc., these are not only costs of crossing a border, as companies have to pay the cost of compliance with export/ import regulations, such as compulsory documentation and information requirements.

16.6. TOTAL COST APPROACH(TRADE-OFF APPROACH)

The total cost approach focuses to balance two essential variables:

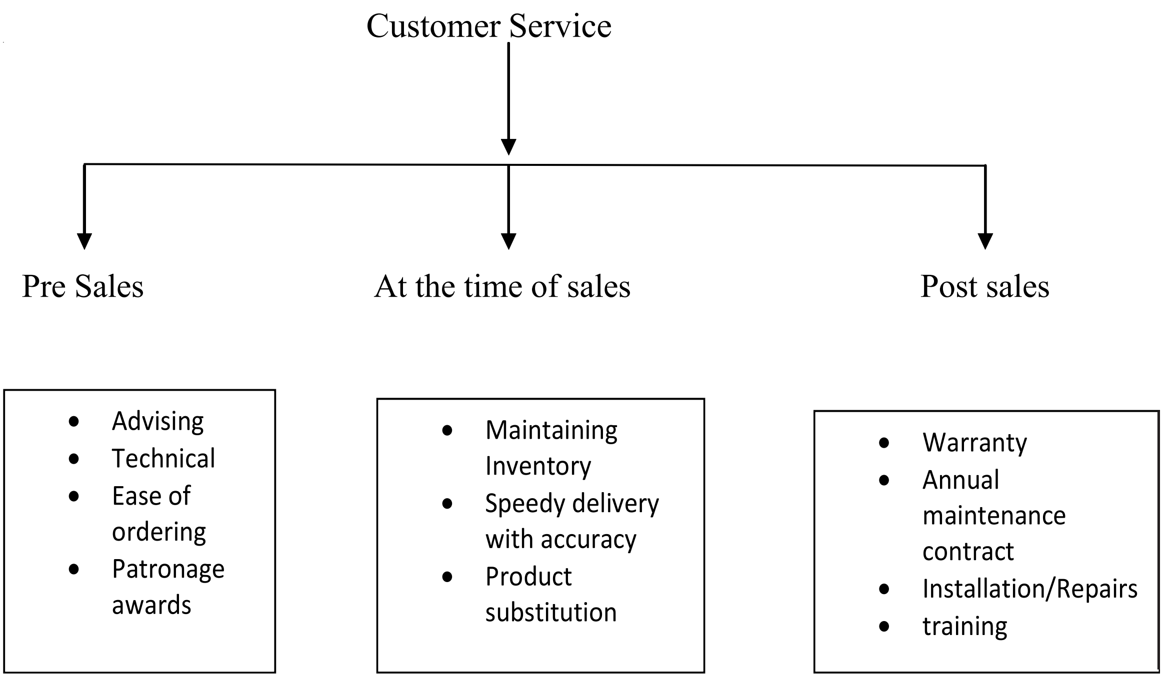
- Total distribution costs, and
- The level of logistical service provided to the customers.

The total cost approach is designed in such a way that it tries to achieve a combination of cost and service levels that maximizes the profits to the company and the channel members. In this approach, the total cost of distribution is considered instead of the individual cost of the elements of physical distribution as the decision made for one logistical variable affects all or some of the other logistics variables.

For example, if inventory is reduced below the required quantity in order to reduce inventory costs, it may result in stock outs and increase in order backlogs. This may necessitate extra productions to provide the stock out items and air-freight them at high cost to customers whose production stopped due to non-delivery of products. All this would finally lead to reduction in future orders from the unsatisfied customers due to poor delivery performance. Thus, to save a small individual cost, the total cost substantially increased. The interactions among logistics activities (i.e. transportation, inventory, warehousing) involves a cost trade off as these cost elements are sometimes in economic conflict with one another. Thus, manager must be willing to trade-off a cost increase in one activity for a larger cost decrease in another activity that should finally result in reduced total logistics costs.

Service cost tradeoff

Service aspect is the other half of the total cost approach. It is to be understood that all customers or products do not require same level of service. Each element of service (as given in the figure below) has different levels of importance that the industrial marketer should recognize. The cost involved in providing the level of service must be evaluated in light of the revenue generated. Once the important elements of customer service are determined by the industrial marketer, he should set goals of customer service levels for each service element, compare the actual with goals and finally take corrective actions to minimize the difference.



Elements of Service

Physical distribution impact on middlemen

An ineffective performance of physical distribution system will impact the operations of the intermediaries. This needs to be well understood by the industrial marketers who have to plan accordingly to avoid such inefficiencies. For instance, delaying the delivery of products will result in intermediary trying to avoid the manufacturer's products and searching for another company. This leads to slow down of business and customer dissatisfaction. Therefore, the marketer needs to take several steps as given below that would help him to improve the physical distribution system.

Develop proper MIS system

The marketer should create online network with his distributor through the use of information technology tools that helps him to know the inventory levels and provide more stock on time.

Standardize the procedure

He should try to standardize the various activities and operational procedures involved like product packing, handling of materials etc., at all the organizations of the channel members. This helps to improve the overall operational efficiency and also brings in consistency within the system.

Integration

The industrial marketer should properly integrate the physical distribution with the channel members that helps to improve the overall marketing effectiveness. For example, the shipment consolidation programs where the distributors in particular area are encouraged to place all their orders on the same day or transport their orders through a common truck.

Marketing logistics is considered to have a viable benefit of providing finer customer service at low delivery cost that is to be regarded as a long-term strategic issue. The physical distribution cannot be easily replicated by the competitors as it entails high costs in terms of investments in people, system, money and time. With many concepts emerging like outsourcing, Just in Time (JIT), and Total Quality Management (TQM) there is a big role and scope for logistics in the future.

16.7 FACTORS INFLUENCING DISTRIBUTION AND LOGISTICS

1. **Cost**
2. **Customer Service**
3. **Timing**
4. **Quality**
5. **Product Flexibility**
6. **Volume Flexibility**
7. **Technology**
8. **Location**

1. Cost

Most organizations want low costs, but some adopt a positive strategy of minimizing their logistics costs. This leads to higher profits for the organization and lower prices for customers

2. Customer Service

Logistics controls stock levels, delivery times, speed of response, and other measures of customer service. By concentrating the logistics strategy on customer service, organizations can get a long-term competitive advantage.

3 Timing

Customers generally want products as soon as possible, so a common logistics strategy guarantees fast deliveries. Timing can also mean rapid supply of new products, or delivering at the time specified by a customer.

4 Quality

Customers demand higher quality in all products. A common logistics strategy guarantees high quality service, even though it can be difficult to say exactly what mean by 'high quality logistics'.

5. Product Flexibility

This is the ability of an organization to customize products to individual specifications. One logistics strategy is based on a specialized or customized service, such as pick fords removals.

6. Volume Flexibility

Changing levels of business can cause severe problems for logistics, as one can see during the morning rush hours in any major city. Volume flexibility allows an organization to respond quickly to changing levels of demand.

7. Technology

Logistics uses a wide range of technologies for communication, tracking loads, sporting parcels, identifying products, recording stock movements, and so on. Some organizations have a strategy of developing and using the latest technologies.

8. Location

Customers generally want products to be delivered as close to them as possible. This might mean that a book club delivers directly to door, a shop has a convenient location 60 in a town centre, or a wholesaler has a regional logistics centre near to major cities. One logistics strategy is to provide a service in the best possible location, such as bus station in town centers.

16.8 CASE STUDY

Supply Chain Success: Mumbai Dabbawalas

The Dabbawalas of Mumbai are unique case in logistics. Neatly stacked dabbas (tiffins or lunch boxes) are a common sight at most of the rail way stations, late every morning in Mumbai, India. A man is who is illiterate or semi-literate delivers hot lunch at the doorstep of the subscriber. It is an error-free and there are virtually no mismatches.

The Mumbai Tiffin Box Suppliers Association is a 38-year-old organization with 4,500 members and a huge, loyalty customer base. Their customer base includes office goers, students, shopkeepers, etc. Instead of carrying their own lunch at an early hour in the morning, they prefer to subscribe this dabba service.

For a small fee, the dabbawala picks up the freshly packed lunch form the subscribers house and deliver it to his/her office at lunch time. Once lunch is over, the empty dabba is again collected by the dabbawala. This is done with the help of Mumbai's extremely efficient railway system called th Mumbai locals.

There are special trains known as dabbawala specials. The dabbas change many hands and are loaded and offloaded in many trains before their final delivery.

There is a scientific method of putting an identification mark on each dabba. Each dabba lid is marked a particular code. The code format is 'DBOF' where D denotes the dabbawala's number (assigned by the association), BO is a combination indicating the building/office and F is the floor number of that building where the tiffin box has to be delivered.

The lid is also marked with a number denoting the railway station where the box has to be off-loaded, followed by an alphabet indicating the station where it is to be picked up. Can you imagine what the fee for all of this is? The service charges vary between ' 150 (US$3) to ' 300 (US$6) per month, depending on the customer's location and the distance covered.

This service was started by a Parsi banker when he enjoyed a carrier to fetch his lunch every afternoon. The idea caught on and this inspired many unemployed people to become dabba carriers. Soon, each dabbawala had a handful of customers. To ensure that each carrier worked only in a particular district and didn't interfere with other dabbawalas, a union called the 'Mumbai Tiffin Box Carriers Association' was formed in 1968. Today, there are more than 5000 semi-literate dabbawallas who transport 1,75,000 boxes in a 3-hour period, traversing 25 km using public transportation, involving multiple transfer points. In 1998, Forbes Global magazine conducted an analysis of the service and gave the dabbawalas a six sigma efficiency rating.

Analyze the case:

16.9. NOTES

16.10. SUMMARY

Logistics deals with optimizing the activities like transportation, inventory, warehousing of the raw materials at the manufacturer's end from the stage of processing till conversion to finished goods that are ready for customers' use. Physical supply and Physical distribution are the two product movements of logistics. Physical distribution (a part of Marketing Logistics) involves the delivery of finished products to the intermediaries and the end users. During physical distribution, the industrial marketers follow the total cost approach that involves a trade-off and balances the total distribution cost and the service level to the customers.

A physical distribution system needs to be well planned in order to avoid inefficiency that impacts the intermediaries. Certain measures like developing a good MIS system, standardizing the operational procedures and integration of physical distribution with channel members can be taken by the industrial marketer to improve the performance of physical distribution and improve marketing effectiveness.

16.11 KEYWORDS

Physical distribution, Supply chain management, International logistics, warehouse, inventory

16.12 SELFASSESSMENT QUESTIONS

1. Define logistics management and explain its objectives
2. Define logistics management and discuss its role in today's business.
3. How do you think international logistics differ from domestic logistics?
4. What do you mean by supply chain management?
5. Explain are the factors influencing the distribution and logistics decisions in international business?

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MODULE - V
PROMOTION OF INDUSTRIAL GOODS

UNIT - 17 : MEANINGAND OBJECTIVES OF PROMOTION

Structure:

17.0 OBJECTIVES

After studying this unit, you should be able to;

- Define the meaning of Promotion
- Explain the objectives of Promotion
- Discuss the concept of branding of industrial product
- Give the meaning of Corporate image

17.1 INTRODUCTION

It is no longer enough for a business to have great products. Lots of businesses have those too. Customers need to know about a great product and be persuaded to buy. That is the role of promotion.

Promotion is all about communication. Why because promotion is the way in a business makes its products known to the customers, both current and potential.

The main aim of promotion is to ensure that customers are aware of the existence and positioning of products. Promotion is also used to persuade customers that the product is better than competing products and to remind customers about why they may want to buy.

It is a common mistake to believe that promotion by business is all about advertising. It isn't. There are a variety of approaches that a business can take to get their message across to customers, although advertising is certainly an important one.

It is important to understand that a business will use more than one method of promotion. The variety of promotional methods used is referred to as the promotional mix.

17.2 MEANING

Promotion refers to raising customer awareness of a product or brand, generating sales, and creating brand loyalty. It is one of the four basic elements of the market mix, which includes the four P's: price, product, promotion, and place.

Promotion is also defined as one of five pieces in the promotional mix or promotional plan. These are personal selling, advertising, sales promotion, direct marketing, and publicity. A promotional mix specifies how much attention to pay to each of the five factors, and how much money to budget.

17.3 OBJECTIVES OF PROMOTION

The possible objectives for marketing promotions may include the following:

♦ **Build Awareness** – New products and new companies are often unknown to a market, which means initial promotional efforts must focus on establishing an identity. In this situation the marketer must focus promotion to:

1) Effectively reach customers, and

2) Tell the market who they are and what they have to offer.

♦ **Create Interest** – Moving a customer from awareness of a product to making a purchase can present a significant challenge. As we saw with our discussion of consumer and business buying behavior, customers must first recognize they have a need before they actively start to consider a purchase. The focus on creating messages that convince customers that a need exists has been the hallmark of marketing for a long time with promotional appeals targeted at basic human characteristics such as emotions, fears, sex, and humor.

♦ **Provide Information** – Some promotion is designed to assist customers in the search stage of the purchasing process. In some cases, such as when a product is so novel it creates a new category of product and has few competitors, the information is simply intended to explain what the product is and may not mention any competitors. In other situations, where the product competes in an existing market, informational promotion may be used to help with a product positioning strategy. As we discuss in the Targeting Markets tutorial, marketers may use promotional means, including direct comparisons with competitor's products, in an effort to get customers to mentally distinguish the marketer's product from those of competitors.

♦ **Stimulate Demand** – The right promotion can drive customers to make a purchase. In the case of products that a customer has not previously purchased or has not purchased in a long time, the promotional efforts may be directed at getting the customer to try the product. This is often seen on the Internet where software companies allow for free demonstrations or even free downloadable trials of their products. For products with an established customer-base, promotion can encourage customers to increase their purchasing by providing a reason to purchase products sooner or purchase in greater quantities than they normally do. For example, a pre-holiday newspaper advertisement may remind customers to stock up for the holiday by purchasing more than they typically purchase during non-holiday periods.

♦ **Reinforce the Brand** – Once a purchase is made, a marketer can use promotion to help build a strong relationship that can lead to the purchaser becoming a loyal customer. For instance, many retail stores now ask for a customer's email address so that follow-up emails containing additional product information or even an incentive to purchase other products from the retailer can be sent in order to strengthen the customer-marketer relationship.

17.4 BRANDING OF INDUSTRIAL PRODUCT

Branding AddValue:

- Branding makes the buying process easier
- Helps reduce the risk of buying the wrong product
- Add values to a company's intangible assets
- Can create price premium
- Branding is a distinct form of differentiation

Brand function

- Increased information efficiency
- Branded product have recognized value
- Risk reduction
- Ensure and legitimize buying decisions
- Image benefits creation

B2B branding has its specific features. First of all, these features are related to the fact that the commercial brand is working with the professional audience. Requirements for the professional audience are tougher, so the emphasis in creating brand shifts from the emotional angle to rational one. Requirements for the B2B brand are the same as the requirements for professionals - being reliable, predictable and guaranteeing quality.

If the emotions are decisive in the brand's future on consumer market, industrial brand is a brand that solves the problem. It is the brand that is trusted in business as a serious partner. Another important detail that should be taken into account in the industrial branding is the factor of marketing communications. Marketing communications which help to develop a B2B brand work in more sophisticated way. The brand has to build relationships at different levels of decision-making, each time from scratch.

We recommend distinguishing 3 main phases in industrial branding:

- Naming
- Corporate identity
- Developing the concept of brand

Naming

Naming is the choice of brand name. Choosing a name in the industrial branding is the choice of the brand's future. The name in the B2B sector is clear associations with a specific area of activity. There's nothing more dangerous in the industrial branding than an abstract and empty name. Of course, there are some cases when a fundamentally new product, a unique product, is created in the B2B sector and the task of the name is to inform the market: "Please do not compare me with anything! I am really like a unique product! That's just what my name tells about! ". However, to be frank, there are not so much cases today. As a rule, the new product can be classified and put into a number of similar goods. The task of the name is to win the competition. The task is to draw attention, make the first impression, say about the brand as much as possible and do it very quickly.

How to create the name which can do it? We believe that creating something new it's always good to consider the existing experience. Well, you can always look at the experience of others and learn useful lessons. Who of the predecessors was successful and why? B2B should not have unnecessary words because the task of business is to earn more money! It means that the most successful brand names are "speaking" names. About what should they speak? They should speak about what is important. The brand name which says nothing about the product and the company's business will not help to find new contacts and proper positioning and even affect it. It's not just that the brand can not be correctly perceived by the market and rejected only on this ground, but that the abstract name of the brand will make the owner to invest more money in brand building.

The brand name is like its testimonial letter. The brand will be perceived by its name immediately making the first conclusions. Actually, one of the features of industrial branding is that it has very strong stereotypes. To some extent, this is the very feature which is associated with the fact that industrial brands are harder to diversify or reposition. However, the explanation is simple - more sophisticated marketing communications are to blame. Their complexity is explained by the fact that industrial brand has to build contacts at various levels of decision-making because the decision making process in business, as a rule, includes several stages.

Industrial brands are the big fish of modern industry. They are trusted, they are matched and they are the marks of economic prosperity as a whole. The appearance of a new name is the event and the disappearance of the old one is the tragedy. The decisions on the B2B brands are sometimes taken by the governments as so great is their role in the modern society.

Creating the Corporate Identity

Corporate identity in industrial branding should reflect several qualities of the brand:

- Industry specialization
- Geography of business

The potential customer will have only several seconds for the corporate identity contact to make a decision whether to continue the dialogue. If a business card will go in the trash it will be difficult to return to constructive dialogue. That is why the corporate identity should be not only recognizable, unique and attractive, but also substantive. Corporate identity should represent the business telling the maximum useful information about it in a short period of time provided.

Creating a corporate identity of a company operating in the B2B sector includes several stages:

1. Creating a design solution
2. Creating a slogan
3. Description of design solutions and a slogan, description or creation of business legend from scratch
4. Creating a brand-book or guidelines for corporate identity use

None of these items can not be missed because the corporate identity will be the image of your brand for many years. You should understand it, you should be comfortable with it, but, and which is more important your customers should feel comfortable with your corporate identity. You create a corporate identity not for yourself, but for the business, and, strangely enough, your business has different needs. Corporate identity must be recognizable and understandable. This is of crucial importance when we talk about B2B business which is the professional sector.

The concept of industrial brand development should handle the following tasks:

- **Defining the goals and tasks of the brand**
- **Shaping the corporate mission of the brand.**It is important to remember that the b2b market is real people who make decisions on the ground of business feasibility never forgetting about the moral aspects. If there are two competing brands on the market one of which has a more human-friendly image it is the image the customers will prefer. Ultimately, people like to make decisions that from their point of view make the world a little better. The corporate identity mission of the brand solves this particular problem explaining what exactly

this brand is different from its competitors and why it is so important for the brand to be successful.

- **Specifying the target group** as industrial brand usually works in one or more clearly defined sectors. It is important to know these sectors very well, to investigate the decision-making process in the companies represented in the sector in order to make sure that marketing communications really contribute to the dialogue with all the links of the decision-making chain.

- **Specifying a plan of geographic priorities of the brand** . At the stage of brand development is necessary to anticipate that the brand can go beyond the certain geographical scope and become successful in various countries. The brand should be technically ready for the eventual success.

- **Developing the concept of brand extension**, its development in the market, entering adjacent markets.

- **Specifying the communication brand concept.** Fist of all, you should specify the communication tools which will help to bring the brand on the market. This is very important to make the brand technically ready to work with certain media. All technical questions concerning the use of the brand should be reflected in the brand-book, but we must be realistic. Today's world is so diversified offering such a large number of communications solutions that it is almost impossible to predict everything. If you need a quality brand-book you should focus on the decisions that you plan to use without spending time and effort on something that won't be popular in the foreseeable future.

Creating the concept of industrial brand development is the creation of a better future because every successful brand it is the way to make the world better and solve one more problem.

17.5 CREATING CORPORATE IMAGE

Corporate image is the reputation of the firm with the various audiences that are important to it. These groups that have a stake in the company are known as stakeholders. Stakeholders are affected by the actions of the company and, in turn, their actions can affect the company. Consequently, its image in the eyes of its stakeholders is important to the company. The principal stakeholders with whom most large corporations must be concerned are: customers, distributors and retailers, financial institutions and analysts, shareholders, government regulatory agencies, social action organizations, the general public, and employees.

The image that stakeholders have of the company will influence their willingness to either provide or withhold support. Thus, if customers develop a negative perception of a company or its products, its sales and profits assuredly will decline. Government regulatory latory agencies, another important set of stakeholders, are required by law to monitor and regulate firms for specific, publicly defined purposes. Nevertheless, these agencies have considerable discretion in how they interpret and apply the law. Where they have a positive perception of the firm, they are likely to be much less censorious.

Obviously, each of the various stakeholder groups is likely to have a somewhat different perception of the corporation because each is concerned primarily with a different facet of its operation. Thus, consumers are principally interested in the price, quality, and reliability of the company's products and services. Financial institutions are concerned with financial structure and performance. Employees are mainly concerned with wages, working conditions, and personnel policies. Logically, then, a company should tailor its communication to each stakeholder group individually to address the special concerns of that group.

However, maintaining a consistent image among the several stakeholder groups is also vital. Although it is prudent to stress different facets of the firm's identity to its various publics, the firm should avoid projecting an inconsistent image, because the concerns and memberships of different stakeholder groups often overlap. For instance, the financial community and the shareholders would have many of the same financial and strategic concerns about the company. In fact, many shareholders rely heavily on the advice of experts from financial institutions. Similarly, both employees and the general public have an interest in the overall prestige of the firm and the reputation of its products. A social action group's criticism, whether economically effective or not, is bound to influence some customers and affect the company's public reputation. A regulatory agency such as OSHA would focus narrowly on the firm's safety record and policies, but the company's employees and their labor unions also have a stake in these matters.

A corporate identity is the manner which a corporation, firm or business presents themselves to the public, such as customers and investors as well as employees. It is a primary task of the corporate communications department to maintain and build this identity to accord with and facilitate business objectives. It is typically visually manifested by way of branding and the use of trademarks, but also includes things like product design, advertising, public relations and the like.

In general, this amounts to a corporate title, logo (logotype and/or logogram) and supporting devices commonly assembled within a set of guidelines. These guidelines govern how the identity is applied and would include approved colour palettes, typefaces, page layouts and other such.

Below are five simple, but important, ways organizations can shore up their brand image and create a positive reaction.

1. **Active Social Media Presence:** Every company in the modern world needs a social media presence. This is more than just throwing up a Facebook or LinkedIn page or sending out self-promoting Tweets on occasion. Social media allows for targeted groups and interaction. Someone inside your company should be populating any social media presence regularly. They should be responding and interacting with the community. And they should be pushing out content that is both educational and relevant and aligns with your business. It's all about building a trusted community—having it feel inclusive goes a long way.

2. **Website Appearance:** Like it or not, your website may be the first impression a potential customer has with your organization. Your website should be dynamic, contain updated industry news or company information, and include any relevant content feeds or blogs. It's a platform for someone to get to know you better. Use it like Madison Avenue retailers use their display windows. Your website should invite them to come in and learn more. Having a poorly designed or out-of-date, stagnant website will turn away potential customers fast.

3. **Thought Leadership:** Take a close look at the content your marketing team is pumping out. Is it all product- and services-related? Or is the content you are making available—either through your website, social avenues or email marketing campaigns—educational? Are you providing value or just spamming? Users are savvy and finicky. Smart companies use these marketing avenues to push out educational content—industry news, analysis, research, white papers—that aligns with their brand's business. This creates a more positive brand experience because it educates the audience and not just solicits them.

4. **Corporate Culture:** Often overlooked in today's fast-paced digital world is the importance of the corporate culture. Word spreads fast nowadays. Employees who have a positive work experience share it through their own social media channels and word gets around. Conversely, employees who are treated miserably or feel taken advantaged of also share. How you run your company is on display for the world to see. Companies will want to do business with like-minded companies that share the same values.

5. **Executive Access:** Just as every employee is an extension of his or her company's brand, the same is true for the C-level executives. If you're in the C-suite you need exposure. You should be working with marketing to get your name and face out as a trusted industry leader. This should include corporate blogs, speaking engagements and accessibility to the

business press. White papers should be produced where you are quoted. You should be speaking at industry conferences, participating in industry roundtables and webcasts. When a potential customer sees a CEO active in his or her industry and a thought leader, it gives them more confidence in the company.

IMPORTANCE OF CORPORATE IMAGE

1. To identify the strength and weakness of your company's corporate image based on the 4 basic dimensions

- ♦ Quality
- ♦ Performance
- ♦ Responsibility
- ♦ Attractiveness

2. To measure the relative position of your company's corporate image in comparison to other companies within the industry

3. To evaluate the level of importance of dimension and attributes that drives your company's corporate image. The information will enable you to maximize opportunity and reduce possible threats

4. Given that corporate image index is an omnibus survey, your company will acquire comprehensive, reliable and indispensible information at a sensible cost

17.6 PROMOTIONAL STRATEGIES

Companies use all types of promotional methods, depending on their budget and industry. For example, small business owners may use fliers or referrals to get their business going. Large corporations often sponsor major sporting events, such as auto racing. Whatever the case, companies must have a particular objective when executing promotional strategies: To garner sales leads, increase store traffic or get the order, as in mail order or Internet advertising.

Search Engine Optimization

Search engine optimization is the process of tweaking your website, keywords and web pages to achieve a first-page listing in search engines, such as Google.com and Yahoo. Find someone who specializes in search engine optimization in your area. Start with web designers. Start out by obtaining a user-friendly URL, which is an acronym for Uniform Resource Label, or website address, according to the Business Insider website. Help your SEO by thinking of all the two- to- five-word phrases that best describe your business. Once your site has been optimized, start linking to other sites to build traffic. Purchase Internet traffic software to track your results.

Frequency Card Programs

Small retailers use frequency card or loyalty programs to build store traffic and visit frequency. The objective is to reward customers according to how much they purchase. For example, a movie theater can offer free popcorn after a customer accumulates 250 points equivalent to four movies. The customer may then earn a free movie after accumulating 1,000 points. Create a display that apprises shoppers about your frequency program. Keep applications near the display for customers to fill out. Have people fill out their name, address and email. Issue customers a card that will keep track of their purchases. Contact a marketing consultant in your area that specializes in frequency card marketing if you need help programming cards into your register.

Inquiry Follow-up Method

The inquiry follow-up method is a cost-effective way to build your business. Start by placing classified ads in newspaper and various weekly shopper guides or free papers. Create a catchy heading that describes the benefits of your offer. For example, use a heading like "Get Rid of Your Gray Hair In Five Minutes" if you are selling a hair coloring product. Write three to five lines that briefly describes your offer and where to get more information. Include a phone number or website if you sell online. Invite people to write or call for a catalog or information piece if you operate by mail. Respond to potential customers immediately to demonstrate highly effective customer service, as this can result in more sales.

Online Video Promotions

Videos are an effective way to promote your website, store or business-to-business customer. However, it is best to integrate them with other promotional or advertising methods, according to Entrepreneur.com. Write out a small script for your five- to- eight-minute video. Offer some free advice that entices people to visit your site or call you. For example, an owner of a small marketing research firm may instruct businesses how to create the ideal survey. Create a Youtube.com account and place your video in online business publications or social networking sites, including Facebook.com. Target the customers that you want to attract by labeling your video appropriately.

17.7 NOTES

17.8 SUMMARY

Consumer sees is an exciting, professional and relevant promotion. This encourages them to choose the promoted brand and, in the case of almost a million households in the Star WarsTM campaign, to buy the Kellogg cereal brand. Behind these results is an enormous amount of planning and communication, all of which must be both effective in itself and in supporting other parts of the event.

A successful event takes teamwork, careful management and precise communication. But that isn't the end; the business must then immediately go back to planning. This will help to decide how to keep the market it has gained, or how to create yet another exciting and impressive promotion.

17.9 KEY WORDS

- Promotion
- Corporate Image
- Brand
- Branding

17.10 SELFASSESSMENT QUESTIONS

1. What is promotion?
2. Explain the objectives of promotion
3. Discuss the significance of promotion in industrial marketing
4. Explain the concept of corporate image
5. Discuss the importance of branding

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UNIT - 18 : SALES PROMOTION

Structure:

18.0 OBJECTIVES

After studying this unit, you should be able to;

- Define Sales promotion
- Explain the objectives of Sales Promotion
- Highlights the uses of Sales Promotion
- Examine the methods of Sales Promotion
- Give the meaning of public relation

18.1 INTRODUCTION

Where advertising offers a reason to buy, sales offers an incentives to buy. Sales promotion consists of myriad of incentives tools, mostly short term designed to stimulate quicker/ greater purchase of particular product/ services by consumers or the trade.

It is a key ingredient in the communication mix. Sales Promotion tools vary in their specific objectives. A free management advisory service aims at cementing a long term relationship with a retailer.

Sales promotion includes several communications activities that attempt to provide added value or incentives to consumers, wholesalers, retailers, or other organizational customers to stimulate immediate sales. These efforts can attempt to stimulate product interest, trial, or purchase. Examples of devices used in sales promotion include coupons, samples, premiums, point-of-purchase (POP) displays, contests, rebates, and sweepstakes.

Sales promotion is implemented to attract new customers, to hold present customers, to counteract competition, and to take advantage of opportunities that are revealed by market research. It is made up of activities, both outside and inside activities, to enhance company sales. Outside sales promotion activities include advertising, publicity, public relations activities, and special sales events. Inside sales promotion activities include window displays, product and promotional material display and promotional programs such as premium awards and contests.

Sale promotions often come in the form of discounts. Discounts impact the way consumers think and behave when shopping. The type of savings and its location can affect the way consumers view a product and affect their purchase decision. The two most common discounts are price discounts ("on sale items") and bonus packs ("bulk items"). Price discounts are the reduction of an original sale by a certain percentage while bonus packs are deals in which the consumer receives more for the original price. Many companies present different forms of discounts in advertisements, hoping to convince consumers to buy their products.

18.2 MEANING OF SALES PROMOTION

Sales promotion is the process of persuading a potential customer to buy the product. Sales promotion is designed to be used as a short-term tactic to boost sales – it is rarely suitable as a method of building long-term customer loyalty.

Sales promotions are the set of marketing activities undertaken to boost sales of the product or service.

Sales promotion is any initiative undertaken by an organization to promote an increase in sales, usage or trial of a product or service (i.e. initiatives that are not covered by the other elements of the marketing communications or promotions mix). Sales promotions are varied

18.3 OBJECTIVES OF SALES PROMOTION

Sales promotion activities are undertaken to achieve the following objectives:

1. To increase sales by publicity through the media which are complementary to press and poster advertising.
2. To disseminate information through salesmen, dealers etc., so as to ensure the product getting into satisfactory use by the ultimate consumers.
3. To stimulate customers to make purchases at the point of purchase.
4. To prompt existing customers to buy more.
5. To introduce new products.
6. To attract new customers.
7. To meet competition from others effectively.
8. To check seasonal decline in the volume of sales.

18.4 USES OF SALES PROMOTION

1. Enables industrial manufacturers to adjust to short term variation in supply and demand
2. To test how high a test price they can charge, because they can always discount it.
3. Induce customers to try new products instead of straying from their current ones.
4. They promote greater awareness of prices
5. Helps the industrial market to adopt programmes to different consumer segments

18.5 TECHNIQUES/ METHODS OF SALES PROMOTION

There are various methods/ tools/ techniques of sales promotion are as follows:

1. Price Off
2. Allowances
3. Trade Show
4. Exhibition
5. Catalogs
6. Samples
7. Promotional Novelties
8. Promotional Letters
9. Sales Contests
10. Free goods

1. Price Off: A straight discount off the test price on each case purchased during the stated time period encourages dealers to carry a new item that they might not ordinarily buy. The dealers can use the buying allowance for immediate profit advertising or price reduction.

2. Allowances: An amount offered in return for the retailers agreeing to feature the manufacturer's product is some way.

3. Trade Show: A trade fair (trade show, trade exhibition, or expo) is an exhibition organized so that companies in a specific industry can showcase and demonstrate their latest products and services, meet with industry partners and customers, study activities of rivals, and examine recent market trends and opportunities. In contrast to consumer fairs, only some trade fairs are open to the public, while others can only be attended by company representatives (members of the trade, e.g. professionals) and members of the press, therefore trade shows are classified as either "public" or "trade only". A few fairs are hybrids of the two; one example is the Frankfurt Book Fair, which is trade only for its first three days and opens to the general public on its final two days. They are held on a continuing basis in virtually all markets and normally attract companies from around the globe. For example, in the U.S., there are currently over 10,000 trade shows held every year, and several online directories have been established to help organizers, attendees, and marketers identify appropriate events.

Objectives of Trade Shows:

- Overall purpose of participation

- Creating actual sales
- Identifying potential customers
- Obtaining sales leads
- Gathering competitive intelligence
- Target audience to be reached

Benefits of Trade Shows:

- An opportunity to introduce new products to a large audience in a short duration
- Establishing personal contact with new customers
- Establishing contacts and increasing company awareness with key members of decision making units who cannot otherwise be reached
- Making direct sales by booking orders at trade fair
- Display and demonstration of products
- Evaluating competitors' product
- Discovering new suppliers and distributors
- Obtaining new product ideas
- Training for new salespersons
- Generating new sales leads which help salespersons to close sales

4. Exhibition: An exhibition, in the most general sense, is an organized presentation and display of a selection of items. In practice, exhibitions usually occur within museums, galleries and exhibition halls, and World's fairs. Exhibitions can include many things such as art in both major museums and smaller galleries, interpretive exhibitions, natural history museums and history museums, and also varieties such as more commercially focused exhibitions and trade fairs

Though exhibitions are common events, the concept of an exhibition is quite wide and encompasses many variables. Exhibitions range from an extraordinarily large event such as a World's fair exposition to small one-artist solo shows or a display of just one item. Curators are sometimes involved as the people who select the items in an exhibition. Writers and editors are sometimes needed to write text, labels and accompanying printed material such as catalogs and books. Architects, exhibition designers, graphic designers and other designers may be needed to shape the exhibition space and give form to the editorial content. Organizing and holding exhibitions also requires effective event planning, management, and logistics.

5. **Catalogs: Printed** catalogues are one of the few promotional support that provide buyer organization information about a supplier's product lines and product items. Buyer firms rely on catalogues to determine which supplier makes what products or services. From the information available in catalogues, a buyer may prepare a list of potential suppliers for new purchase and ask these suppliers to submit quotations or bids. Catalogues also help salesperson to establish contacts with technical persons in the buyer's organization.

6. **Samples:** Samples are the promotional tools used to create interest in mind set of industrial customer by giving free samples to the customers.

7. **Promotional Novelties:** This is nothing but gift items given by salespersons to existing and new customers. Many companies get item made once a year, bearing company's name and address and if possible, an advertising message. The common gift items are calendars, dairies, ball point pens, leather bags, memo pads and so on. An effective promotional novelty or gift should be inexpensive, unusual, eye catching and useful. The purpose is to keep buyers constantly aware of supplier's identity. Some companies make two or three categories of gift items, based on high, medium and low costs, for distribution of the gifts to senior, middle, and junior management positions in customer firms. It also gives an opportunity for salesperson to meet the various decision making persons in an organization like technical, commercial and top management. However, care should be taken by salesperson to distribute the gifts in discreet manner at the offices or residences of key persons in customer's organizations so that the buyer should not misunderstand of find it offensive or embarrassing.

8. **Promotional Letters:** Promotional letters, particularly for products purchased infrequently are effective in keeping in touch with customers. It also facilities the work of industrial salespersons. Individualized letters ie, promotional letters, when sent to specific customers along with catalogues, advertising reprints, and technical data sheets, receive good attention. The task of sending promotional letters may be assigned to a special correspondence section. Salesperson can then advise this section about what kind of covering letter to be sent. The objective of the special correspondence section is to convey the message that the company is a good one with which to do business.

9. **Sales Contests:** Many industrial marketing firms hold sales contest or incentives for their sales people and or dealers. The objective is to motivate the sales force and dealers to improve their sales performance over the period of one year. Those who perform well get cash prizes or gifts or foreign trips.

10. Free goods: Offers extra cases of merchandise or free specialty advertising items like pens, paper weight, calendars, planner,, pads etc for those who buy a certain quantity or in a specified time period.

18.6 PUBLIC RELATION

Public relations (PR) are the practice of managing the spread of information between an individual or an organization (such as a business, government agency, or a nonprofit organization) and the public. Public relations may include an organization or individual gaining exposure to their audiences using topics of public interest and news items that do not require direct payment. This differentiates it from advertising as a form of marketing communications. Public relations are the idea of creating coverage for clients for free, rather than marketing or advertising. An example of good public relations would be generating an article featuring a client, rather than paying for the client to be advertised next to the article. The aim of public relations is to inform the public, prospective customers, investors, partners, employees, and other stakeholders and ultimately persuade them to maintain a certain view about the organization, its leadership, products, or political decisions.Public relations professionals typically workfor PR and marketing firms, businesses and companies, government, government agencies and public officials as PIOs and nongovernmental organizations, and nonprofit organizations. Jobs central to public relations include account coordinator, account executive, account supervisor, and media relations manager.

Public relations specialists establish and maintain relationships with an organization's target audience, the media, and other opinion leaders. Common responsibilities include designing communications campaigns, writing news releases and other content for news, working with the press, arranging interviews for company spokespeople, writing speeches for company leaders, acting as an organization's spokesperson, preparing clients for press conferences, media interviews and speeches, writing website and social media content, managing company reputation (crisis management), managing internal communications, and marketing activities like brand awareness and event management. Success in the field of public relations requires a deep understanding of the interests and concerns of each of the client's many publics. The public relations professional must know how to effectively address those concerns using the most powerful tool of the public relations trade, which is publicity.

18.7 NOTES

18.8 SUMMARY

Sales promotion will also play an important role in the promotional mix of industrial marketing firms. Some of the methods used for sales promotion are trade shows, sales contests, promotional novelties and seminars. Sales promotion also helps the industry to promoting the products of the company in effective manner. Sales promotion not only promotes the company's product but also promote company brand image.

18.9 KEY WORDS

- **Sales Promotion**
- **Sales Contests**
- **Gift Item**
- **Samples**
- **Novelties**
- **Promotional letters**

18.10 SELFASSESSMENT QUESTIONS

1. What is sales promotion? Explain the objectives of sales promotion
2. Discuss the importance of sales promotion
3. Explain the techniques of sales promotion
4. Explain the concept of public relation

18.11 REFERENCES

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UNIT 19 :ADVERTISEMENT

Structure:

19.0 OBJECTIVES

After studying this unit, you should be able to;

- Define advertisement
- Explain the objectives of advertisement
- Discuss the uses of advertisement
- Examine the process of media selection

19.1 INTRODUCTION

As a per cent of sales, industrial product advertising is much smaller than consumer products advertising. An industrial product is bought by a very elaborate buying process affected by a member of variables. The advertising is thus very complicated. Most common objectives for industrial product advertising are to inform, to bring in orders, to stimulate queries, to enhance the market's name on the buyer's panel of sources. It also seems to influence the buying process in the purchasing organization that sales people cannot access.

Industrial advertising is prepared in the form of message inserted in trade journals and periodically in business magazines and newspapers. It also motivates the distributors and seeks to build up a corporate image. It reminds the final consumers about role the industrial market play in their lives by offering products, which a customer finally ends up using. For example, Intel advertisement, in the magazines talks about the advantages to the final customer. It is one of the success stories of component branding.

19.2 MEANING OF ADVERTISING

Advertising is an audio or visual form of marketing communication that employs an openly sponsored, non personal message to promote or sell a product, service or idea. Sponsors of advertising are often businesses who wish to promote their products or services. Advertising is differentiated from public relations in that an advertiser usually pays for and has control over the message. It is differentiated from personal selling in that the message is non personal, i.e., not directed to a particular individual. Advertising is communicated through various mass media, including old media such as newspapers, magazines, Television, Radio, outdoor advertising or direct mail; or new media such as search results, blogs, websites or text messages. The actual presentation of the message in a medium is referred to as an advertisement or "ad".

Commercial ads often seek to generate increased consumption of their products or services through "branding," which associates a product name or image with certain qualities in the minds of consumers. On the other hand, ads that intend to elicit an immediate sale are known as direct response advertising. Non-commercial advertisers who spend money to advertise items other than a consumer product or service include political parties, interest groups, religious organizations and governmental agencies. Non-profit organizations may use free modes of persuasion, such as a public service announcement. Advertising may also be used to reassure employees or shareholders that a company is viable or successful.

19.3 OBJECTIVES OFADVERTISING

The purpose of advertising is nothing but to sell something -a product, a service or an idea. The real objective of advertising is effective communication between producers and consumers. The following are the main objectives of advertising:

Preparing Ground for New Product

New product needs introduction because potential customers have never used such product earlier and the advertisement prepares a ground for that new product.

Creation of Demand

The main objective of the advertisement is to create a favorable climate for maintaining of improving sales. Customers are to be reminded about the product and the brand. It may induce new customers to buy the product by informing them its qualities since it is possible that some of the customers may change their brands.

Facing the Competition

Another important objective of the advertisement is to face to competition. Under competitive conditions, advertisement helps to build up brand image and brand loyalty and when customers have developed brand loyalty, becomes difficult for the middlemen to change it.

Creating or Enhancing Goodwill:

Large scale advertising is often undertaken with the objective of creating or enhancing the goodwill of the advertising company. This, in turn, increases the market receptiveness of the company's product and helps the salesmen to win customers easily.

Informing the Changes to the Customers

Whenever changes are made in the prices, channels of distribution or in the product by way of any improvement in quality, size, weight, brand, packing, etc., they must be informed to the public by the producer through advertisement.

Neutralizing Competitor's Advertising

Advertising is unavoidable to complete with or neutralize competitor's advertising. When competitors are adopting intensive advertising as their promotional strategy, it is reasonable to follow similar practices to neutralize their effects. In such cases, it is essential for the manufacturer to create a different image of his product.

Barring New Entrants

From the advertiser's point of view, a strongly built image through long advertising helps to keep new entrants away. The advertisement builds up a certain monopoly are for the product in which new entrants find it difficult to enter.

In short, advertising aims at benefiting the producer, educating the consumer and supplementing the salesmen. Above all it is a link between the producer and the consumer.

19.4 USES OFADVERTISING IN INDUSTRIALMARKETS

Advertising is one of the communication tools available to help an industrial organization achieve its marketing objectives. It is only one part of the communication mix; a firm can also communicate through the sales force, through publicity or public relation and through various trade promotions.

The following can be the uses of advertising in industrial markets,

Create awareness:

Since customer go through a series of buying processes they have many parameters to consider, advertising alone will not lead to a sale. But it can be used to create awareness among the customers so that at the time of considering alternative vendors, the consumers recall the advertisement.

At the time of release of a new product into the market, an awareness of its existence can be communicated through advertising.

Compliment to the distribution channel:

The use of advertising will also depend on the distribution channel selected. If sales force is employed then advertising paves the way for them by creating supplier preference. When the customers are aware of a company, its reputation, its product and its stature in the industry, sales people are more confident and hence more effective.

If wholesalers, retailers or other middlemen are employed, advertisements are released in agreement with the contact details of the middlemen.

Cheaper:

Within the communication mix advertising is a much cheaper way to reach large consumers, unlike the high cost of sales call. Unlike sales calls, advertising can use emotional devices to increase the personal awareness of the message, though advertising alone would actually not get the sales and has to be complimented.

Reach Buying Influence:

Many a times the industrial market is not aware of the influencers in the customer's firm. As it becomes necessary to reach them at the time of decision making advertisements can be a solution. The influencers after seeing the advertisement would contact the industrial firm for information, thus identifying themselves for later communication.

Customer retention or Royalty building:

For examples, Du Pont, the company that discovered nylon and Teflon which has varied application today, might advertise regularly on its new research. A new product must enhance customer relations.

It can provide a toll free number for them, so that they can be advised on how the product can enhance the customer's value.

19.5 MEDIA SELECTION

Media selection is the process of choosing the most cost-effective media for advertising, to achieve the required coverage and number of exposures in a target audience.

Television advertising

Television advertising offers the benefit of reaching large numbers in a single exposure. Yet because it is a mass medium capable of being seen by nearly anyone, television lacks the ability to deliver an advertisement to highly targeted customers compared to other media outlets. Television networks are attempting to improve their targeting efforts. In particular, networks operating in the pay-to-access arena, such as those with channels on cable and satellite television, are introducing more narrowly themed programming (i.e., TV shows geared to specific interest groups) designed to appeal to selective audiences. However, television remains an option that is best for products that targeted to a broad market.

The geographic scope of television advertising ranges from advertising within a localized geographic area using fee-based services, such as cable and fiber optic services, to national coverage using broadcast programming.

Television advertising, once viewed as the pillar of advertising media outlets, is facing numerous challenges from alternative media (e.g., Internet) and the invasion of technology devices, such as digital video recorders (see more in the Advertising Trends section in the Advertising) tutorial, that have empowered customers to be more selective on the advertisements they view. Additionally, television lacks effective response tracking which has led many marketers to investigate other media that offer stronger tracking options.

Radio advertising

Promotion through radio has been a viable advertising option for over 80 years. Radio advertising is mostly local to the broadcast range of a radio station, however, at least three options exist that offer national and potentially international coverage. First, in many countries there are radio networks that use many geographically distinct stations to broadcast simultaneously. In the United States such networks as Disney (children's programming) and ESPN (sports programming) broadcast nationally either through a group of company-owned stations or through a syndication arrangement (i.e., business agreement) with partner stations. Second, within the last few years the emergence of radio programming delivered via satellite has become an option for national advertising. Finally, the potential for national and international advertising may become more attractive as radio stations allow their signals to be broadcast over the Internet.

In many ways radio suffers the same problems as television, namely, a mass medium that is not highly targeted and offers little opportunity to track responses. But unlike television, radio presents the additional disadvantage of limiting advertisers to audio-only advertising. For some products advertising without visual support is not effective.

Print publications advertising

Print publications such as magazines, books, newspapers and Special Issue publications offer advertising opportunities at all geographic levels.

Magazines, especially those that target specific niche or specialized interest areas, are more narrowly targeted compared to broadcast media. Additionally, magazines offer the option of allowing marketers to present their message using high quality imagery (e.g., full color) and can also offer touch and scent experiences (e.g., perfume).

Newspapers have also incorporated color advertisements, though their main advantage rests with their ability to target local markets.

Special Issue publications can offer very selective targeting since these often focus on an extremely narrow topics (e.g., auto buying guide, tour guides, college and university ratings, etc.).

Internet advertising

The fastest growing media outlet for advertising is the Internet. Compared to spending in other media, the rate of spending for Internet advertising is experiencing tremendous growth and in the U.S. trails only newspaper and television advertising in terms of total spending. Internet advertising's influence continues to expand and each year more major marketers shift a larger portion of their promotional budget to this medium. Two key reasons for this shift rest with the Internet's ability to:

1) Narrowly target an advertising message and,

2) Track user response to the advertiser's message.

The Internet offers many advertising options with messages delivered through websites or by email.

Website Advertising- Advertising tied to a user's visit to a website accounts for the largest spending on Internet advertising. For marketers, website advertising offers many options in terms of:

Creative Types

Size

Placement

Delivery

Email Advertising – Using email to deliver an advertisement affords marketers the advantage of low distribution cost and potentially high reach. In situations where the marketer possesses a highly targeted list, response rates to email advertisements may be quite high. This is especially true if those on the list have agreed to receive email, a process known as "opt-in" marketing. Email advertisement can take the form of a regular email message or be presented within the context of more detailed content, such as an electronic newsletter. Delivery to a user's email address can be viewed as either plain text or can look more like a website using web coding (i.e., HTML). However, as most people are aware, there is significant downside to email advertising due to highly publicized issues related to abuse (i.e., spam).

Direct mail advertising

This method of advertising uses postal and other delivery services to ship advertising materials, including postcards, letters, brochures, catalogs and flyers, to a physical address of targeted customers. Direct mail is most effective when it is designed in a way that makes it appear to be special to the customer. For instance, a marketer using direct mail can personalize mailings by including a message recipient's name on the address label or by inserting their name within the content of marketer's message.

Direct mail can be a very cost-effective method of advertising, especially if mailings contain printed material. This is due to cost advantages obtained by printing in high volume since the majority of printing costs are realized when a printing machine is initially set up to run a print job and not the because of the quantity of material printed. Consequently, the total cost of printing 50,000 postcards is only slightly higher than printing 20,000 postcards but when the total cost is divided by the number of cards printed the cost per-card drops dramatically as more pieces are printed. Obviously there are other costs involved in direct mail, primarily postage expense.

While direct mail can be seen as offering the benefit of a low cost-per-contact, the actual cost-per-impression can be quite high as large numbers of customers may discard the mailing before reading. This has led many to refer to direct mail as "junk mail" and due to the name some marketers view the approach as ineffective. However, direct mail, when well-targeted, can be an extremely effective promotional tool.

Signage and billboard advertising

The use of signs to communicate a marketer's message places advertising in geographically identified areas in order to capture customer attention. The most obvious method of using signs is through billboards, which are generally located in high traffic areas. Outdoor billboards come in many sizes, though the most well-known are large structures located near transportation points intending to attract the interest of people traveling on roads or public transportation. Indoor billboards are often smaller than outdoor billboards and are designed to attract the attention of foot traffic (i.e., those moving past the sign). For example, smaller signage in airports, train terminals and large commercial office space fit this category.

While billboards are the most obvious example of signage advertising, there are many other forms of signage advertising include:

Sky writing where airplanes use special chemicals to form words Plane banners where large signs are pulled behind an airplane Mobile billboards where signs are placed on vehicles, such as buses and cars, or even carried by people Plastic bags used to protect newspapers delivered to homes Advertisements attached to grocery carts

Product placement advertising

Product placement is an advertising approach that intentionally inserts products into entertainment programs such as movies, TV programs and video games.

Placement can take several forms including:

Visual imagery in which the product appears within the entertainment program actual product use by an actor in the program words spoken by an actor that include the product name

Product placement is gaining acceptance among a growing number of marketers for two main reasons. First, in most cases the placement is subtle so as not to divert significant attention from the main content of the program or media outlet. This approach may lead the audience to believe the product was selected for inclusion by program producers and not by the marketer. This may heighten the credibility of the product in the minds of the audience since their perception, whether accurate or not, is that product was selected by an unbiased third-party.

Second, entertainment programming, such as television, is converging with other media, particularly the Internet. In the future a viewer of a television program may be able to easily request information for products that appear in a program by simply pointing to the product on the screen. With the information they may get the option to purchase the product. As this technology emerges it is expected that product placement opportunities will become a powerful promotional option for many marketers.

Mobile device advertising

Handheld devices, such as cellphones, smartphones, portable computers and other wireless devices, make up the growing mobile device market. Such devices allow customers to stay informed, gather information and communicate with others without being tied to a physical location. While the mobile device market is only beginning to become a viable advertising medium, it may soon offer significant opportunity for marketers to reach customers at any time and anywhere.

Also, with geographic positioning features included in newer mobile devices, the medium has the potential to provide marketers with the ability to target customers based on their geographic location. Currently, the most popular advertising delivery method to mobile devices is through plain text messaging, however, over the next few years multimedia advertisements are expected to become the dominant message format.

Sponsorship advertising

A subtle method of advertising is an approach in which marketers pay, or offer resources and services, for the purpose of being seen as a supporter of an organization's event, program or product offering (e.g., section of a website). Sponsorships are intended not to be viewed a blatant advertisement and in this way may be appealing for marketers looking to establish credibility with a particular target market. However, many sponsorship options lack the ability to tie spending directly to customer response. Additionally, the visibility of the sponsorship may be limited to relatively small mentions especially if the marketer is sharing sponsorship with many other organizations

19.6 NOTES

19.7 SUMMARY

Advertising is a communication between the buyer and the seller. It creates awareness about the product to the potential buyers. In case of changes or new products, it highlights the advantages of the product due to changes made. Some commonly used products can be dealt through magazines, newspaper and journals. Those, which are not commonly used, are advertised through mailing system to product buyers.

In planning for the advertising media 4Ws called Who, When, Where, What are important. This is essential to achieve the purpose. Different product requires different media. Now a days sending catalogues to selected clientele has became very common. Advertising needs money. Hence some portion is earmarked in the budget. The percentage depends upon the product, market share, competition and the product development.

19.8 KEY WORDS

- **Advertising**
- **Competition**
- **Media**

19.9 SELFASSESSMENT QUESTIONS

1. What is advertisement? Explain the objectives of advertisement
2. Discuss the concept of Media in Advertising
3. Explain the uses of Advertising
4. Discuss the process of media selection

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UNIT 20 : EVALUATION OF ADVERTISEMENT

Structure:

20.0 OBJECTIVES

After studying this unit, you should be able to;

- Explain the process of evaluation of Advertisement
- Discuss the Advertisement Techniques for Industrial Goods
- Bring out the concept of E-procurement
- Highlights the challenges of industrial Market.

20.1 EVALUATION OFADVERTISMENT

Good Planning and control of advertising depends greatly on measures of advertising effectiveness. To ensure that the advertising objectives are being achieved and the budget utilized efficiently, the effectiveness of the advertising programme needs to be evaluated.

Every plan needs to be evaluated to see if what it was started off for is achieved and advertising plan is no exception. The decisions that have been taken pertaining to the budget, media and message are analyzed. Determining effectiveness after it has been implemented is known as postulating. It is time consuming and costly. An alternative is preventing, where the effectiveness is measured before the ad is implemented. By pre-testing the plan, the ad agency/ industrial markets can identify ineffective elements so chosen and make alternations before the actual ad is released.

20.2 ADVERTISEMENT EVALUATION TECHNIQUES FOR INDUSTRIALGOODS

In today's advertising world, every firm invests heavily on advertisement for making their products or services known to the target audience and to arouse the interest of target audience in firm's products or services. Advertising is done with some predefined objectives- to generate awareness about product, to arouse interest in product, to change the attitude of audience towards product, to stimulate desire for product, or to make them buy the product.

Advertising is of no use if the defined objectives of communication are not achieved. So, it is necessary to evaluate the effectiveness of advertisement at different level, starting from creation of ad-copy to running of ad on media, and also after execution of ad to know to what extent the objectives are achieved.

Types of Test

Following are the types of test applied in advertisement evaluation:

- Pre-Testing
- Concurrent Testing

- Post Testing

1. Pre-Testing

Pre-Testing follows the universal law "Prevention is better than cure". Advertising can be pretested at several points in the creative development process. Pre-Testing helps the advertiser to make a final go or no go decision about finished or nearly finished advertisement. Pre-Testing method refer to testing the potentiality of a communication message or ad-copy before printing, broadcasting, or telecasting. Following are the types of pre-testing methods:

A. **Qualitative Methods of Pre-Testing**

- **Focus Group**: Focus group involves exposing the ad to a group of 8 to 12 respondents. Focus groups are used with surprising frequency for making final go or no go decision. A moderator facilitates the discussion and walk s the group through a series of issues that are outlined in discussion guide.
- **In-depth Interview**: In-depth interview involve one on one discussion with respondents. Interviews are very effective when a researcher has a good idea of critical issues but does not have a sense of the kind of responses one will get. This method can be effectively used to generate new ad concepts and ideas.
- **Projective Techniques**: In this technique the respondent is instructed to project himself into the situation and verbalize the thoughts. Projective technique can be very effective for evaluating ad concepts and for generating new ad concepts. But, it cannot be used for making final decisions.

B. **Quantitative Methods of Pre-Testing**

- **Checklist Method**: Checklist method is used to test the effectiveness of ad-copy. The purpose of this method is to ensure that all elements of the ad-copy are included with due importance in the advertisement. As it is a pre-test method any omitted element of ad can be included in the copy before release of the advertisement.
- **Consumer Jury Method** : This method involves the exposure of alternative advertisements to a sample of jury or prospects. This test is designed to learn from a typical group of prospective customers. Advertisements which are unpublished are presented before the consumer jury either in personal interviews or group interviews and their reactions are observed and responses are recorded.
- **Sales Area Test**: Under this method advertising campaign is run in the markets selected for testing purposes. The impact of the campaign is evaluated by actual sales in the selected markets. The market with high sales is considered the best market for effective sales campaign. In other markets suitable changes are made in the advertising campaign.

- **Questionnaire Method**: It is a list of questions related to an experiment. The draft of an advertisement along with some relevant questions is to be sent to a group of target consumers or advertising experts. Their opinions are collected and analyzed to find out whether the proposed advertisement is satisfactory or not.
- **Recall Test**: Under this method, advertising copies are shown to a group of prospects. After few minutes they are asked to recall and reproduce them. This method is used to find out how far the advertisements are impressive.
- **Reaction Test**: The potential effect of an advertisement is judged with the help of certain instruments, which measure heartbeats, blood pressure, pupil dilution etc. Their reactions reveal the psychological or nervous effects of advertising.
- **Readability Test**: All the listeners of advertisements cannot read it equally. So respondents are drawn from different socio economic and geographical backgrounds. This method is used to find out the level of effectiveness when and advertisement is read.
- **Eye Movement Test**: The movements of eyes of the respondents are recorded by using eye observation camera when advertisements are shown to them in a screen. This helps to find out the attention value of advertisement.

2. Concurrent Testing

Concurrent testing is evaluated throughout the whole advertisement execution process. Tests are conducted while audience is exposed to different type of media. Following are the types of concurrent testing methods:

- **Consumer Diaries**: Diaries are provided to selected customers. They are also informed to record the details of advertisements they watch, listen or read. The diaries are collected periodically. The result obtained from such a survey reveals the effectiveness of advertisement.
- **Co-incidental Surveys**: This method is also called as co-incidental telephone method. Under this method, samples of customers are selected and calls are made at the time of broadcast of the advertisement programme. The data obtained and analyzed will give a picture about the effectiveness of an advertisement.
- **Electronic Devices**: Now day's electronic devices are widely used to measure the effectiveness of an advertisement. They are mainly used in broadcast media. These are auto meters, track electronic units etc.

3. Post Testing

Post testing is done to know- to what extent the advertising objectives are achieved. Following are the types of post testing methods:

- **Recognition Test**: Recognition test involves the ability of viewers to correctly identify ad, brand, or message they previously exposed to. The types of recognition test are:
- **Starch Test** - The Starch test is applied only to print ads that have already run. The interviewer shows each respondent a magazine or newspaper containing the ads being tested. For each ad the interviewer asks the respondents to reply to ad related questions.
- **Bruzzone Test -** The Bruzzone test is conducted through mail surveys. Questionnaires containing frames and audio scripts from television commercials are sent to respondents and respondents are asked whether they recognize the ad and brand.
- **Recall or Impact Test**: The recall test is designed to measure the impression of readers or viewers of the advertisement. If a reader has a favorable impression of the advertisement, he will certainly retain something of the advertisement. The measures of interest would be obtained by interviewing the readers or viewers or listeners, days after the advertisement or commercial is appeared in the newspaper, or on T.V. Interviewer asks the readers or viewers to answer some ad related questions, and in response to the question asked, the reader reveals the accuracy and depth of his impression.

20.3 E-PROCUREMENT

E-procurement (**electronic procurement)**, sometimes also known as **supplier exchange**) is the business-to-business or business-to-consumer or business-to-government purchase and sale of supplies, work, and services through the Internet as well as other information and networking systems, such as electronic data interchange and enterprise resource planning.

The e-procurement value chain consists of indent management, e-Informing, e-Tendering, e-Auctioning, vendor management, catalogue management, Purchase Order Integration, Order Status, Ship Notice, e-invoicing, e-payment, and contract management. Indent management is the workflow involved in the preparation of tenders. This part of the value chain is optional, with individual procuring departments defining their indenting process. In works procurement, administrative approval and technical sanction are obtained in electronic format. In goods procurement, indent generation activity is done online. The end result of the stage is taken as inputs for issuing the NIT.

Elements of e-procurement include request for information, request for proposal, request for quotation, RFx (the previous three together), and eRFx (software for managing RFx projects).

Benefits of e-Procurement

- A virtual elimination of paperwork and paperwork handling.
- A reduction in the time between need recognition and the release and receipt of an order.
- Improved communication both within the company and with suppliers.
- A reduction in errors.
- Lower overhead costs in the purchasing area.
- Purchasing personnel spend less time on processing of purchase orders and invoices, and more time on strategic value-added purchasing activities.

E- Procurement is the counterpart to e sourcing, starting where e sourcing ends and ending where e sourcing begins. It is the e implementation of the procurement cycle which is concerned with the requisitioning, receiving and reconciliation of the received goods as opposed to the analysis, action and award that takes place in the sourcing cycle. It is essentially the automation of the non strategic and transactional activities that consume the majority of a buyer's time, but one that comes with increased enterprise level visibility of all purchases.

The basic procurement cycle consists of up to nine steps, depending on the complexity of the buy and organizational policies. At a bare minimum, it consists of an order, an invoice and payment. For high dollar purchase, the process will generally also include authorization and reconciliation of the invoice. In addition, if taxes were paid that the organization is capable of reclaiming, then the forms or entries to reclaim such taxes at the proper time will also be filled out or made. Finally,, in a leading procurement organization, every step will be completed, although may will be completed automatically for low dollar or non- strategic purchases by the e procurement system using defines rules in the workflow engine.

- **Requisition**

A buyer recognizes a need and places a request for goods or services.

- **Authorization**

Each requisition made by a buyer gets routed to an appropriate approval agent. The approver verifies that the goods or services are needed, that they are either off of an appropriate contract or acceptable as a stand-alone non-contract order, and that the purchase amount is acceptable.

- **Purchase Order**

  Once a requisition is approved, a purchase order is created and automatically delivered to the supplier(s).

- **Receipt of Goods**

  Once goods are received, the buyer issues or confirms a receipt of such goods to the supplier.

- **Invoice**

  After a supplier prepares goods for shipment, an invoice is created that denotes the individual goods ordered by SKU and the amounts being charged.

- **Reconciliation**

  After the goods are received, the invoice needs to be reconciled to the purchase order and goods receipt before payment is made. Are the charges for the right goods or services? Are the amounts the contracted amounts? Were the quantities correct? Are any other charges, including taxes, valid and correct?

- **Payment**

  Once the goods have been received and the invoice reconciled with the order and contract, payment is scheduled and made using an appropriate payment method, which could be p-card, electronic funds transfer, or good old fashioned cheque.

- **Reclamation of Taxes**

  In some situations, the supplier of a good or service will be obligated to charge a tax, but the buyer may be eligible to retain some or all of that tax because of its corporate status. Examples include European Value Added Tax, Canadian Goods and Services Tax, and out-of-state sales taxes.

- **Analysis**

  After a number of procurement cycles have been completed, it is important to take measurements of the efficiency and accuracy of the procurement process.

20.4 CHALLENGES OF INDUSTRIAL MARKET

The marketing of industrial products presents its own unique bunch of challenges. Maybe if you're marketing an industrial IT application you can throw in some pretty screen shots and invite customers and the press around to sit through a flashy Power Point presentation now and then. But, it doesn't work quite so well when you're trying to market the latest in air compressor technology or an industrial pump or valve or an obscure piece of laboratory equipment.

Key things to consider when marketing industrial products are:

- **Brand reinforcement**: As a marketer for these kinds of industrial applications or products, a lot of focus needs to be placed on reinforcing the brand name. Sounds simple – but a number of PR and marketing professionals go off on a tangent promoting this benefit or that feature and forget to focus on pushing the strongest feature an industrial product has – its brand name. When a widget breaks, the engineer doesn't go onto the internet and type in that he is looking for an a widget that does XYZ – he types in the brand name of the widget that's damaged and then tries to find who his closest local supplier of the same widget is. It's not particularly exciting from a marketer's point of view – but imperative if you want the brand to be found.

- **Think like an engineer**: If you're planning to sell to an engineer – then think like an engineer. If you're planning to sell to a quality assurance job title, then think like a QA person. It sounds obvious but as they say – to catch a criminal you have to think like one. Blanket PR coverage in any publication that might have an industrial slant isn't going to necessarily reach your audience. The PR agency might look good for a bit, showing you all their press clippings they've achieved but you also need to be realistic – online media ferociously consumes new content, so take a hard look at your return on this investment. If your keywords and brand name are coming up consistently well in search engines and you are getting referrals and website traffic, this means the strategy is paying off.

Branding industrial-type products takes a lot of time and specialized skills. It's not just a case of applying a standard PR model or branding model and hoping for the best. Even straightforward aspects such as article preparation can be tricky if the account manager can't articulate what the technology does and where it is utilised.

If your agency or marketing manager can put a well-presented case study in front of 20 of the right consumers, presented in a format and language that is easy to understand, you may find your return on investment is better than if it were simply blanket editorial in any publication which might consider using your article as a space filler.

Marketing industrial-type products invariably comes with a "dull" image, but the right team with the right understanding of your product and industry can provide a good return and make sure your product is always in the client's mind.

20.5 ROLE OF TECHNOLOGY IN INDUSTRIAL BUYING

The digitization of information, content and processes is transforming the technology buying process. A recent Bain & Company survey of the marketing, customer service and supply chain functions found that nearly one-third of technology purchasing power has moved to executives outside of IT. This has less to do with IT budgets being reallocated to the line of business than with non-IT business leaders transferring investments from labor and traditional services to new technology tools and technology-enabled services.

Traditionally, chief information officers (CIOs) have called the shots in IT purchasing decisions after aligning with the business on its needs. At times, technology spending has moved from IT to other parts of the organization—as it did in the 2000s when companies began building websites—but typically, the CIO and IT have regained control once the technology matures and cost pressures arise.

Digitization, however, is bringing a more permanent change to the IT buying process, one that will create a far more complex sales environment for technology providers. Whereas responsibility for managing and maintaining a website can shift, organizations transforming work processes through digitization must retain authority over those processes. While this shift in buying power presents new opportunities for technology providers, most are not set up to sell to these new buyers.

Changes in technology spending

The digitization of business is shifting enterprise-level investments in technology along two dimensions. First, investment is moving from traditional workflows, such as print ad targeting in marketing, to new digital workflows, such as mobile ad targeting and delivery. Investment is also being directed from within the enterprise to a new generation of third-party service providers. New business models, like pay-for-performance and as-a-service, will displace traditional models, such as perpetual software licenses.

These changes affect billions of investment dollars: The $1.5 trillion invested in marketing and communications worldwide in 2012 is expected to grow to $1.7 trillion by 2017. Of that roughly $200 billion in growth, two-thirds will come from new digitized workloads, such as digital advertising media buying systems that enable micro-segmentation and advanced customer analytics, according to our analysis and discussions with chief marketing officers in the US

20.6 NOTES

20.7 SUMMARY

Evaluation of advertising is crucial role of any industrial marketer to know the effectiveness of their advertisement. It is important to identify the role of advertisement in communicating the message to target audience about their objectives prescribed by the company.

20.8 KEY WORDS

- Evaluation
- E-procurement
- Technology

20.9 SELFASSESSMENT QUESTIONS

1. Explain the evaluation techniques of advertisement
2. Discuss the concept of evaluation of advertisement effectiveness
3. Examine the challenges of industrial market
4. Explain the role of technology in industrial buying process

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