# **UNIT – III**

# **Pricing: Introduction**

**Pricing** is the process whereby a business sets the price at which it will sell its products and services, and may be part of the business’s marketing plan. In setting prices, the business will take into account the price at which it could acquire the goods, the manufacturing cost, the market place, competition, market condition, brand, and quality of product.

**Pricing** is a fundamental aspect of financial modeling and is one of the four Ps of the marketing mix, the other three aspects being product, promotion, and place. Price is the only revenue generating element amongst the four Ps, the rest being cost centers. However, the other Ps of marketing will contribute to decreasing price elasticity and so enable price increases to drive greater revenue and profits.

**Pricing** can be a manual or automatic process of applying prices to purchase and sales orders, based on factors such as: a fixed amount, quantity break, promotion or sales campaign, specific vendor quote, price prevailing on entry, shipment or invoice date, combination of multiple orders or lines, and many others. Automated pricing systems require more setup and maintenance but may prevent pricing errors. The needs of the consumer can be converted into demand only if the consumer has the willingness and capacity to buy the product. Thus, pricing is the most important concept in the field of marketing, it is used as a tactical decision in response to comparing market situations.

### **Factors Affecting the Pricing Decisions**

Price is the only element of marketing mix that helps in generating income.

Therefore, a marketer should adopt a well-planned approach for pricing decisions.

The marketer should know the factors that influence the pricing decisions before setting the price of a product.



1. **Organizational Objectives**

Affect the pricing decisions to a great extent. The marketers should set the prices as per the organizational goals. For instance, an organization has set a goal to produce quality products, thus, the prices will be set according to the quality of products. Similarly, if the organization has a goal to increase sales by 18% every year, then the reasonable prices have to be set to increase the demand of the product.

1. **Legal and Regulatory Issues**

Persuade marketers to change price decisions. The legal and regulatory laws set prices on various products, such as insurance and dairy items. These laws may lead to the fixing, freezing, or controlling of prices at minimum or maximum levels.

1. **Competition**

Affects prices significantly. The organization matches the prices with the competitors and adjusts the prices more or less than the competitors. The organization also assesses that how the competitors respond to changes in the prices.

1. **Distribution Channels**

Implies a pathway through which the final products of manufacturers reach the end users. If the distribution channel is large, price of the product will be high and if the distribution channel is short, the price of the product will be low. Thus, these are the major factors that influence the pricing decisions.

1. **Competitor’s Pricing Policies**

Influence the pricing policies of the organizations. The price of a product should be determined in such a way that it should easily face price competition.

1. **Price Elasticity of Demand:**

Refers to change in demand of a product due to change in price.

There are three situations that arise under it:

* Products that have inelastic demand will be highly priced
* Products that have more than elastic demand will be priced low
* Products that have elastic demand will be reasonably priced.
1. **Pricing Objectives**

Help an organization in determining price decisions. For instance, an organization has a pricing objective to increase the market share through low pricing. Therefore, it needs to set the prices less than the competitor prices to gain the market share. Giving rebates and discounts on products is also a price objective that influences the customer’s decisions to buy a product.

1. **Product Characteristics**

Include the nature of the product, substitutes of the product, stage of life-cycle of the product, and product diversification.

1. **Costs**

Influence the price setting decisions of an organization. The organization may sell products at prices less than that of the competitors even if it is incurring high costs. By following this strategy, the organization can increase sales volumes in the short run but cannot survive in the long run. Thus, the marketers analyze the costs before setting the prices to minimize losses. Costs include cost of raw materials, selling and distribution overheads, cost of advertisement and sales promotion and office and administration overheads.

# **Pricing Process**

The different pricing process are discussed below;



### **Cost-based Pricing**

Cost-based pricing refers to a pricing method in which some percentage of desired profit margins is added to the cost of the product to obtain the final price. In other words, cost-based pricing can be defined as a pricing method in which a certain percentage of the total cost of production is added to the cost of the product to determine its selling price. Cost-based pricing can be of two types, namely, cost-plus pricing and markup pricing.

These two types of cost-based pricing are as follows:

**(i) Cost-Plus Pricing** - Refers to the simplest method of determining the price of a product. In cost-plus pricing method, a fixed percentage, also called mark-up percentage, of the total cost (as a profit) is added to the total cost to set the price. For example, XYZ organization bears the total cost of Rs. 100 per unit for producing a product. It adds Rs. 50 per unit to the price of product as’ profit. In such a case, the final price of a product of the organization would be Rs. 150.

Cost-plus pricing is also known as average cost pricing. This is the most commonly used method in manufacturing organizations.

In economics, the general formula given for setting price in case of cost-plus pricing is as follows:

P = AVC + AVC (M)

AVC= Average Variable Cost

M = Mark-up percentage

AVC (m) = Gross profit margin

Mark-up percentage (M) is fixed in which AFC and net profit margin (NPM) are covered.

AVC (m) = AFC+ NPM

For determining average variable cost, the first step is to fix prices. This is done by estimating the volume of the output for a given period of time. The planned output or normal level of production is taken into account to estimate the output.

The second step is to calculate Total Variable Cost (TVC) of the output. TVC includes direct costs, such as cost incurred in labor, electricity, and transportation. Once TVC is calculated, AVC is obtained by dividing TVC by output, Q. [AVC= TVC/Q]. The price is then fixed by adding the mark-up of some percentage of AVC to the profit [P = AVC + AVC (m)].

The advantages of cost-plus pricing method are as follows:

* Requires minimum information
* Involves simplicity of calculation
* Insures sellers against the unexpected changes in costs

The disadvantages of cost-plus pricing method are as follows:-

* Ignores price strategies of competitors
* Ignores the role of customers

### **(II) Markup Pricing -** Refers to a pricing method in which the fixed amount or the percentage of cost of the product is added to product’s price to get the selling price of the product. Markup pricing is more common in retailing in which a retailer sells the product to earn profit. For example, if a retailer has taken a product from the wholesaler for Rs. 100, then he/she might add up a markup of Rs. 20 to gain profit.

It is mostly expressed by the following formulae:

Markup as the percentage of cost= (Markup/Cost) \*100

Markup as the percentage of selling price= (Markup/ Selling Price)\*100

For example, the product is sold for Rs. 500 whose cost was Rs. 400. The mark up as a percentage to cost is equal to (100/400)\*100 =25. The mark up as a percentage of the selling price equals (100/500)\*100= 20.

### **2. Demand-Based Pricing**

Demand-based pricing refers to a pricing method in which the price of a product is finalized according to its demand. If the demand of a product is more, an organization prefers to set high prices for products to gain profit; whereas, if the demand of a product is less, the low prices are charged to attract the customers.

The success of demand-based pricing depends on the ability of marketers to analyze the demand. This type of pricing can be seen in the hospitality and travel industries. For instance, airlines during the period of low demand charge less rates as compared to the period of high demand. Demand-based pricing helps the organization to earn more profit if the customers accept the product at the price more than its cost.

### **3. Competition-based Pricing**

Competition-based pricing refers to a method in which an organization considers the prices of competitors’ products to set the prices of its own products. The organization may charge higher, lower, or equal prices as compared to the prices of its competitors.

The aviation industry is the best example of competition-based pricing where airlines charge the same or fewer prices for same routes as charged by their competitors. In addition, the introductory prices charged by publishing organizations for textbooks are determined according to the competitors’ prices.

### **4. Other Pricing Methods**

In addition to the pricing methods, there are other methods that are discussed as follows:

**(i) Value Pricing** - Implies a method in which an organization tries to win loyal customers by charging low prices for their high- quality products. The organization aims to become a low cost producer without sacrificing the quality. It can deliver high- quality products at low prices by improving its research and development process. Value pricing is also called value-optimized pricing.

**(ii) Target Return Pricing** - Helps in achieving the required rate of return on investment done for a product. In other words, the price of a product is fixed on the basis of expected profit.

**(iii) Going Rate Pricing** - Implies a method in which an organization sets the price of a product according to the prevailing price trends in the market. Thus, the pricing strategy adopted by the organization can be same or similar to other organizations. However, in this type of pricing, the prices set by the market leaders are followed by all the organizations in the industry.

**(iv) Transfer Pricing** - Involves selling of goods and services within the departments of the organization. It is done to manage the profit and loss ratios of different departments within the organization. One department of an organization can sell its products to other departments at low prices. Sometimes, transfer pricing is used to show higher profits in the organization by showing fake sales of products within departments.

# **Pricing Strategies**

A business can use a variety of pricing strategies when selling a product or service. The price can be set to maximize profitability for each unit sold or from the market overall. It can be used to defend an existing market from new entrants, to increase market share within a market or to enter a new market.



1. **Penetration Pricing**

The price charged for products and services is set artificially low in order to gain market share. Once this is achieved, the price is increased. This approach was used by France Telecom and Sky TV. These companies need to land grab large numbers of consumers to make it worth their while, so they offer free telephones or satellite dishes at discounted rates in order to get people to sign up for their services. Once there is a large number of subscribers prices gradually creep up. Taking Sky TV for example, or any cable or satellite company, when there is a premium movie or sporting event prices are at their highest – so they move from a penetration approach to more of a skimming/premium pricing approach.

1. **Skimming Pricing**

Price skimming sees a company charge a higher price because it has a substantial competitive advantage. However, the advantage tends not to be sustainable. The high price attracts new competitors into the market, and the price inevitably falls due to increased supply.

Manufacturers of digital watches used a skimming approach in the 1970s. Once other manufacturers were tempted into the market and the watches were produced at a lower unit cost, other marketing strategies and pricing approaches are implemented. New products were developed and the market for watches gained a reputation for innovation.

1. **Competition Pricing**

Competitive pricing consists of setting the price at the same level as one’s competitors. This method relies on the idea that competitors have already thoroughly worked on their pricing. In any market, many firms sell the same or very similar products, and according to classical economics, the price for these products should, in theory, already be at an equilibrium (or at least at a local equilibrium). Therefore, by setting the same price as its competitors, a newly-launched firm can avoid the trial and error costs of the price-setting process. However, every company is different and so are its costs. Considering this, the main limit of the competitive pricing method is that it fails to account for the differences in costs (production, purchasing, sales force, etc.) of individual companies. As a result, this pricing method can potentially be inefficient and lead to reduced profits.

For example, a firm needs to price a new coffee maker. The firm’s competitors sell it at $25, and the company considers that the best price for the new coffee maker is $25. It decides to set this very price on their own product. Moreover, this pricing method can also be used in combination with other methods such as penetration pricing for example, which consists of setting the price below that of its competition (for instance, in this example, setting the price of the coffee maker at $23).

1. **Product Line Pricing**

Where there is a range of products or services the pricing reflects the benefits of parts of the range. For example car washes; a basic wash could be $2, a wash and wax $4 and the whole package for $6. Product line pricing seldom reflects the cost of making the product since it delivers a range of prices that a consumer perceives as being fair incrementally – over the range.

If you buy chocolate bars or potato chips (crisps) you expect to pay X for a single packet, although if you buy a family pack which is 5 times bigger, you expect to pay less than 5X the price. The cost of making and distributing large family packs of chocolate/chips could be far more expensive. It might benefit the manufacturer to sell them singly in terms of profit margin, although they price over the whole line. Profit is made on the range rather than single items.

1. **Psychological Pricing**

This approach is used when the marketer wants the consumer to respond on an emotional, rather than rational basis. For example Price Point Perspective (PPP) 0.99 Cents not 1 US Dollar. It’s strange how consumers use price as an indicator of all sorts of factors, especially when they are in unfamiliar markets. Consumers might practice a decision avoidance approach when buying products in an unfamiliar setting, an example being when buying ice cream. What would you like, an ice cream at $0.75, $1.25 or $2.00? The choice is yours. Maybe you’re entering an entirely new market. Let’s say that you’re buying a lawnmower for the first time and know nothing about garden equipment. Would you automatically by the cheapest? Would you buy the most expensive? Or, would you go for a lawnmower somewhere in the middle? Price therefore may be an indication of quality or benefits in unfamiliar markets.

1. **Cost Plus Pricing**

Your company has been developing a new printer that will streamline many processes for your small business customers. Your job is to determine the price of the printer. After doing some research, you determine that the best method for pricing the printer is the cost-plus method.

Cost-plus pricing is a straightforward and simple way to arrive at a sales price by adding a markup to the cost of a product. In our example of the printer, you first have to determine the break-even price, which is the sum of all of the expenses involved in creating a product, including expenses like supplies, production costs, and marketing costs. When you pull all of the expenses together to determine the cost of each printer, you determine that each one will cost $78 to produce. If you sold the printer at $78 your company would break even, meaning there would be no profit or loss.

1. **Cost-based Pricing**

Cost-based pricing involves setting prices based on the costs for producing, distributing and selling the product. Also, the company normally adds a fair rate of return to compensate for its efforts and risks. To begin with, let’s look at some famous examples of companies using cost-based pricing. Firms such as Ryanair and Walmart work to become the low-cost producers in their industries. By constantly reducing costs wherever possible, these companies are able to set lower prices. Certainly, that leads to smaller margins, but greater sales and profits on the other hand. But even companies with higher prices may rely on cost-based pricing. However, these companies usually intentionally generate higher costs so that they can claim higher prices and margins.

1. **Optional Product Pricing**

Companies will attempt to increase the amount customers spend once they start to buy. Optional ‘extras’ increase the overall price of the product or service. For example airlines will charge for optional extras such as guaranteeing a window seat or reserving a row of seats next to each other. Again budget airlines are prime users of this approach when they charge you extra for additional luggage or extra legroom.

1. **Premium Pricing**

Use a high price where there is a unique brand. This approach is used where a substantial competitive advantage exists and the marketer is safe in the knowledge that they can charge a relatively higher price. Such high prices are charged for luxuries such as Cunard Cruises, Savoy Hotel rooms, and first class air travel.

1. **Bundle Pricing**

The act of placing several products or services together in a single package and selling for a lower price than would be charged if the items were sold separately. The package usually includes one big ticket product and at least one complementary good. Bundled pricing is a marketing method used by retailers to sell products in high supply.

**Initiating and Responding To Price Changes**

Internal or external forces often lead an organization to change its prices. Price changes are often initiated by the organization. The organization also has to design its strategy to deal with price changes initiated by competitors.

**INITIATING PRICE CHANGES**

An organization may initiate price changes to deal with new forces arising within the organization or the market. The price change may occur at both directions: increasing price or lowering prices.

**(i) Increasing Price**

Increasing price of a product is an attractive proposition for every business organization, since a small increase in the price results in huge increase in the revenue and profits. If an organization feels that the sales volume will not be affected by a small price increase, it may always be tempted to increase the price.

Most price rise are the results of inflation that causes the organization’s costs to increase. Costs often increase when the government introduces new taxes or raises the current tax rates. Increase in the price of any factors of production – wage levels, raw materials prices and interest rates – cause the price to increase. Often, organizations anticipate such increases and may raise the price of its products in advance.

Sometimes, an organization may increase the price in order to reduce the demand for the product. When an organization cannot increase the supply of its over demanded product, it may raise the price level to manage the demand at the current supply point.

**(ii) Lowering Price**

Several situations lead an organization to reduce the price of its products. Organizations with excess capacity try for extra sales in order to achieve higher capacity utilization rates. In such a situation, it may find lowering price the most easy method of achieving higher sales volume.

Some organizations often lower the price to achieve higher sales volume, and thereby capture larger market share. These organizations believe that once they are to dominate the market and hold to a large market share, the resulting sales volume may allow it to achieve economies of scale.

Lowering price is very risky strategy. It usually invites sharp reactions from competitors and often results into a price war. Care less prices cuts may lead an organization into the following traps:

* **Low quality trap:** An organization initiating price cuts may fall in a low quality trap when consumers associate the new low prices to a poorer quality product.
* **Fragile market trap:** It may fall into a fragile market trap when price sensitive consumers wait for further price cuts or search for cheaper products.
* **Shallow pocket trap:** It may fall into the shallow pocket trap if financially strong organizations react by huge price cuts to counter the price cuts initiated by a weak organization.

### **RESPONDING TO PRICE CHANGES**

An organization faces a strategic decision situation when competitors initiate price changes. Responding to the price change, particularly in the case of price cuts is a difficult question. The organization has to consider the objective and time frame of the price change. The following clues are important in responding to price changes:

If the price cut has been initiated in order to use excess capacity or to cover rising costs, it does not warrant any response.

* If the price change is temporary or short term, initiated to clear old stocks, there is no need for response.
* If the objective is to dominate the market and the price change is long term, the organization has to respond quickly and effectively.
* The organization should also evaluate the consequences of non response to the price change.
* If the price change does not seriously affect it current sales and market share, there is no need for response.
* Before showing any response, it should carefully watch how other competitors react to the price change.

 Responding to a competitor’s price change is also influenced by the status of the organization in the market. Small follower firms are forced to follow the price changes initiated by a large organization that forced to follow the price changes initiated by a large organization that performs the role of the price leader. The price leader normally establishes the market price that is adopted by several price follower firms.

Sometimes, the price leader is also troubled by smaller firms through severe price cuts. In such a situation, the price leader has the options of response or non response. The leader organization may not respond if it does not expect to lose any significant portion of its market share.

If the price cut is expected to seriously hurt the market share and profit situation, the leader organization may take one or more of the strategic options:

**Option 1:** Increase customers perceived value of the product by increasing promotional level.

**Option 2:** Increase the price complemented by an improvement in quality and features of the product. This requires a re-positioning strategy to establish the brand at a higher price position.

**Option 3:** Add a new lower price brand to the current product line and position it directly with the attacker’s brand. This trading down strategy helps the organization to maintain high quality image for the old brand.

**Option 4:** As a last option, reduce the price to off set the negative effects of the price attack.



# **Distribution Management**

 **Distribution management** refers to the process of overseeing the movement of goods from supplier or manufacturer to point of sale. It is an overarching term that refers to numerous activities and processes such as packaging, inventory, warehousing, supply chain, and logistics.

**Distribution management** is an important part of the business cycle for distributors and wholesalers. The profit margins of businesses depend on how quickly they can turnover their goods. The more they sell, the more they earn, which means a better future for the business. Having a successful distribution management system is also important for businesses to remain competitive and to keep customers satisfied.

Distribution management is critical to a company’s financial success and corporate longevity. Executing it successfully requires effective management of the entire distribution process. The larger a corporation, or the greater the number of supply points a company has, the more it will need to rely on automation to effectively manage the distribution process.

**Modern distribution management** encompasses more than just moving products from point A to point B. It also involves gathering and sharing relevant information that can be used to identify key opportunities for growth and competitiveness in the market. Most progressive companies now use their distribution forces to obtain market intelligence which are vital in assessing their competitive position.

There are basically two types of distribution: commercial distribution—commonly known as sales distribution—and physical distribution—better known as logistics. Distribution involves diverse functions such as customer service, shipping, warehousing, inventory control, private trucking-fleet operations, packaging, receiving, materials handling, along with plant, warehouse, store location planning, and the integration of information.

The goal is to achieve ultimate efficiency in delivering raw materials and parts, both partially and completely finished products to the right place and time in the proper condition. Physical distribution planning should align with overall channel strategy.



### **Advantages of a Distribution Management Strategy**

**(i)** Aside from keeping profits up, there are many reasons a company may want to use a distribution management strategy. First, it keeps things organized. If there was no proper management system in place, retailers would be forced to hold stock in their own locations—a bad idea, especially if the seller lacks proper storage space.

**(ii)** A distribution management system also makes things easier for the consumer. It allows them to visit one location for a variety of different products. If the system didn’t exist, consumers would have to visit multiple locations just to get what they need.

**(iii)** Putting a proper distribution management system in place also alleviates any potential for errors in delivery, as well as the times products need to be delivered.

Effective distribution management involves selling your product while assuring sufficient stocks in channels while managing promotions in those channels and their varying requirements. It also involves making sure a supply chain is efficient enough that distribution costs are low enough to allow a product to be sold at the right price, thus supporting your marketing strategy and maximizing profit.

# **Needs for Marketing Channels**

**Marketing channels** are channels used by any company to reach their end customers. These channels are generally interdependent on each other and interact with each other so as to ensure that the product reaches from the company to the end customer.

Marketing Channels can be defined as the set of people, activities, and the intermediary organizations that play a crucial role in transferring the ownership of the goods from the point of production or manufacturing to the point of consumption. Basically, they are the various channels or platforms through which the products reach to the consumers or the end-users. They are also known as the distribution channels.

### **Needs for Marketing Channels:**

1. **Information Provider**

The first and foremost aspect in the list of the importance of the Marketing Channels is that the middlemen such as agents provide the vital and crucial market information to the manufacturer that helps him to plan his production and other related business strategies accordingly. Developments in the market such as the change in the preferences in the taste of the consumer, entry of new manufactures in the market, shift in the government policies, and the various pricing points of the other manufacturers are given to the manufacturer without any additional cost owing to their relationship and working association with the manufacturer.

1. **Stability of the Price**

Yet another important function that is performed by the middlemen is that they maintain the stability of price by absorbing the increment along with keeping the overheads cost low and charge the consumers with the old price of the products. Their main motive behind this strategy is to have a strong foothold in the market due to the completion from the other middlemen in the market.

1. **Promotion**

Another aspect in the importance of Marketing Channels is that the middlemen perform the function of promoting the goods of the manufacturer by planning and designing their own sales incentive and customer loyalty programs to attain their sales targets and increased market share objectives. This ultimately works for the benefit of the manufacturer and all the parties involved in the process.

1. **Pricing Strategy**

As the middlemen and the agents are at the sales field on a daily basis and have a thorough knowledge about the marketing dynamics and the customer preferences, many manufacturers ask for their suggestion whilst deciding on the pricing of the various products. The pricing and the features of the products are also customized for the different set of target markets and consumers along with the channel of distribution.

1. **Matching the Demand and Supply of the Products**

The main and significant function of the middlemen and commission agents in the Marketing Channels is to match the demand and supply of the products in the target market. They should provide the manufacturers with the crucial information on how to assemble the goods to match the taste and preferences of the targeted consumers that result in the ease of sales and attainment of the sales objectives of the manufacturer.

1. **Financing**

Middlemen finance manufacturers’ operation by providing the necessary working capital in the form of advance payments for goods and services. The payment is in advance even though the manufacturer may extend credit, because it has to be made even before the products are bought, consumed and paid for by the ultimate consumer.

1. **Title**

Most middlemen take the title to the goods, services and trade in their own name. This helps in diffusing the risks between the manufacturer and middlemen. This also enables middlemen to be in physical possession of the goods, which in turn enables them to meet customer demand at very moment it arises.

1. **Help in Production Function**

The producer can concentrate on the production function leaving the marketing problem to middlemen who specialize in the profession. Their services can best utilized for selling the product. The finance, required for organizing marketing can profitably be used in production where the rate of return would be greater.

1. **Standardizing Transactions**

Standardizing transactions is another function of marketing channels. Taking the example of the milk delivery system, the distribution is standardized throughout the marketing channel so that consumers do not need to negotiate with the sellers on any aspect, whether it is price, quantity, method of payment or location of the product.

By standardizing transactions, marketing channels automate most of the stages in the flow of products from the manufacturer to the customers.

1. **Matching Buyers and Sellers**

The most crucial activity of the marketing channel members is to match the needs of buyers and sellers. Normally, most sellers do not know where they can reach potential buyers and similarly, buyers do not know where they can reach potential sellers. From this perspective, the role of the marketing channel to match the buyers’ and sellers’ needs becomes very vital. For example, a painter of modern art may not know where he can reach his potential customers, but an art dealer would surely know.

In case of the large manufacturers of the products, the manufacturers require the well aligned and properly planned Marketing Channels so that the products reach to the end users in a convenient and effortless manner

# **Decisions Involved in Setting up the Channel**

**Choosing a distribution channel** is a pivotal decision for your business. What you choose determines how your products are handled and the speed in which they are delivered.

Among the several factors that affect your decision are the following:

* **Type of product.** If your product is perishable or is unstable, you will need it much faster and need to use a direct distribution method.
* M**arket** If your market is consumers, retailers are an essential distribution method whereas business markets may need another approach that you’ll need to identify.
* **Middlemen** Depending on your needs and the demands on your time, a middleman can help distribute products quickly and efficiently. This is something that’s worth checking out and is usually determined by your budget.

### **Following Decisions Involved in Setting up the Channel:**

1. **A Step-by-Step Process**

Many people, erroneously consider their marketing campaign before deciding upon their distribution plan. This is a mistake. Marketing comes after you’ve made the decision about your distribution channel because marketing is the strategy you use to reach your distribution channel. And, much of your wholesale business depends heavily on which method you select as a way to reach your customers.

For example, if you decide to use a sales force as your primary means of reaching people, then much of your focus will be on training your sales force to position your product (or service) effectively. You’ll need to hire staff, coach them, and equip them with key messages. On the other hand, if you choose to reach people through direct mail, then you’ll focus heavily on obtaining reliable contact lists and setting up and staffing call-centers.

1. **Consider Your Competitors**

You need to ask yourself what methods your competitors are using, and, more importantly, why. Ask yourself if there is a qualitative advantage over other channels, or is it simply the way the industry has always operated? Perhaps there is a distribution channel that your competitors have overlooked. In which case, you’ll gain an edge by taking advantage of it. For example, if your competitors are mainly distributing product via big-box retailers, taking advantage of direct sales through the internet can give you a unique angle.

1. **Examine Costs and Benefits**

After deciding on a method of distribution, creating all the support systems that go along with it is time-consuming and expensive. First, you need to orientate your entire company in a certain direction, and once that’s done it’ll be difficult to reverse your decision. Also, the actual act of building an infrastructure to support a selected distribution channel is expensive and time-consuming. It’s best to carefully weigh the costs and benefits associated with each and every one of your options before committing resources to it.

1. **Rank Your Options**

After examining the different methods available to you, rank them by order of preference according to what will net you the most amount of revenue at the end of the year. You may find that you’ll begin by pursuing one distribution channel and find that that doesn’t preclude you from adding additional channels as you acquire more capital. You may even find that some methods are complementary to each other and that synergy will make you more productive and efficient.

The most important thing you can do is carefully consider your options and not just select a direction because it’s the industry standard or most convenient avenue for your business. If you question the reason behind your decision at the onset, you may discover an overlooked advantage or drawback.

# **Channel Management Strategies**

**Channel management** involves creating operational strategies that go beyond a single organization. Channel management strategies bring together partners in a supply chain, including material suppliers, manufacturers, distributors and resellers, in an effort to lower costs and increase operational efficiency throughout the chain.

### **Following Channel Management Strategies are:**

1. **Strategic Partnerships**

Developing long-term relationships with your suppliers and retail customers is the first step toward effective channel management. Rather than switching suppliers for price discounts and promotional offers, build a solid supplier base by entering into price/volume contracts, cooperative marketing arrangements, inter-company financing arrangements or other activities designed to strengthen your relationships. Develop a loyal reseller base by helping your resellers to market and sell your product effectively. Provide credit arrangements to loyal retail customers, and offer price/volume contracts to your customers as well.

1. **Technology Leveraging**

Technological tools can be used to increase efficiency along a supply chain, but dedication and cooperation is required of all parties. Automatic order systems can instantly place orders along the supply chain when stock levels reach economic quantities. Picking, packing and shipping activities can be tied into automatic order systems to further improve efficiency and decrease delivery lead times. Order tracking technology can help individual companies to provide better customer service by knowing exactly when materials and other orders will arrive.

1. **Vertical Integration**

Vertical integration is the act of purchasing or building your own suppliers or customers. This technique can be costly and sophisticated compared to others, but vertical integration can provide the most significant cost savings and quality control of all channel management options. Owning your own supplier or retail customer can allow you to set your own prices along the supply chain and exercise total control over operational procedures and quality standards.

1. **Logistical Support**

Acting as a consultant to your suppliers and resellers may be one of the most hands-off channel management techniques, but it can still improve efficiency and productivity across the supply chain. Sharing best practices, technological innovations and managerial expertise can help your strategic partners to get their houses in order, resulting in lower prices and higher quality from suppliers, as well as more reliable orders from resellers. Providing marketing materials and sales training to resellers’ employees can help to boost sales for your brands as well.

1. **Monitoring**

Continually monitor and assess the performance and progress of your supply chain. Create thorough monitoring systems to accompany each channel management technique, whether it be something as simple as employee and customer surveys or something as complex as statistical reports from a chain-wide automatic order system. Reassess your supply chain strategies regularly and adjust them to respond to changes in the market or in a particular link in the chain.

### **Logistics Management**

Logistics management consists of the process of planning, implementing and controlling the efficient flow of raw-materials, work-in-progress and finished goods and related information-from point of origin to point of consumption; with a view to providing satisfaction to the customer.

According to Phillip Kotler, “Market logistics involve planning, implementing and controlling physical flow of material and final (finished) goods from the point of origin to the point of use to meet customer requirements, at a profit.”

### **Classification of Logistical Activities**



### **(i) Inbound Logistics**

Inbound logistics is concerned with the smooth and cost effective inflow of materials and other inputs (that are needed in the manufacturing process) from suppliers to the plant. For proper management of inbound logistics, the management has to maintain a continuous interface with suppliers (vendors).

### **(ii) Outbound Logistics**

Outbound logistics (also called physical distribution management or supply chain management); is concerned with the flow of finished goods and other related information from the firm to the customer. For proper management of outbound logistics, the management has to maintain a continuous interface with transport operators and channels of distribution.

### **Significance (or Objectives) of Logistics Management**

### **(i) Cost Reduction and Profit Maximization**

Logistics management results in cost reduction and profit maximization, primarily due to-

* Improved material handling
* Safe, speedy and economical transportation
* Optimum number and convenient location of warehouses etc.

### **(ii) Efficient Flow of Manufacturing Operations**

Inbound logistics helps in the efficient flow of manufacturing operations, due to on-time delivery of materials, proper utilization of materials and semi-finished goods in the production process and so on.

**(iii) Competitive Edge**

Logistics provide, maintain and sharpen the competitive edge of an enterprise by-

* Increasing sales through providing better customer service
* Arranging for rapid and reliable delivery
* Avoiding errors in order processing; and so on.

**(iv) Effective Communication System**

An efficient information system is a must for sound logistics management. As such, logistics management helps in developing effective communication system for continuous interface with suppliers and rapid response to customer enquiries.

**(v) Sound Inventory Management**

Sound inventory management is a by-product of logistics management. A major headache of production management, financial management etc. is how to ensure sound inventory management; which headache is cured by logistics management.

### **Key Activities Involved in Logistics Management**

**(i) Network Design**

Network design is one of the prime responsibilities of logistics management. This network is required to determine the number and location of manufacturing plants, warehouses, material handling equipment’s etc. on which logistical efficiency depends.

**(ii) Order Processing**

Customers’ orders are very important in logistics management. Order processing includes activities for receiving, handling, filing, recording of orders. Herein, management has to ensure that order processing is accurate, reliable and fast.

Further, management has to minimize the time between receipt of orders and date of dispatch of the consignment to ensure speedy processing of the order. Delays in execution of orders can become serious grounds for customer dissatisfaction; which must be avoided at all costs.

**(iii) Procurement**

It is related to obtaining materials from outside suppliers. It includes supply sourcing, negotiation, order placement, inbound transportation, receiving and inspection, storage and handling etc. Its main objective is to support manufacturing, by providing timely supplies of qualitative materials, at the lowest possible cost.

**(iv) Material Handling**

It involves the activities of handling raw-materials, parts, semi-finished and finished goods into and out of plant, warehouses and transportation terminals. Management has to ensure that the raw-materials, parts, semi-finished and finished goods are handled properly to minimize losses due to breakage, spoilage etc. Further, the management has to minimize the handling costs and the time involved in material handling.

Material handling systems, in logistics management are divided into three categories:

* Mechanized systems
* Semi-automated systems
* Automated systems

**(v) Inventory Management**

The basic objective of inventory management is to minimize the amount of working capital blocked in inventories; and at the same time to provide a continuous flow of materials to match production requirements; and to provide timely supplies of goods to meet customers’ demands.

Management has to maintain inventories of:

* Raw-materials and parts
* Semi-finished goods
* Finished goods

Management has to balance the benefits of holding inventories against costs associated with holding inventories like – storage space costs, insurance costs, risk of damage and spoilage in keeping stocks etc.

**(vi) Packaging and Labeling**

Packaging and labeling are an important aspect of logistics management. Packaging implies enclosing or encasing a product into suitable packets or containers, for easy and convenient handling of the product by both, the seller and specially the buyer.

Packaging facilities the sale of a product. It acts as a silent salesman. For example, a fancy and decorative packaging of sweets, biscuits etc. on the eve of Diwali, makes for a good sale of such items.

Labeling means putting identification marks on the package of the product. A label provides information about – date of packing and expiry, weight or size of product, ingredients used in the manufacture of the product, instructions for sale handling of the product, price payable by the buyer etc.

Labeling is a strong sales promotion tool. The consumer who is persuaded to read the label may, in fact, try to buy the product; even though he/she had no such premeditation (advance idea).

**(vii) Warehousing**

Storage or warehousing is that logistical activity which creates time utility by storing goods from the time of production till the time these are needed by ultimate consumers.

Here, the management has to decide about-

* The number and type of warehouses needed and
* The location of warehouses.

The above two decisions depend on the desired level of customer service and the distance between the supply source and final destination i.e. markets.

**(viii) Transportation**

Transportation is that logistical activity which creates place utility.

Transportation is needed for:

* Movement of raw-materials from suppliers to the manufacturing unit.
* Movement of work-in-progress within the plant.
* Movement of finished goods from plant to the final consumers.

Major transportation systems include:-

* Railways
* Roadways
* Airways
* Waterways

The choice of a particular mode of transportation is dependent on a balancing of following considerations:

* Speed of transportation system
* Cost involved in transportation
* Safety in transportation
* Reliability of transportation time schedules
* Number of locations served etc.

# **Retailing**

**Retailing** is a distribution process, in which all the activities involved in selling the merchandise directly to the final consumer (i.e. the one who intends to use the product) are included. It encompasses sale of goods and services from a point of purchase to the end user, who is going to use that product.

Any business entity which sells goods to the end user and not for business use or for resale, whether it is a manufacturer, wholesaler or retailer, are said to be engaged in the process of retailing, irrespective of the manner in which goods are sold.

**Retailer** implies any organization, whose maximum part of revenue comes from retailing. In the supply chain, retailers are the final link between the manufacturers and ultimate consumer.

### **Types of Retailing**

**(i) Store Retailing**

Department store is the best form of store retailing, to attract a number of customers. The other types of store retailing includes, speciality store, supermarket, convenience store, catalogue showroom, drug store, super store, discount store, extreme value store. Different competitive and pricing strategy is adopted by different store retailers.

**(ii) Non-Store Retailing**

It is evident from the name itself, that when the selling of merchandise takes place outside the conventional shops or stores, it is termed as non-store retailing. It is classified as under:

* **Direct Marketing:** In this process, consumer direct channels are employed by the company to reach and deliver products to the customers. It includes direct mail marketing, catalog marketing, telemarketing, online shopping etc.
* **Direct Selling:** Otherwise called as multilevel selling and network selling, that involves door to door selling or at home sales parties. Here, in this process the sales person of the company visit the home of the host, who has invited acquaintances, the sales person demonstrate the products and take orders.
* **Automatic Vending:** Vending machines are primarily found in offices, factories, gasoline stations, large retail stores, restaurants etc. which offer a variety of products including impulse goods such as coffee, candy, newspaper, soft drinks etc.
* **Buying Service:** The retail organization serves a number of clients collectively, such as employees of an organization, who are authorized to purchase goods from specific retailers that have contracted to give discount, in exchange for membership.

**(iii) Corporate Retailing**

It includes retail organizations such as corporate chain store, franchises, retailer and consumer cooperatives and merchandising conglomerates. There are a number of advantages that these organizations can achieve jointly, such as economies of scale, better and qualified employees, wider brand recognition, etc.

With the emergence of new forms of retailing, competition is also increasing between them. It is one of the fast-growing and challenging industry.

# **Wholesaling**

**Wholesaling** is the sale and distribution of goods to specific customer types such as those most commonly referred to as resellers. Resellers are traditionally retailers, other wholesalers or merchants who will resell the good to an end user. Certain industrial, commercial and institutional customers also qualify, as the goods are often a component of a different end product.

Wholesaling often occurs when large quantities of merchandise are purchased, referred to as purchasing in bulk, with the intent of reassembling, sorting, repackaging or distributing the goods in smaller lots. Due to the volume of the purchase, the price of the goods is often lower than the price offered to retail consumers. A wholesaler can also be a business that acts as a middleman, brokering deals between businesses that produce certain components that are not intended for immediate sale on the open market.

###  **Types of Wholesalers**

1. **Merchant Wholesalers**

These are the most common type of wholesalers used in the FMCG industry, agriculture industry or Private label industry. Quite simply, Merchant wholesalers are the ones who buy directly from the manufacturer, store the product and then sell it to the customer. They might sell in any channel and they are not restricted to selling to retail only or to online only.

If there is any loss between the buying and selling of the product, it must be borne by the merchant wholesaler.

**Example –** A vegetable wholesaler buys produce directly from the farm and stocks it at his own warehouse. He then sells these products to the local retail outlets or even to end customers. He may also sell to restaurants. However, any loss of the produce due to spillage or any other reason is a cost to the merchant wholesalers.

Even in FMCG, companies like Britannia or P&G use merchant wholesalers. These wholesalers have a greater control in the region they operate. They benefit because they buy in bulk from the company and take charge of the risk they are facing. Plus, they are responsible for the sales targets, however, they achieve it.

1. **Full-Service Wholesalers**

They are most commonly observed in Consumer Durables or Engineering products. The full-service type of wholesalers is, as the name suggests, giving full service to the end retailer. These wholesalers mainly operate in the retail market and sell products to a reseller (a retailer in this case) everything except service of the product is the responsibility of the full-service wholesaler.

**Example –** Samsung wants to expand its operation in region A but it does not have a sales office in that region. So it appoints a distributor in region A. This distributor is solely responsible for order picking, delivery, training sales associates, promotions and everything for the Samsung brand. He is now a full-service wholesaler. However, for service of the product, there is a different service franchise opened in the same region.

In real life scenario, Many full-service wholesalers also start a second services related business and start giving services for the products they are wholesaling. Example – A Samsung wholesaler also starting a service center of Samsung.

As a result, they might get both – sales and service orders. However, for theoretical purposes, Servicing and maintenance of the product is not a part of a full-service wholesaler. He is mainly for sales, deliveries, and financing. These are the second most common types of wholesalers in the market.

1. **Limited Service Wholesalers**

A limited service wholesaler is someone who stocks the products of the company and sells it in a limited channel. He does not have a large turnover or does not cover all channels of the company.

**Example –** Company X wants to sell its products online but it knows that if it allows local distributors to sell online, there will be a huge price war. As a result, Company X appoints an exclusive online wholesaler. This online wholesaler has only one job – To purchase the product and stock it and sell it online. So whenever an order comes from Amazon or eBay, this wholesaler gives the machine to Amazon or eBay. That’s his only job.

The same way – there are other limited-service wholesalers. 2 are mentioned below.

* Cash and Carry wholesalers: Strong FMCG products are sold as cash and carry. Immediate payment is demanded on a delivery of material.
* Logistics wholesalers: A milk wholesaler who delivers whole trucks of milk across the market. His only work is to deliver the milk and not to get orders for the company.
1. **Brokers and Agents**

Most commonly observed in the real estate industry or in the chemical markets. A broker assumes no risk. He has the producer or the manufacturer on one side and he has the buyer on the other side. The work of the broker is to get the deal done and he gets a commission on the deal.

**Example –** A small lab has regular requirement of litmus paper. There is a litmus paper wholesaler in their area who is a broker for several companies and who arranges any lab material in bulk. The lab approaches the broker and wants to purchase huge quantity. The broker then talks to multiple manufacturers and finally, a deal is struck with one manufacturer. The manufacturer pays 2% commission to the broker for his work and for bringing the enquiry. Similarly, this broker can pick an order of Beakers, Petri dishes or any other equipment. He will keep arranging meetings with the right supplier and keep earning commissions.

A similar example like above is also observed in the retail industry wherein the broker earns a commission to sell an apartment.

The difference between a broker and agent is that a Broker is short-term and he will be there for a couple of orders. However, an Agent is long-term and specialized in repeated purchase so that he stays for a longer time with the company and specifically works for the betterment of the company. Example – Insurance has Agents (repeated buying) whereas real estate has brokers (single buying).

1. **Branches and Mini Offices**

Although branches and mini offices do not come in the various types of wholesalers, these are common ways for companies to start selling their products in a region they are targeting. A branch can also be called a type of wholesaling wherein the branch directly picks the orders from the end customers in bulk and ensures the supply and reorders from the customer.

**Example –** Paper Company like B2B or 3M knows that large companies require a lot of print paper across the month. These companies then establish branch offices which also act as the sales office. They pick a bulk order of paper and the company might transport the complete order from their warehouse to the company.

1. **Specialized Wholesalers**

These are wholesalers who do wholesale of specialized items only. Example – A used car wholesaler who sells directly to customers or to other used car dealers. He is specialized in used cars and knows the ins and outs of selling a used car to consumers or refurbishing the used cars.

Similarly, there are other specialized wholesalers who are known for the specific product that they sell.

The above were the various types of wholesalers in the market. As E-commerce rises in sales, there is a lesser requirement of Wholesalers in developing economies. However, emerging markets still use various types of wholesalers to their advantage.

# **Multi-Channel Marketing**

**Multichannel marketing** refers to the practice by which companies interact with customers via multiple channels, both direct and indirect, in order to sell them goods and services. Companies use direct channels, or ones in which the company proactively reaches the customer – such as physical stores, catalogs or direct mail – or indirect ones in which they push content via websites or social media, also known as inbound marketing. Other means of reaching customers with multichannel marketing include via **mobile devices, text messaging, email, company website, social media, search engine optimization (SEO) or GPS to track customers’ proximity to goods and services.** Multichannel marketing combines the practices of inbound and outbound marketing with the goal of reaching customers on the channel of their choice. In this way, the buying process is more controlled by the customer than the marketer.

**Multichannel marketing** is based on the fact that customers have more choices than ever in terms of getting information on products. The spread of available channels, including the growth of email, social media and mobile, has caused marketing departments to increase their presence on these channels in order to **develop their customer relationship management (CRM) efforts**. The old ways of marketing, such as using print sources, telemarketing or broadcasting on radio and TV are no longer the sole focus of marketing departments. These methods are still present, but are part of a bigger strategy that includes new media and evolve along with changing customer tastes and communication preferences.

Companies strive to develop analytics in order to determine which customers get which messages based on their demographic information and other behaviors. Beyond knowing who the customer is and what he/she wants, companies try to understand which channel a particular customer prefers to maximize the visibility of their messages. This enables companies to target the right audience with the right content to facilitate sales.

To have success in multichannel marketing, or any other digital marketing, efforts, companies aim to devise campaigns that span multiple channels easily. Since expecting customers to adapt to the company’s preferred channel is an unrealistic hope, companies cater to the customer and tailor campaigns to fit multiple channels. Another goal of companies is to know which campaigns on which channels lead to the most sales, enabling them to determine the effectiveness of their efforts and measuring the return on investment of their presence on each respective channel.



Companies can coordinate their online and offline marketing efforts in order to optimize both. For example, keyword testing from online marketing can inform the effectiveness of certain campaigns before they are made into print ads or other advertisements.

### **Main benefits of multichannel marketing include:**

* **Management of sales through feedback:** By maximizing marketing efforts through promoting a message through as many channels as possible, companies have the potential to collect feedback from different customer segments. Overall performance can be determined through this feedback and improvements can be made by crowdsourcing information. By ensuring that resources are being used effectively and efficiently, operational costs decrease.
* **More sales:** The more visible a message is the more potential customers a company can attract. By concentrating efforts on a single channel, the potential to reach the most prospective customers is diminished. Companies can use their presences on various channels to mold a personalized image that can build a customer following and boost retention and loyalty.
* **Achieving a 360-degree view of the customer:** When companies collect feedback from customers, they can better understand what is expected by their customer bases and how to improve product and service offerings. Companies can then augment marketing efforts and identify which channels work best for certain customer segments and strategize to cater to the needs of that group of customers.

Companies struggle to centralize goals and figure out things like measuring the message’s reach or frequency when devising multichannel strategies. Difficulties stem from the inability to coordinate the message across all departments and brands to make sure it is consistent on each channel. Due to a lack of common technology to satisfy every channel, staff and IT support is another pain point in developing multichannel campaigns. General challenges companies struggle with in developing overall CRM, such as getting a single repository for customer data, is also a hindrance to multichannel marketing.

### **VERTICAL MARKETING SYSTEM**

**A Vertical Marketing System (VMS)** comprises of the main distribution channel partners- the producer, the wholesaler and the retailer who work together as a unified group to serve the customer needs.

In conventional marketing system, the producer, wholesaler and the retailer worked separately with the intention to maximize their profits even at the expense of one another. This led to the unending conflicts between the channel partners resulting in less profits for the business as a whole.

In order to overcome these conflicts, several firms have started using a vertical marketing system wherein producers, wholesalers and retailers have joined hands with each other and are working in unison towards the accomplishment of the business objective as a whole. This has led to the increased profits for each involved in the channel of distribution.

Vertical Marketing System is further divided into three parts which are explained below:



**(i) Corporate Vertical Marketing System:** In Corporate VMS, one member of the distribution channel be it a producer, a wholesaler or a retailer Owns all the other Members of the Channel, thereby having all the elements of production and distribution channel under a single ownership. For example,: Amway is an American cosmetic company, which manufactures its own product range and sell these products only through its authorized Amway stores. Here the ownership of production and distribution is with the company itself.

**(ii) Contractual Vertical Marketing System:** In Contractual VMS, every member in the distribution channel works independently and integrate their activities on a Contractual Basis to earn more profits that are earned when working in isolation. The most common form of Contractual VMS is franchising. In franchising, the producer authorizes the distributor to sell its product under the producer’s name against some annual license fee. For example, Mc-Donalds, Dominos, Pizza Hut, etc. are all forms of the franchise which are working on a contractual basis.

**(iii) Administered Vertical Marketing System:** Under Administered VMS, there is no contract between the members of production & distribution channel but their activities do get influenced by the Size and Power of any one of the member. In simple words, any powerful and influential member of the channel dominate the activities of other channel members. For example, Big brands like HUL, ITC, Procter& Gamble, etc. command a high level of cooperation from the retailers in terms of display, shelf space, pricing policies, and promotional schemes.

Thus, through a vertical marketing system, the channel partners establishes a close contact with each other and work in unison towards the accomplishment of common objectives thereby enjoying more profits which they would have been earning when working alone.

### **HORIZONTAL MARKETING SYSTEM**

**A Horizontal Marketing system (HMS)** is a form of distribution channel wherein two or more companies at the same level unrelated to each other come together to gain the economies of scale.

In other words, Horizontal marketing system is the merger of two unrelated companies who have come together to exploit the market opportunities.

Generally, this type of marketing system is followed by companies who lack in capital, human resources, production techniques, marketing programs and are afraid of incurring the huge losses. In order to overcome these limitations, the companies join hands with other companies who are big in size either in the form of joint venture –that can be temporary or permanent, or mergers to sustain in the business.

Horizontal marketing system has gained popularity in the recent times due to an immense competition in the market where everybody is striving to gain a good position in the market along with huge profits.



In this marketing system, the collaboration can be between:

* **Two or more Manufacturers:** With an objective of making optimum utilization of scarce resources.
* **Two or more Wholesalers:** With the objective of covering a larger area of the distribution of goods and services.
* **Two or more Retailers:** With the objective of providing bulk quantities in a particular area.

**Examples of Horizontal Marketing**

Nike and Apple have entered into a partnership, with the intent to have a Nike+ footwear in which the iPod can be connected with these shoes that will play music along with the display of information about time, distance covered, calories burned and heart pace on the screen.

Johnson & Johnson, a health care company, have joined hands with Google, with an objective of having a robotic-assisted surgical platform. That will help in the integration of advanced technologies, thereby improving the healthcare services.

Thus, two or more companies join hands to capitalize on the expertise of each and capture a greater market share.